

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

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2016  
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 001-11001



**FRONTIER COMMUNICATIONS CORPORATION**  
(Exact name of registrant as specified in its charter)

<u>Delaware</u> (State or other jurisdiction of incorporation or organization)	<u>06-0619596</u> (I.R.S. Employer Identification No.)
<u>401 Merritt 7</u> <u>Norwalk, Connecticut</u> (Address of principal executive offices)	<u>06851</u> (Zip Code)

Registrant's telephone number, including area code: (203) 614-5600

**Securities registered pursuant to Section 12(b) of the Act:**

Title of each class	Name of each exchange on which registered
<u>Common Stock, par value \$0.25 per share</u>	<u>The NASDAQ Stock Market LLC</u>
<u>Series A Participating Preferred Stock Purchase Rights</u>	<u>The NASDAQ Stock Market LLC</u>

**Securities registered pursuant to Section 12(g) of the Act: NONE**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes  No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer  Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

The aggregate market value of common stock held by non-affiliates of the registrant on June 30, 2016 was \$5,764,318,000 based on the closing price of \$4.94 per share on such date. The number of shares outstanding of the registrant's common stock as of February 10, 2017 was 1,172,525,000.

**DOCUMENT INCORPORATED BY REFERENCE**

Portions of the Proxy Statement for Frontier's 2017 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-K.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

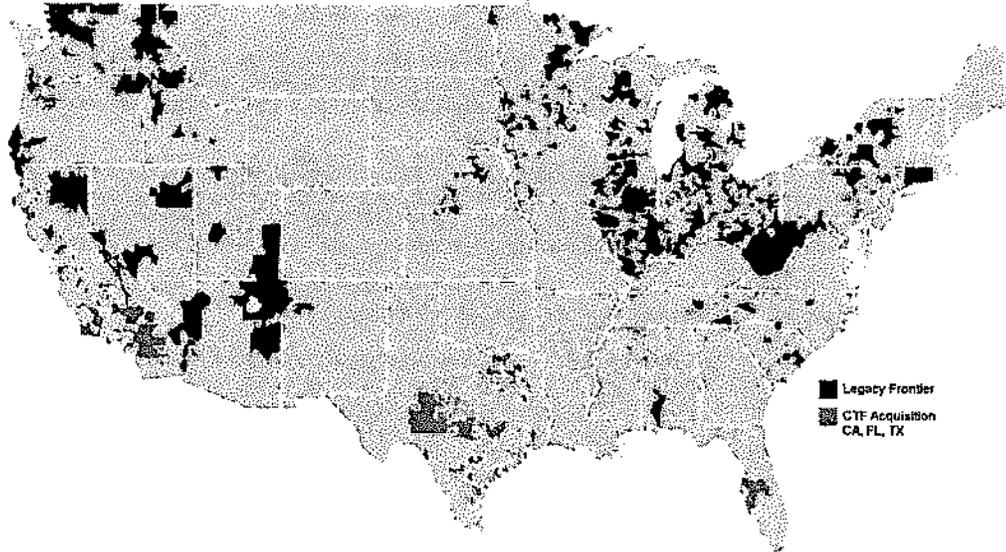
TABLE OF CONTENTS

	<u>Page No.</u>
<u>PART I</u>	
Item 1. <u>Business</u>	2
Item 1A. <u>Risk Factors</u>	12
Item 1B. <u>Unresolved Staff Comments</u>	22
Item 2. <u>Properties</u>	22
Item 3. <u>Legal Proceedings</u>	22
Item 4. <u>Mine Safety Disclosures</u>	22
<u>PART II</u>	
Item 5. <u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	23
Item 6. <u>Selected Financial Data</u>	26
Item 7. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	27
Item 7A. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	48
Item 8. <u>Financial Statements and Supplementary Data</u>	48
Item 9. <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	49
Item 9A. <u>Controls and Procedures</u>	49
Item 9B. <u>Other Information</u>	49
<u>PART III</u>	
Item 10. <u>Directors, Executive Officers and Corporate Governance</u>	50
Item 11. <u>Executive Compensation</u>	51
Item 12. <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	51
Item 13. <u>Certain Relationships and Related Transactions, and Director Independence</u>	51
Item 14. <u>Principal Accountant Fees and Services</u>	51
<u>PART IV</u>	
Item 15. <u>Exhibits and Financial Statement Schedules</u>	52
<u>Signatures</u>	56
<u>Index to Consolidated Financial Statements</u>	F-1

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

PART I**Item 1. Business**

Frontier Communications Corporation (Frontier) is a provider of communications services in the United States, with approximately 5.4 million customers, 4.3 million broadband subscribers and 28,300 employees, operating in 29 states. In recent years, Frontier has completed multiple acquisitions. On April 1, 2016, we acquired the wireline operations of Verizon Communications, Inc. in California, Texas and Florida for a purchase price of \$10,540 million in cash and assumed debt.

**Frontier's Service Territories****How We Serve Our Customers**

We conduct business with both residential and business customers.

*Residential.* We provide broadband, video, voice and other services and products to our residential customers. We deliver these services generally over a combination of fiber and copper based networks.

*Business (commercial customers and wholesale carrier customers).*

*Commercial.* We sometimes refer to our commercial customers as SME (small business, medium business and larger enterprise) customers. We provide a broad range of services to our SME customers, including broadband service, Ethernet service, traditional circuit-based services (TDM services) and voice services. We also sell customer premise equipment (CPE) and provide CPE-related maintenance services.

- *Larger Enterprise:* Fortune 1000, multi-location companies, large government entities, large educational institutions, and non-profits.
- *Medium Business:* Single or multi-location companies and mid-sized government entities, educational institutions and non-profits.
- *Small Business:* Mostly single-location businesses, the smaller of which have purchase patterns similar to residential customers.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

*Carrier.* Carrier customers are often referred to as wholesale customers and include national operators such as AT&T and Verizon, Local Exchange Companies that need to access locations within Frontier's footprint, Competitive Local Exchange Companies (CLECs) and wireless carriers. Carrier customers buy both voice and data services.

**Services and Products**

We offer a broad portfolio of communications services for residential and business customers. These services are offered on either a standalone basis or in a bundled package, depending on each customer's needs.

*Data and Internet services.* We offer a comprehensive range of broadband services. The principal residential service we provide is broadband internet service. Commercial services include Ethernet, Dedicated Internet, Multiprotocol Label Switching (MPLS), Time Division Multiplexing (TDM) data transport services and optical transport services. These services are all supported by 24/7 technical support and an advanced network operations center. We also offer wireless broadband services (using unlicensed spectrum) in select markets utilizing networks that we own or operate. In addition, we offer our Frontier Secure suite of products, including computer security, cloud backup and sharing, identity protection and equipment insurance.

*Video services.* We offer video services under the Vantage brand to certain of our customers in portions of Connecticut, South Carolina, Minnesota, and Illinois and under the FiOS® brand in portions of California, Texas, Florida, Indiana, Oregon and Washington. We also offer satellite TV video service to our customers under an agency relationship with DISH® in all of our markets.

*Voice services.* We provide voice services, including data-based VoIP, long distance and voice messaging services, to residential and business customers in our markets. These services are billed monthly in advance. Long distance service to and from points outside our operating properties are provided by interconnection with the facilities of interexchange carriers. Our long distance services are billed in advance for unlimited use service and on a per minute-of-use basis for a fixed number of minutes.

We also offer packages of communications services. These packages permit customers to bundle their products and services, including voice service, video and Internet services, and other product offerings.

*Access services.* We offer a range of access services. Our switched access services allow other carriers to use our facilities to originate and terminate their local and long distance voice traffic. These services are generally offered on a month-to-month basis and the service is billed primarily on a minutes-of-use basis. Switched access charges have been based on access rates filed with the FCC for interstate services and with the respective state regulatory agency for intrastate services. Intercarrier compensation reform has impacted the rates that we may charge for these services. See, "Regulatory Environment" below. Other access services we offer, such as special access, allow other carriers to have a continuous, non-switched connection to customers within our service territory.

*Customer Premise Equipment.* We offer our SME customers third-party communications equipment tailored to their specific business needs by partnering with Mitel, Airbus, Avaya, Hewlett Packard, Adtran and other equipment manufacturers. CPE is typically sold in conjunction with voice, data and Internet services, and may also be sold on a standalone basis.

**Frontier Operating Strategies**

*Grow Broadband and Invest in our Network.* A main component of our strategy is to enable and strengthen the broadband capabilities of our network. We focus on broadband as the core growth component of our service offering, either bundled with our voice and/or video services, or on a standalone basis. We continuously improve our broadband speeds and availability in our markets and view these investments as opportunities to attract and retain a greater number of customers and increase average revenue per residential and business customer. Our capital expenditures include enhancing the existing outside plant by expanding fiber-based infrastructure throughout our network, upgrading network hardware, expanding transport capacity of our middle-mile and data backbone, and growing our video capabilities. We continue to deploy next generation Broadband Remote Access Servers throughout our network to facilitate the expansion of broadband and video service offerings and increase broadband speeds. Similarly, for our commercial customers we are focused on expanding and upgrading our premium Ethernet service offerings across our network.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Improve Customer Experience and Retention.** We provide multiple service and product options in our residential and business offerings to the customer base in each of our markets. We believe this strategy results in a better customer experience and allows us to maximize retention of existing customers and to attract new customers. At December 31, 2016, 63% of our residential broadband customers subscribed to at least one other service offering. Our bundled services include broadband, voice, and video offerings, including simplified messaging services, higher speed products and digital security products. In late 2016, we announced a new organization structure, including separate and specialized consumer and commercial operations which will focus on the differing needs of these customer groups.

**Improve Productivity and Operational Efficiency.** We continuously engage in productivity initiatives with a focus on simplifying our processes, eliminating redundancies and further reducing our cost structure while improving our customer service capabilities. We have achieved significant day one cost savings in the wireline acquisition in California, Texas and Florida in 2016. There are substantial operational cost take-out opportunities that we are aggressively pursuing across all of our properties.

#### Network Architecture and Technology

Our local exchange carrier networks consist of host central office and remote sites, primarily equipped with digital and Internet Protocol switches. The outside plant consists of transport and distribution delivery networks connecting our host central office with remote central offices and ultimately with our customers. We own fiber optic and copper cable, which have been deployed in our networks and are the primary transport technologies between our host and remote central offices and interconnection points with other incumbent carriers.

We have expanded and enhanced our fiber optic and copper transport systems to support increasing customer demand for high bandwidth transport services. We routinely enhance our network and upgraded with the latest Internet Protocol Transport and routing equipment, Reconfigurable Optical Add/Drop Multiplexers (ROADM) transport systems, Very High Bit-Rate Digital Subscriber Line (VDSL) broadband equipment, and VoIP switches. These systems will support advanced services such as Ethernet, Dedicated Internet, Multiprotocol Label Switching (MPLS) transport, and VoIP. The network is designed with redundancy and auto-failover capability on our major circuits.

We connect to the households and business locations in our service territory using a combination of fiber optic and copper technologies. In some cases we provide direct fiber into a residence or a business premises. In other cases a location is served with a hybrid combination of fiber and copper. Residences in our service territory are served by fiber-to-the-home (FTTH) and by fiber-to-the-node (FTTN), meaning fiber carries the traffic to an intermediate location where the signals are converted to copper wire for the final delivery to the household. We provide data, video, and voice services to the customer over both of these architectures.

As of December 31, 2016, our broadband availability to the households throughout Frontier's territories is as follows:

<u>(Downstream speed capability)</u>	Number of Households (in millions)	% of Households with capability
Up to 10 Mbps	13.4	88%
10 Mbps and above	8.9	58%
25 Mbps and above	6.0	39%
50 Mbps and above	4.5	29%
100 Mbps and above	3.8	24%
No broadband capability	1.8	12%
Total Households	15.2	

In certain markets, we have begun to offer residential broadband services with 1 gigabit download speed capabilities.

Rapid and significant changes in technology are occurring in the communications industry. Our success will depend, in part, on our ability to anticipate and adapt to technological changes. We believe that our existing network

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

architecture strategy will enable us to respond to these ongoing technological changes efficiently. In addition, we anticipate reducing costs through the sharing of best practices across operations, centralization or standardization of functions and processes, and deployment of technologies and systems that provide for greater efficiencies and profitability. We will continue to make strategic enhancements to our network, with a focus on higher return investments.

**Competitive Positioning**

Competition for residential customers comes from cable operators, wireless carriers and online video providers, among others.

- *Cable operators:* in a majority of our markets, cable operators offer high speed Internet, video and voice services than we do and compete with us aggressively on speed and price by marketing their offerings with significant promotional period pricing.
- *Wireless carriers:* primarily compete with us for broadband, video, and voice services in our markets by offering increasingly larger data packages to mobile customers. The percentage of homes with a landline telephone has been declining, a trend we expect will continue.
- *Online video providers:* many consumers are opting for internet-delivered video services (Over the Top, or OTT) through providers such as Netflix, Hulu, Amazon, YouTube and DirectTV Now rather than traditional, multi-channel video. In response, we have made investments in our network to deliver OTT video content to consumers who might not opt for traditional video services.

Many residential customers prefer to bundle their voice, data and Internet and video services with a single provider. In areas where we do not directly offer a network based video service, we offer satellite TV video service through DISH. This can impact acquisition of new customers and retention of existing customers, representing a critical factor for the attachment of video, broadband and voice products. As of December 31, 2016 34% of our residential customers subscribed to at least two service offerings, and 19% subscribed to at least three service offerings.

Competition for business customers comes from telecommunications providers, cable operators, CLECs and other enterprises, some of which are substantially larger than us. As compared to our residential customers, these customers often require more sophisticated and more data-centered solutions (e.g., IP PBX, E911 networks, Ethernet, SIP trunking).

In order to remain competitive, we must continue to evolve our product offerings to remain current with the changing needs of the market, to provide strong customer service and support, to invest in our network so we maintain adequate capacity and can deliver new capabilities as needed, and to package our offerings to make them attractive to customers.

**Regulatory Environment**

Some of our operations are subject to regulation by the FCC and various state regulatory agencies, often called public service or utility commissions. We expect federal and state lawmakers, the FCC and the state regulatory agencies to continue to revise the statutes and regulations governing communications services.

**Regulation of our business**

We are subject to federal, state and local regulation and we have various regulatory authorizations for our regulated service offerings. At the federal level, the FCC generally exercises jurisdiction over information services; interstate or international telecommunications services and over facilities to the extent they are used to provide, originate or terminate interstate or international services. State regulatory commissions generally exercise jurisdiction over intrastate telecommunications services and the facilities used to provide, originate or terminate those services. Most of our local exchange companies operate as incumbent carriers in the states in which they operate and are certified in those states to provide local telecommunications services. In addition, local governments often regulate the public rights-of-way necessary to install and operate networks, and may require service providers to obtain licenses or franchises regulating their use of public rights-of-way. Municipalities and other local government agencies also may regulate other limited aspects of our business, by requiring us to obtain cable franchises and construction permits and to abide by applicable building codes.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Some states regulatory agencies have substantial oversight over incumbent telephone companies, and their interconnection with competitive providers and provision of non-discriminatory network access to certain network elements to them. Under the Federal Telecommunications Act of 1996, state regulatory commissions have jurisdiction to arbitrate and review interconnection disputes and agreements between incumbent telephone companies and competitive local exchange carriers, in accordance with rules set by the FCC. The FCC and state regulatory commissions also impose fees on providers of telecommunications services to support state universal service programs. Many of the states in which we operate require prior approvals or notifications for certain acquisitions and transfers of assets, customers, or ownership of regulated entities.

In addition, in some states we are subject to operating restrictions and minimum service quality standards (the failure to meet such restrictions may result in penalties). We also are required to report certain financial information. At the federal level and in a number of the states in which we operate, we are subject to price cap or incentive regulation plans under which prices for regulated services are capped. Some of these plans have limited terms and, as they expire, we may need to renegotiate with various states. These negotiations could impact rates, service quality and/or infrastructure requirements, which could also impact our earnings and capital expenditures. In other states in which we operate, we are subject to rate of return regulation that limits levels of earnings and returns on investments. Approximately 19% of our total access lines at December 31, 2016 are in state jurisdictions under the rate of return regulatory model. We will continue to advocate for no or reduced regulation with various regulatory agencies in those states. In some of our states, we have already been successful in reducing or eliminating price regulation on end-user services.

**Federal Regulatory Environment**

Frontier, along with all telecommunications providers, is subject to FCC rules governing privacy of specified customer information. Among other things, these rules obligate carriers to implement procedures to: protect specified customer information from inappropriate disclosure; obtain customer permission to use specified information in marketing; authenticate customers before disclosing account information; and annually certify compliance with the FCC's rules. Although most of these regulations are generally consistent with our business plans, they may restrict our flexibility in operating our business.

Some regulations are, or could in the future be, the subject of judicial proceedings, legislative hearings and administrative proposals or challenges that could change the manner in which the entire industry operates. Neither the outcome of any of these developments, nor their potential impact on us, can be predicted at this time. Regulation can change rapidly in the communications industry, and such changes may have an adverse effect on us.

The current status of material regulatory initiatives is as follows:

*Federal High-Cost Subsidies:* The FCC has adopted rules changing the eligibility requirements for federal subsidies offered to wireline carriers providing service to high-cost, low-density markets, as well as the amounts of such subsidies, as follows:

*Connect America Fund (CAF):* On November 18, 2011, the FCC adopted the Universal Service Fund (USF)/Intercarrier Compensation (ICC) Report and Order (the 2011 Order), which changed how federal subsidies are calculated and disbursed, and began the transition of Federal USF (Universal Service Fund), which supported voice services in high-cost areas, to the CAF, which supports broadband deployment in high-cost areas. Frontier received \$133 million from 2012 through 2014 across two rounds of CAF Phase I funding to make broadband available to approximately 194,600 previously unserved or underserved households. We completed deployment of broadband service to the first round of CAF Phase I households in 2015 as required by the FCC rules and will complete the second round of CAF Phase I build by the March 2017 deadline.

On April 29, 2015, the FCC released offers of support to price cap carriers under the CAF Phase II program. The intent of these offers is to provide long-term support for carriers for establishing and providing broadband service with at least 10 Mbps downstream/1 Mbps upstream speeds in high cost unserved or underserved areas. Frontier accepted the CAF Phase II offer in 29 states, including our CTF properties, which provides for \$332 million in annual support, through 2020 and a commitment to make broadband available to approximately 774,000 households. CAF Phase II support is a successor to the approximately \$156 million in annual USF frozen high cost support that Frontier had been receiving prior to the CTF acquisition, and the \$42 million in annual transitional USF frozen high cost support that Verizon had been receiving in California and Texas. In addition to the annual support levels, these amounts also include frozen support phasedown amounts in states where the annual CAF II funding is

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

less than the prior annual frozen high cost support funding. The frozen support phasedown support was \$35 million in 2015 and \$27 million in 2016, and is expected to be \$17 million in 2017 and \$6 million in 2018.

In 2017, the FCC is expected to adopt a competitive bidding process to continue to distribute CAF Phase II funding in those high-cost areas where price cap carriers declined the FCC's offer of support, possibly presenting a new support and deployment opportunity. The FCC's competitive bidding process has not yet been finalized, therefore, Frontier is unable to determine whether it will participate in any competitive bid process at this time.

*Intercarrier Compensation:* In the 2011 Order, the FCC also reformed Intercarrier Compensation, which is the payment framework that governs how carriers compensate each other for the exchange of interstate switched traffic, and began a multi-year transition to the new rates. The 2011 Order provided for the gradual elimination of terminating traffic charges by July 2017 with a related decline in operating expenses. Switched access revenue declined sequentially in the third quarter of 2016, reflecting the rate reductions mandated by the 2011 Order, and we anticipate that we have experienced nearly all of the rate decline related to the 2011 Order. Frontier has been able to recover a significant portion of those lost revenues through end user rates and other replacement support mechanisms, a trend we expect will continue through 2017 and beyond. There are no longer any active Intercarrier Compensation-related challenges to the 2011 Order, and we believe that the 2011 Order provides a stable regulatory framework to facilitate our ongoing focus on the deployment of broadband into our rural markets.

*Special Access:* The FCC also has an ongoing proceeding, which dates back to 2015, to consider whether to make changes to its regulatory regime governing special access services, including whether to mandate lower rates, change standards for deregulation and pricing flexibility, or to require changes to other terms and conditions. In connection with its inquiry into specifically identified special access tariff pricing plans discussed below, on April 28, 2016, the FCC released a Notice of Proposed Rulemaking on special access or "business data" services. It sought comment on proposed changes to the way the FCC regulates traditional special access services based on market competition, and on a proposal to adopt pricing rules for Ethernet services in markets that are found to be "noncompetitive." On October 7, 2016, the FCC released a Fact Sheet detailing former FCC Chairman Wheeler's proposal for addressing special access issues, though this proposal was never adopted. The composition of the FCC has since changed following the Presidential election, and as a result the proceeding remains open and the potential impact to Frontier of this proceeding is unknown.

On April 28, 2016, the FCC completed its inquiry into whether certain terms and conditions contained in specifically identified special access tariff pricing plans offered by four carriers, including Frontier, are just and reasonable. The FCC held that certain of the tariff terms for business data TDM services, specifically DS1s and DS3s, were unreasonable. Specifically, the FCC struck down "excessive" early termination fees and "all-or-nothing" provisions. Frontier has revised its tariffs in accordance with the FCC's Order. The FCC's decision has no retroactive effect, and there has been no material impact to Frontier from it. The FCC deferred the issue of how its ruling will affect customers currently purchasing services from these tariffs to the Notice of Proposed Rulemaking mentioned above.

*Intrastate Services:* Some state regulatory commissions regulate some of the rates ILECs charge for intrastate services, including rates for intrastate access services paid by providers of intrastate long distance services. Some states also have their own open proceedings to address reform to intrastate access charges and other intercarrier compensation and state universal service funds. Although the FCC has pre-empted state jurisdiction on most access charges, some states could consider moving forward with their proceedings. We cannot predict when or how these matters will be decided or the effect on our subsidy or switched access revenues.

*Voice Over Internet Protocol (VoIP):* Regulators at both the federal and state levels continue to address whether VoIP services are subject to the same or different regulatory and intercarrier compensation regimes as traditional voice telephony. The FCC has concluded that VoIP and facilities-based broadband Internet access providers must comply with the Communications Assistance for Law Enforcement Act, a decision that the United States Court of Appeals for the District of Columbia Circuit has upheld. The FCC has also required VoIP providers to provide enhanced 911 emergency calling capabilities. In the 2011 Order, the FCC determined that VoIP-originated traffic terminating on the Public Switched Telephone Network is subject to interstate access rates. Effective December 29, 2011, the 2011 Order required providers to pay interstate access rates for the termination of VoIP toll traffic. On April 25, 2012, the FCC, in an Order on Reconsideration, specified that changes to originating access rates for VoIP traffic would not be implemented until July 2014. The 2011 Order was challenged in court, and the FCC was petitioned to reconsider various aspects. While most challenges have been resolved, on November 18, 2016, the U.S. Court of Appeals for the D.C. Circuit remanded to the FCC AT&T's challenge regarding the ability of competitive carriers to assess VoIP access charges. The net impact of the 2011 Order during the period from July

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

2012 through December 2014 was not significant for Frontier. The net effect of 2011 Order changes to originating access after July 1, 2014 is dependent upon the percentage of VoIP traffic.

Additionally, the 2011 Order requires VoIP providers to pay interstate terminating interconnection charges and requires all carriers terminating traffic to provide appropriate call information, thus prohibiting so-called "phantom traffic." However, the FCC declined to address other VoIP-related issues, and the FCC has stated its intent to address open questions regarding the treatment of VoIP services in its ongoing "IP-Enabled Services Proceeding." Internet telephony may have an advantage in the marketplace over our traditional services if this service remains less regulated.

*Current and potential Internet regulatory obligations:* On June 14, 2016, the United States Court of Appeals for the D.C. Circuit upheld the FCC's 2015 Order in which the FCC asserted jurisdiction over broadband service, utilizing its jurisdictional authority under Title II and Section 706 of the Communications Act of 1996, classified broadband service as a "telecommunications service". The FCC adopted rules to "preserve a Free and Open Internet" (i.e., net neutrality) that impose specific obligations for fixed and mobile providers of broadband Internet access services and specifically prohibit the following: blocking access to legal content, applications, services, or non-harmful devices; impairing or degrading lawful Internet traffic on the basis of content, applications, services, or non-harmful devices; favoring some lawful Internet traffic over other lawful traffic in exchange for consideration; and otherwise unreasonably harming consumers or edge providers. These obligations are largely consistent with the practices Frontier already had in place. The FCC also announced additional transparency requirements, which allow for a "safe harbor" disclosure framework, intended to provide consumers more information about a provider's network management practices, performance, speed, price, and data caps.

Several parties have asked the D.C. Circuit to reconsider its decision and, depending on the outcome, are likely to ask the Supreme Court to review the Order. Frontier continues to comply with the existing regulatory requirements, and it is unclear whether the pending appeal will have any impact on the regulatory structure.

In addition to the net neutrality rules, the FCC on October 27, 2016, relied on its newfound Title II authority to promulgate privacy rules for broadband providers. These rules govern how broadband providers can use sensitive customer information and the steps providers must take to protect that information. Petitions for reconsideration of these rules were due in January 2017, and whether these rules will remain in place is uncertain, particularly due to the change in administration.

**Video programming**

Federal, state and local governments extensively regulate the video services industry. Our FiOS and Vantage video services are subject to, among other things: subscriber privacy regulations; requirements that we carry a local broadcast station or obtain consent to carry a local or distant broadcast station; rules for franchise renewals and transfers; the manner in which program packages are marketed to subscribers; and program access requirements.

We provide video programming in some of our markets in California, Connecticut, Florida, Indiana, Minnesota, North Carolina, Oregon, South Carolina, Texas and Washington pursuant to franchises, permits and similar authorizations issued by state and local franchising authorities. Most franchises are subject to termination proceedings in the event of a material breach. In addition, most franchises require payment of a franchise fee as a requirement to the granting of authority.

Many franchises establish comprehensive facilities and service requirements, as well as specific customer service standards and monetary penalties for non-compliance. In many cases, franchises are terminable if the franchisee fails to comply with material provisions set forth in the franchise agreement governing system operations. We believe that we are in compliance and meeting all material standards and requirements. Franchises are generally granted for fixed terms of at least ten years and must be periodically renewed. Local franchising authorities may resist granting a renewal if either past performance or the prospective operating proposal is considered inadequate.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Environmental regulation**

The local exchange carrier subsidiaries we operate are subject to federal, state and local laws and regulations governing the use, storage, disposal of, and exposure to hazardous materials, the release of pollutants into the environment and the remediation of contamination. As an owner and former owner of property, we are subject to environmental laws that could impose liability for the entire cost of cleanup at contaminated sites, including sites formerly owned by us, regardless of fault or the lawfulness of the activity that resulted in contamination. We believe that our operations are in substantial compliance with applicable environmental laws and regulations.

**Segment information**

We currently operate in only one reportable segment.

**Financial Information about Foreign and Domestic Operations and Export Sales**

We have no foreign operations.

**General**

The dollar amount of our order backlog is not a significant consideration in our business and is not a meaningful metric for us. We have no material contracts or subcontracts that may be subject to renegotiation of profits or termination at the election of the federal government.

**Intellectual Property**

We believe that we have the trademarks, trade names and intellectual property licenses that are necessary for the operation of our business.

**Employees**

As of December 31, 2016, we had approximately 28,300 employees, as compared to approximately 19,200 employees as of December 31, 2015. During 2016, reduction in workforce activities resulted in the severance of approximately 1,950 employees of which approximately 450 employees remained as employees as of December 31, 2016. Approximately 17,900 of our total employees are represented by unions. The number of employees covered by a collective bargaining agreement that expired in 2016, but have been extended and are still effective for 2017, is approximately 600. The number of employees covered by collective bargaining agreements that expire in 2017 is approximately 3,800. We consider our relations with our employees to be good.

**Available Information**

We are subject to the informational requirements of the Securities Exchange Act of 1934 (the Exchange Act). Accordingly, we file periodic reports, proxy statements and other information with the Securities and Exchange Commission (SEC). These reports, proxy statements and other information may be obtained by visiting the Public Reference Room of the SEC at 100 F Street, NE, Washington, D.C. 20549 or by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an Internet site ([www.sec.gov](http://www.sec.gov)) that contains reports, proxy and information statements and other information regarding Frontier and other issuers that file electronically.

We make available, free of charge on our website, our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to these reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act, as soon as practicable after we electronically file these documents with, or furnish them to, the SEC. These documents may be accessed through our website at [www.frontier.com](http://www.frontier.com) under "Investor Relations." The information posted or linked on our website is not part of this report. We also make our Annual Report available in printed form upon request at no charge.

We also make available on our website, as noted above, or in printed form upon request, free of charge, our Corporate Governance Guidelines, Code of Business Conduct and Ethics, Specific Code of Business Conduct and Ethics Provisions for Certain Officers, and the charters for the Audit, Compensation, and Nominating and Corporate Governance committees of the Board of Directors. Stockholders may request printed copies of these materials by writing to: 401 Merritt 7, Norwalk, Connecticut 06851 Attention: Corporate Secretary.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Forward-Looking Statements**

This Annual Report on Form 10-K contains "forward-looking statements," related to future, not past, events. Forward-looking statements address our expected future business and financial performance and financial condition, and contain words such as "expect," "anticipate," "intend," "plan," "believe," "seek," "see," "will," "would," or "target." Forward-looking statements by their nature address matters that are, to different degrees, uncertain. For us, particular uncertainties that could cause our actual results to be materially different than those expressed in our forward-looking statements include:

- competition from cable, wireless and wireline carriers, satellite, and OTT companies, and the risk that we will not respond on a timely or profitable basis;
- our ability to successfully adjust to changes in the communications industry, including the effects of technological changes and competition on our capital expenditures, products and service offerings;
- our ability to implement successfully our organizational structure changes;
- risks related to the operation of properties acquired from Verizon, including our ability to retain or obtain customers in those markets, our ability to realize anticipated cost savings, and our ability to meet commitments made in connection with the acquisition;
- reductions in revenue from our voice customers that we cannot offset with increases in revenue from broadband and video subscribers and sales of other products and services;
- our ability to maintain relationships with customers, employees or suppliers;
- the impact of regulation and regulatory, investigative and legal proceedings and legal compliance risks;
- continued reductions in switched access revenues as a result of regulation, competition or technology substitutions;
- the effects of changes in the availability of federal and state universal service funding or other subsidies to us and our competitors;
- our ability to effectively manage service quality in our territories and meet mandated service quality metrics;
- our ability to successfully introduce new product offerings;
- the effects of changes in accounting policies or practices, including potential future impairment charges with respect to our intangible assets;
- our ability to effectively manage our operations, operating expenses, capital expenditures, debt service requirements and cash paid for income taxes and liquidity, which may affect payment of dividends on our common and preferred shares;
- the effects of changes in both general and local economic conditions on the markets that we serve;
- the effects of increased medical expenses and pension and postemployment expenses;
- the effects of changes in income tax rates, tax laws, regulations or rulings, or federal or state tax assessments;
- our ability to successfully renegotiate union contracts;
- changes in pension plan assumptions, interest rates, regulatory rules and/or the value of our pension plan assets, which could require us to make increased contributions to the pension plan in 2017 and beyond;
- adverse changes in the credit markets;

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

- adverse changes in the ratings given to our debt securities by nationally accredited ratings organizations;
- the availability and cost of financing in the credit markets;
- covenants in our indentures and credit agreements that may limit our operational and financial flexibility;
- the effects of state regulatory cash management practices that could limit our ability to transfer cash among our subsidiaries or dividend funds up to the parent company;
- the effects of severe weather events or other natural or man-made disasters, which may increase our operating expenses or adversely impact customer revenue; and
- the impact of potential information technology or data security breaches or other disruptions.

Any of the foregoing events, or other events, could cause our results to vary from management's forward-looking statements included in this report. You should consider these important factors, as well as the risks set forth under Item 1A, "Risk Factors," in evaluating any statement in this report or otherwise made by us or on our behalf. We have no obligation to update or revise these forward-looking statements and do not undertake to do so.

Investors should also be aware that while we do, at various times, communicate with securities analysts, it is against our policy to disclose to them selectively any material non-public information or other confidential information. Accordingly, investors should not assume that we agree with any statement or report issued by an analyst, irrespective of the content of the statement or report. To the extent that reports issued by securities analysts contain any projections, forecasts or opinions, such reports are not our responsibility.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Item 1A. Risk Factors**

Before you make an investment decision with respect to any of our securities, you should carefully consider all the information we have included in this Annual Report on Form 10-K and our subsequent periodic filings with the SEC. In particular, you should carefully consider the risk factors described below and the risks and uncertainties related to "Forward-Looking Statements," any of which could materially adversely affect our business, operating results, financial condition and the actual outcome of matters as to which forward-looking statements are made in this annual report. The risks and uncertainties described below are not the only ones facing Frontier. Additional risks and uncertainties that are not presently known to us or that we currently deem immaterial or that are not specific to us, such as general economic conditions, may also adversely affect our business and operations. The following risk factors should be read in conjunction with the balance of this annual report, including the consolidated financial statements and related notes included in this report.

**Risks Related to Our Business**

***We will likely face further reductions in voice customers, switched access minutes of use, long distance revenues and subsidy revenues.***

We have experienced declining voice customers, switched access minutes of use and related revenues, long distance revenues, federal and state subsidies and related revenues because of economic conditions, increasing competition, changing technology and consumer behavior (such as wireless displacement of wireline use, e-mail use, instant messaging and increasing use of VoIP), technology and regulatory constraints, and financial decisions by governmental authorities. We will likely continue to experience further reductions in the future. These factors, among others, are likely to cause our local network service, switched network access, long distance and subsidy revenues to continue to decline, and these factors may cause our cash generated by operations to decrease.

***We face intense competition.***

The communications industry is extremely competitive. Through mergers and various service expansion strategies, service providers are striving to provide integrated solutions both within and across geographic markets. Our competitors include competitive local exchange carriers, internet service providers, wireless companies, OTT, VoIP providers and cable companies, some of which may be subject to less regulation than we are; these entities may provide services competitive with the services that we offer or intend to introduce. We also believe that wireless and cable telephony providers have increased their penetration of various services in our markets. We expect that competition will remain robust. Our revenue and cash flow will be adversely impacted if we cannot reverse our customer losses or continue to provide high-quality services.

We cannot predict which of the many possible future technologies, products or services will be important in order to maintain our competitive position or what expenditures will be required to develop and provide these technologies, products or services. Our ability to compete successfully will depend on the effectiveness of capital expenditure investments in our properties, our marketing efforts, our ability to anticipate and respond to various competitive factors affecting the industry, including a changing regulatory environment that may affect our business and that of our competitors differently, new services that may be introduced, changes in consumer preferences, demographic trends, economic conditions and pricing strategies by competitors. Increasing competition may reduce our revenues and increase our marketing and other costs as well as require us to increase our capital expenditures and thereby decrease our cash flows.

***Some of our competitors have superior resources, which may place us at a cost and price disadvantage.***

Some of our competitors have market presence, engineering, technical, marketing and financial capabilities, substantially greater than ours. In addition, some of these competitors are able to raise capital at a lower cost than we are able to. Consequently, some of these competitors may be able to develop and expand their communications and network infrastructures more quickly, adapt more swiftly to new or emerging technologies and changes in customer requirements, take advantage of acquisition and other opportunities more readily and devote greater resources to the marketing and sale of their products and services than we will be able to. Additionally, the greater brand name recognition of some competitors may require us to price our services at lower levels in order to retain or

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

obtain customers. Finally, the cost advantages and greater financial resources of some of these competitors may give them the ability to reduce their prices for an extended period of time if they so choose. Our business and results of operations may be materially adversely impacted if we are not able to effectively compete.

***We may be unable to stabilize or grow our revenues and cash flows despite the initiatives we have implemented.***

We must produce adequate revenues and cash flows that, when combined with cash on hand and funds available under our revolving credit facility and other financings, will be sufficient to service our debt, fund our capital expenditures, pay our taxes, fund our pension and other employee benefit obligations and pay dividends pursuant to our dividend policy. We have experienced revenue declines in 2016 and 2015 as compared to prior years for our Frontier legacy operations, and our recently acquired operations have also experienced revenue declines. While we have identified potential areas of opportunity and implemented several revenue and cost initiatives, we cannot assure you that these efforts will be successful or that these initiatives will improve our financial position or our results of operations.

***Weak economic conditions may decrease demand for our services or necessitate increased discounts.***

We could be adversely impacted by weak economic conditions or their effects. Downturns in the economy and competition in our markets could cause some of our customers to reduce or eliminate their purchases of our basic and enhanced voice services, broadband and video services and make it difficult for us to obtain new customers or retain existing customers. In addition, if economic conditions are depressed or further deteriorate, our customers may delay or discontinue payment for our services or seek more competitive pricing from other service providers, or we may be required to offer increased discounts in order to retain our customers, which could have a material adverse effect on our business or results of operations.

***Disruption in our networks, infrastructure and information technology may cause us to lose customers and/or incur additional expenses.***

To attract and retain customers, we must provide reliable service. Some of the risks to our networks, infrastructure and information technology include physical damage, security breaches, capacity limitations, power surges or outages, software defects and other disruptions beyond our control, such as natural disasters and acts of terrorism. From time to time in the ordinary course of business, we experience short disruptions in our service due to factors such as cable damage, theft of our equipment, inclement weather and service failures of our third-party service providers. We could experience more significant disruptions in the future. We could also face disruptions due to capacity limitations if changes in our customers' usage patterns for our broadband services result in a significant increase in capacity utilization, such as through increased usage of video or peer-to-peer file sharing applications. Disruptions may cause interruptions in service or reduced capacity for customers, either of which could cause us to lose customers and/or incur additional expenses, and thereby adversely affect our business, revenues and cash flows.

***Our business is sensitive to the creditworthiness of our wholesale customers.***

We have substantial business relationships with other communications carriers for which we provide service. While bankruptcies of these carriers have not had a material adverse effect on our business in recent years, future bankruptcies in the industry could result in the loss of significant customers, as well as cause more price competition and an increased allowance for doubtful accounts receivable. Such bankruptcies may be more likely in the future if economic conditions stagnate. As a result, our revenues and results of operations could be materially and adversely affected.

***A significant portion of our workforce is represented by labor unions.***

As of December 31, 2016, we had approximately 28,300 employees. Approximately 17,900 of our total employees were represented by unions and were subject to collective bargaining agreements. As of December 31, 2016, we had approximately 600 employees covered by a collective bargaining agreement that expired in 2016, but have been extended and are still effective for 2017. Of the union-represented employees as of December 31, 2016, approximately 3,800, or 21%, of the unionized workforce are covered by collective agreements that expire in 2017 and approximately 3,500, or 20%, of the unionized workforce are covered by collective bargaining agreements that expire in 2018.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

We cannot predict the outcome of negotiations of the collective bargaining agreements covering our employees. If we are unable to reach new agreements or renew existing agreements, employees subject to collective bargaining agreements may engage in strikes, work slowdowns or other labor actions, which could materially disrupt our ability to provide services. New labor agreements or the renewal of existing agreements may impose significant new costs on us, which could adversely affect our financial condition and results of operations in the future.

***If we are unable to hire or retain key personnel, we may be unable to operate our business successfully.***

Our success will depend in part upon the continued services of our management. We cannot guarantee that our key personnel will not leave or compete with us. The loss, incapacity or unavailability for any reason of key members of our management team could have a material impact on our business. In addition, our financial results and our ability to compete will suffer if we are unable to attract, integrate or retain other qualified personnel in the future.

***We may be unable to realize the anticipated benefits of recent acquisitions.***

In recent years, we have completed multiple acquisitions. We cannot assure you that we will be able to realize the full benefit of any anticipated growth opportunities or cost synergies from such acquisitions or that these benefits will be realized within the expected time frames.

***We may complete a future significant strategic transaction that may not achieve intended results or could increase the number of our outstanding shares or amount of outstanding debt.***

We continuously evaluate and may in the future enter into additional strategic transactions. Any such transaction could happen at any time, could be material to our business and could take any number of forms, including, for example, an acquisition, merger or a sale of certain of our assets.

Evaluating potential transactions and integrating completed ones may divert the attention of our management from ordinary operating matters. The success of these potential transactions will depend, in part, on our ability to realize the anticipated growth opportunities and cost synergies through the successful integration of the businesses we acquire with our existing business. Even if we are successful in integrating acquired businesses, we cannot assure you that these integrations will result in the realization of the full benefit of any anticipated growth opportunities or cost synergies or that these benefits will be realized within the expected time frames. In addition, acquired businesses may have unanticipated liabilities or contingencies.

If we complete an acquisition, investment or other strategic transaction, we may require additional financing that could result in an increase in the number of our outstanding shares of stock or the aggregate amount and/or cost of our debt, which may result in an adverse impact to our ratings. The number of shares of our stock or the aggregate principal amount of our debt that we may issue may be significant. Moreover, the terms of any debt financing may be expensive or adversely impact our results of operations.

***Negotiations with the providers of content for our video systems may not be successful, potentially resulting in our inability to carry certain programming channels on our FiOS and Vantage video systems, which could result in the loss of subscribers. Alternatively, because of the power of some content providers, we may be forced to pay an increasing amount for some content, resulting in higher expenses and lower profitability.***

We must negotiate with the content owners of the programming that we carry on our multichannel video systems (marketed as FiOS video and Vantage video). These content owners are the exclusive provider of the channels they offer. If we are unable to reach a mutually-agreed contract with a content owner, including pricing and carriage provisions, our existing agreements to carry this content may not be renewed, resulting in the blackout of these channels. The loss of content could result in our loss of customers who place a high value on the particular content that is lost. In addition, many content providers own multiple channels. As a result, we typically have to negotiate the pricing for multiple channels rather than one, and carry and pay for content that customers do not much value, in order to have access to other content that customers value quite highly. Some of our competitors have materially larger scale than we do, and may, as a result, be better positioned than we are in such

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

negotiations. As a result of these factors, the expense of content acquisition may continue to increase, and this could result in higher expenses and lower profitability.

**Risks Related to Liquidity, Financial Resources and Capitalization**

***We expect to make contributions to our pension plan in future years, the amount of which will be impacted by volatility in asset values related to Frontier's pension plan and/or changes in pension plan assumptions.***

Frontier made contributions of \$28 million and \$62 million to its pension plan in 2016 and 2015, respectively, and we expect to continue to make contributions in future years. Volatility in our asset values, liability calculations, or returns may impact the costs of maintaining our pension plan and our future funding requirements. Any future material contribution could have a negative impact on our liquidity by reducing cash flows.

***We currently have a significant amount of indebtedness, including secured indebtedness, and are able to incur substantial additional indebtedness and grant substantial additional liens in the future. Such debt and debt service obligations may adversely affect us.***

We have a significant amount of indebtedness, which amounted to \$18.2 billion outstanding at December 31, 2016, of which \$2.3 billion was secured. We also have access to a \$750 million secured Revolving Credit Facility, which currently is undrawn.

The terms of our indentures and credit facilities allow us to incur substantial additional indebtedness and grant substantial additional liens in the future. In addition, these terms do not prevent us or our restricted subsidiaries from incurring various types of obligations that do not constitute "indebtedness" under these terms.

If we incur any additional indebtedness that ranks equally with our senior notes and debentures, the holders of that new debt will be entitled to share ratably with holders of our senior notes and debentures in any proceeds distributed in connection with any insolvency, liquidation, reorganization, dissolution or other winding up of Frontier. If any such additional indebtedness is secured, it will be effectively senior to our unsecured senior notes and debentures to the extent of the collateral securing such indebtedness. This may have the effect of reducing the probability of payment, or the amount of proceeds paid, to holders of our senior notes and debentures.

In addition, to the extent other new debt is added to our and our subsidiaries' current debt levels, the substantial leverage risks described below would increase.

The potential significant negative consequences on our financial condition and results of operations that could result from our substantial debt include:

- limitations on our ability to obtain additional debt or equity financing on favorable terms or at all;
- instances in which we are unable to comply with the covenants contained in our indentures and credit agreements or to generate cash sufficient to make required debt payments, which circumstances have the potential of accelerating the maturity of some or all of our outstanding indebtedness;
- the allocation of a substantial portion of our cash flow from operations to service our debt, thus reducing the amount of our cash flows available for other purposes, including capital expenditures and dividends that would otherwise improve our competitive position, results of operations or stock price;
- requiring us to issue debt or equity securities or to sell some of our core assets, possibly on unfavorable terms, to meet payment obligations;
- compromising our flexibility to plan for, or react to, competitive challenges in our business and the telecommunications industry; and
- the possibility of our being put at a competitive disadvantage with competitors who, relative to their size, do not have as much debt as we do, and competitors who may be in a more favorable position to access additional capital resources.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

In addition, our senior notes and debentures are rated below "investment grade" by independent rating agencies. This can result in higher borrowing costs for us. We cannot assure you that these rating agencies will not lower our current debt ratings, if in the rating agencies' judgment such an action is appropriate. A lowering of a rating may further increase our future borrowing costs and reduce our access to capital.

***The indentures and agreements governing our debt, including our senior notes and debentures and our credit facilities, contain covenants that impose restrictions on us and certain of our subsidiaries that may affect our ability to operate our business, make payments on our debt, and pay dividends.***

The indentures and agreements governing our existing indebtedness contain covenants that, among other things, limit our ability and the ability of certain of our subsidiaries to:

- incur additional indebtedness, guarantee indebtedness or issue preferred stock;
- create liens;
- enter into mergers or consolidations, or transfer or sell all or substantially all of our assets;
- pay dividends on, or make distributions in respect of, or redeem or repurchase, capital stock, make certain investments or make other restricted payments;
- make certain asset sales;
- enter into agreements that might prevent certain of our subsidiaries from making distributions, loans or advances to us or other subsidiaries; and
- engage in transactions with affiliates.

In addition, our credit facilities require us to comply with additional covenants, including financial ratios. Any future indebtedness may also require us to comply with similar or other covenants. These restrictions on our ability to operate our business could seriously harm our business by, among other things, limiting our ability to take advantage of financings, mergers, acquisitions and other corporate opportunities.

Various risks, uncertainties and events beyond our control could affect our ability to comply with these covenants. Failure to comply with any of the covenants in our existing or future financing indentures and agreements could result in a default under those documents and under other agreements containing cross-default provisions. A default would permit lenders to accelerate the maturity of the debt and to foreclose upon any collateral securing the debt. Under these circumstances, we might not have sufficient funds or other resources to satisfy all of our obligations. In addition, the limitations imposed by indentures and credit agreements on our ability to incur additional debt and to take other actions might significantly impair our ability to obtain other financing.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

***Frontier is primarily a holding company and, as a result, we rely on the receipt of funds from our subsidiaries in order to meet our cash needs and service our indebtedness, including our senior notes and debentures.***

Frontier is primarily a holding company and its principal assets consist of the shares of capital stock or other equity instruments of its subsidiaries. As a holding company, we depend on dividends, distributions and other payments from our subsidiaries to fund our obligations, including those arising under our senior notes and debentures, and meet our cash needs. We cannot assure you that the operating results of our subsidiaries at any given time will be sufficient to make dividends, distributions or other payments to us in order to allow us to make payments on our indebtedness, including our senior notes and debentures. In addition, the payment of these dividends, distributions and other payments, as well as other transfers of assets, between our subsidiaries and from our subsidiaries to us may be subject to legal, regulatory or contractual restrictions. Some state regulators have imposed and others may consider imposing on regulated companies, including us, cash management practices that could limit the ability of such regulated companies to transfer cash between subsidiaries or to the parent company. While none of the existing state regulations materially affects our cash management, any changes to the existing regulations or imposition of new regulations or restrictions may materially adversely affect our ability to transfer cash within our consolidated companies.

***Our senior notes and debentures are structurally subordinated to liabilities of our subsidiaries.***

Our subsidiaries have not guaranteed our senior notes and debentures. As a result, holders of such securities will not have any claim as a creditor against our subsidiaries. Accordingly, all obligations of our subsidiaries (including any liens granted by our subsidiaries on any of their assets to secure any of our obligations) will have to be satisfied before any of the assets of such subsidiaries would be available for distribution, upon a liquidation or otherwise. Although the indentures governing our senior notes and debentures, and our credit agreements, limit the indebtedness our subsidiaries may incur, our subsidiaries are able to incur a substantial amount of additional debt. Additionally, although the indentures and credit agreements limit the liens that may be granted on the assets of our subsidiaries, our subsidiaries are able to grant liens to secure a substantial amount of liabilities, including, without limitation, certain indebtedness under our credit facilities.

***Our senior notes and debentures are unsecured and subordinated to any secured indebtedness.***

Our senior notes and debentures are unsecured and therefore are subordinated to our existing and future secured indebtedness, to the extent of the value of the assets securing such indebtedness. At December 31, 2016, our secured indebtedness consisted of obligations under the 2015 Credit Agreement, the CoBank Credit Agreements, the Revolving Credit Agreement and the Continuing Agreement for Standby Letters of Credit dated February 4, 2008 between Frontier and Deutsche Bank AG New York Branch, each of which is secured equally and ratably by a pledge of all of the outstanding shares of capital stock of Frontier North Inc., a wholly-owned subsidiary. In the event of a bankruptcy or similar proceeding, the assets that serve as collateral for our secured indebtedness will be available to satisfy the obligations under the secured indebtedness before any payments are made on the senior notes and debentures from the proceeds of such assets. The indentures governing our senior notes and debentures permit us, subject to specified limitations, to incur a substantial amount of additional secured debt.

***If the senior notes issued in September 2015 are rated investment grade by at least two of Moody's, S&P or Fitch, many of the covenants will not apply and the holders of the notes will lose the protection of the covenants.***

Each of the supplemental indentures governing our senior notes issued in September 2015 contain certain covenants that will be suspended during any period in which such series of notes are rated investment grade by at least two of Moody's, S&P or Fitch and no default or event of default has occurred and is continuing. Such covenants limit, among other things, our ability to pay distributions, incur debt and enter into certain other transactions. There can be no assurance that any series of notes will ever be rated investment grade, or that if they are rated investment grade, that the series of notes will maintain these ratings. To the extent the covenants are subsequently reinstated, any such actions taken while the covenants were suspended would not result in an event of default under the supplemental indentures governing the applicable series of notes.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

***Our variable rate indebtedness subjects us to interest rate risk, which could cause our debt service obligations to increase.***

At December 31, 2016, approximately 12% of our total debt is subject to variable rates of interest. Borrowings under our credit facilities are at variable rates of interest and expose us to interest rate risk. If interest rates were to increase, our debt service obligations on the variable rate indebtedness would increase even though the amount borrowed remained the same, and our net income and cash flows, including cash available for servicing our indebtedness, would correspondingly decrease. In the future, we may enter into interest rate swaps that involve the exchange of floating for fixed rate interest payments in order to reduce interest rate volatility. However, we might not maintain interest rate swaps with respect to all of our variable rate indebtedness, and any swaps we enter into might not fully mitigate our interest rate risk.

***We may not have sufficient funds to repurchase our senior notes upon a change of control triggering event.***

The terms of our senior notes require us to make an offer to repurchase the notes upon the occurrence of a Change of Control and Ratings Decline (as defined in the indentures governing the notes) at a purchase price equal to 101% of the respective principal amounts of the notes plus accrued and unpaid interest to, but not including, the date of the purchase. It is possible that we would not have sufficient funds at the time of such a change of control triggering event to make the required repurchase of the applicable series of notes and would be required to obtain third party financing to do so. We may not be able to obtain this financing on commercially reasonable terms, or on terms acceptable to us, or at all. In addition, the occurrence of certain change of control events may constitute an event of default under the terms of our credit facilities. Such an event of default would entitle the lenders under our credit facilities to, among other things, cause all outstanding debt thereunder to become due and payable.

***We cannot assure that we will be able to continue paying dividends.***

The amount and timing of future dividend payments is subject to applicable law and will be made at the discretion of our Board of Directors based on factors such as cash flow and cash requirements, capital expenditure requirements, financial condition and other factors.

***Our ability to declare and pay dividends on the Series A Preferred Stock may be limited.***

Our declaration and payment of dividends on the Series A Preferred Stock in the future will be determined by our Board of Directors in its sole discretion and will depend on business conditions, our financial condition, earnings and liquidity and other factors. Our ability to declare and pay dividends and make other distributions with respect to our capital stock, including the Series A Preferred Stock, is restricted by the terms of certain of our existing financing arrangements and may be restricted by the terms of financing arrangements that we enter into in the future. In the event that the agreements governing any such indebtedness restrict our ability to declare and pay dividends in cash on the shares of Series A Preferred Stock, we may be unable to declare and pay dividends in cash on the shares of Series A Preferred Stock unless we can repay or refinance the amounts outstanding under such agreements.

In addition, under Delaware law, our Board of Directors may only declare and pay dividends on shares of our capital stock out of our statutory "surplus" (which is the amount equal to total assets minus total liabilities, in each case at fair market value, minus statutory capital), or if there is no such surplus, out of our net profits for the then current and/or immediately preceding fiscal year. Further, even if we are permitted under our contractual obligations and Delaware law to declare and pay cash dividends on the shares of Series A Preferred Stock, we may not have sufficient cash to do so through the mandatory conversion date of June 29, 2018.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

***We have a significant amount of goodwill and other intangible assets on our balance sheet. If our goodwill or other intangible assets become impaired, we may be required to record a non-cash charge to earnings and reduce our stockholders' equity.***

Under generally accepted accounting principles, intangible assets are reviewed for impairment on an annual basis or more frequently whenever events or circumstances indicate that their carrying value may not be recoverable. Frontier monitors relevant circumstances, including general economic conditions, enterprise value EBITDA multiples for other providers of communications services, our overall financial performance, and the market prices for our stock, and the potential impact that changes in such circumstances might have on the valuation of Frontier's goodwill or other intangible assets. If our goodwill or other intangible assets are determined to be impaired in the future, we may be required to record a non-cash charge to earnings during the period in which the impairment is determined, which would reduce our stockholders' equity.

**Risks Related to Regulation*****Changes in federal or state regulations may reduce the switched access charge revenues we receive.***

A portion of Frontier's total revenues (\$170 million, or 2%, in 2016 and \$177 million, or 3%, in 2015) are derived from switched access charges paid by other carriers for services we provide in originating and terminating intrastate and interstate long distance traffic. Frontier expects a portion of our revenues will continue to be derived from switched access charges paid by these carriers for these services. The amount of switched access charge revenues that Frontier will receive for these services is regulated by the FCC and state regulatory agencies and the rate Frontier can charge for terminating switched access is expected to decline in 2017.

In 2011, the FCC adopted the 2011 Order regarding Intercarrier Compensation, which is the payment framework that governs how carriers compensate each other for the exchange of interstate traffic. The 2011 Order began a multi-year transition that moves the rate for terminating traffic to near zero by 2017. Frontier is permitted to recover a significant portion of those revenues through end user rates and other replacement support mechanisms. Additionally, the 2011 Order requires VoIP providers to pay interstate terminating interconnection charges and requires all carriers terminating traffic to provide appropriate call information, thus prohibiting so-called "phantom traffic." The reform of the Universal Service Fund shifts the existing High-Cost portion of the fund from supporting voice services to supporting broadband deployment in high-cost areas. The 2011 Order preempts the states with regard to the regulation of intrastate terminating access rates. The 2011 Order has been challenged in court and the FCC was petitioned to reconsider various aspects of it. The only issue that remains active on appeal is the ability of competitive carriers to assess VoIP access charges.

The FCC also has an ongoing proceeding considering whether to make changes to its regulatory regime governing special access services. When and how these proposed changes will be addressed is unknown and, accordingly, we cannot predict the impact of future changes on our results of operations.

Certain states also have their own open proceedings to address reform to intrastate access charges and other intercarrier compensation and state universal service funds. Although the FCC has pre-empted state jurisdiction on most access charges, many states could consider moving forward with their proceedings. We cannot predict when or how these matters will be decided or the effect on our subsidy or switched access revenues. However, future reductions in our subsidy or switched access revenues may directly affect our profitability and cash flows as those regulatory revenues do not have an equal level of associated variable expenses.

***We are reliant on support funds provided under federal and state laws.***

A portion of Frontier's total revenues (\$626 million, or 7%, in 2016 and \$500 million, or 9%, in 2015) are derived from federal and state subsidies for rural and high-cost support, commonly referred to as USF. The FCC's 2011 Order changed how federal subsidies are calculated and disbursed, with these changes being phased-in beginning in July 2012. These changes transition the USF, which supports voice services in high-cost areas, to the CAF, which supports broadband deployment in high-cost areas.

Future reductions in these subsidies, or in our ability to recover such fees, could have a material adverse effect on our business or results of operations.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

***Frontier and our industry will likely remain highly regulated, and we could incur substantial compliance costs that could constrain our ability to compete in our target markets.***

As an incumbent local exchange carrier, some of the services we offer are subject to significant regulation from federal, state and local authorities. This regulation could impact our ability to change our rates, especially on our basic voice services and our access rates, and could impose substantial compliance costs on us. Regulation could constrain our ability to compete and, in some jurisdictions, may restrict our ability to expand our service offerings. In addition, changes to the regulations that govern our business (including any implementation of the 2011 Order or the 2015 Order) may have an adverse effect on our business by reducing the allowable fees that we may charge, imposing additional compliance costs, reducing the amount of subsidies or otherwise changing the nature of our operations and the competition in our industry. At this time it is unknown how these regulations will affect Frontier's operations or ability to compete in the future. This and other FCC rulemakings and state regulatory proceedings, including those relating to intercarrier compensation, universal service and broadband services, could have a substantial adverse impact on our operations.

In addition, on June 14, 2016, the U.S. Court of Appeals for the D.C. Circuit upheld the FCC's February 26, 2015 order that changed the regulatory classification of broadband service from an "information service" to a "telecommunications service". In the Order, the FCC adopted specific obligations for fixed-mobile providers of broadband Internet access services and specifically prohibited the following: blocking access to legal content, applications, services, or non-harmful devices; impairing or degrading lawful Internet traffic on the basis of content, applications, services, or non-harmful devices; favoring some lawful Internet traffic over other lawful Internet traffic in exchange for consideration; and otherwise unreasonably harming consumers or edge providers, and announced additional transparency requirements intended to provide consumers more information about a providers network management practices, performance, speed and data caps.

Our Internet access offerings could become subject to additional laws and regulations as they are adopted or applied to the Internet. As the significance of the Internet expands, federal, state and local governments may pass laws and adopt rules and regulations, or apply existing laws and regulations to the Internet (including Internet access services), and related matters are under consideration in both federal and state legislative and regulatory bodies. We cannot predict whether the outcome of pending challenges to the FCC's order or future proceedings will prove beneficial or detrimental to our competitive position.

**Risks Related to Technology**

***We may be unable to meet the technological needs or expectations of our customers, and may lose customers as a result.***

The telecommunications industry is subject to significant changes in technology, and replacing or upgrading our infrastructure to keep pace with such technological changes could result in significant capital expenditures. If we do not replace or upgrade technology and equipment as necessary, we may be unable to compete effectively because we will not be able to meet the needs or expectations of our customers.

In addition, enhancements to product offerings and the management of broadband speed and capacity issues may influence our customers to consider other service providers, such as cable operators or wireless providers. We may be unable to attract new or retain existing customers from cable companies due to their deployment of enhanced broadband and VoIP technology. In addition, new capacity services for wireless broadband technologies may permit our competitors to offer broadband data services to our customers throughout most or all of our service areas. Any resulting inability to attract new or retain existing customers could adversely impact our business and results of operations in a material manner.

***Our services could be adversely affected and we may be subject to increased costs and claims in connection with Internet and systems security and malicious practices.***

We use encryption and authentication technology licensed from third parties to provide secure transmission of confidential information, including our business data and customer information. We also rely on employees in our network operations centers, data centers, call centers and retail stores to follow our procedures when handling such information. Any unauthorized access, computer viruses, accidental or intentional release of confidential information or other disruptions could result in increased costs, customer dissatisfaction leading to loss of customers and revenues, and fines and other liabilities.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

In addition, Frontier or Frontier's customers using our network to access the Internet may become victim to malicious and abusive Internet activities, including unsolicited mass advertising ("spam"), peer-to-peer file sharing, distribution of viruses, worms and other destructive or disruptive software. These activities could adversely affect our network, result in excessive call volume at our call centers and damage our or our customers' equipment and data.

Frontier maintains security measures, disaster recovery plans and business continuity plans for its business. However, Frontier's information technology networks and infrastructure may nonetheless be vulnerable to damage, disruptions or shutdowns due to attack by hackers or breaches, employee error or malfeasance, power outages, computer viruses, telecommunication or utility failures, systems failures, natural disasters or other catastrophic events. Any such events could result in legal claims or proceedings, liability or penalties, disruption in operations, misappropriation of sensitive data, damage to Frontier's reputation and costly response measures, which could adversely affect Frontier's business. There can be no assurance that such disruptions or misappropriations and the resulting repercussions will not be material to our results of operations, financial condition or cash flows.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Item 1B. Unresolved Staff Comments**

None.

**Item 2. Properties**

We own property, which consists primarily of land and buildings, office and warehouse facilities, central office equipment, software, outside plant and related equipment. Outside communications plant includes aerial and underground cable, conduit, poles and wires. Central office equipment includes digital switches and peripheral equipment. As such, our properties do not provide a basis for description by character or location of principal units. All of our property is considered to be in good working condition and suitable for its intended purpose.

Our gross investment in property, by category, as of December 31, 2016, was as follows:

*(\$ in millions)*

Land	\$	235
Buildings and leasehold improvements		2,300
General support		1,495
Central office/electronic circuit equipment		7,683
Poles		995
Cable, fiber and wire		10,267
Conduit		1,611
Other		52
Construction work in progress		903
Total	\$	<u>25,541</u>

**Item 3. Legal Proceedings**

See Note 19 of the Notes to Consolidated Financial Statements included in Part IV of this report.

We are party to various legal proceedings (including individual, class and putative class actions) arising in the normal course of our business covering a wide range of matters and types of claims including, but not limited to, general contracts, billing disputes, rights of access, taxes and surcharges, consumer protection, trademark and patent infringement, employment, regulatory, tort, claims of competitors and disputes with other carriers. Litigation is subject to uncertainty and the outcome of individual matters is not predictable. However, we believe that the ultimate resolution of all such matters, after considering insurance coverage or other indemnities to which we are entitled, will not have a material adverse effect on our financial position, results of operations, or cash flows.

**Item 4. Mine Safety Disclosures**

Not applicable.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

## PART II

**Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

Our common stock is currently traded on the NASDAQ Global Select Market under the symbol FTR. The amount and timing of dividends payable on our common stock are within the sole discretion of our Board of Directors. On December 11, 2014, our Board of Directors approved a 5% increase over the 2014 dividend rate in the planned quarterly cash dividend rate, commencing with the dividend for the first quarter of 2015. Dividends on shares of the Series A Preferred Stock are payable on a cumulative basis when, as and if declared by our Board of Directors (or an authorized committee thereof) at an annual rate of 11.125% on the liquidation preference of \$100.00 per share, on the last business day of March, June, September and December of each year, up to the mandatory conversion date of June 29, 2018. Series A Preferred Stock dividends of \$214 million and \$120 million were paid in 2016 and 2015, respectively. Cash dividends paid to common shareholders were \$493 million and \$456 million in 2016 and 2015, respectively. The declaration and payment of future dividends on our common stock is at the discretion of our Board of Directors, and will depend upon many factors, including our financial condition, results of operations, growth prospects, funding requirements, payment of cumulative dividends on Series A Preferred Stock, applicable law, restrictions in agreements governing our indebtedness and other factors our Board of Directors deem relevant.

A portion of the dividends on common stock is classified as total ordinary dividends and represents qualified dividends, and a portion of the dividends is classified as non-dividend distributions and represents a return of capital. For the year ended December 31, 2016, all dividends on common stock were classified as non-dividend distributions and represented a return of capital.

The following table indicates the high and low intra-day sales prices per share of common stock, as reported by the NASDAQ Global Select Market, and sets forth dividends paid per share of common stock during the periods indicated.

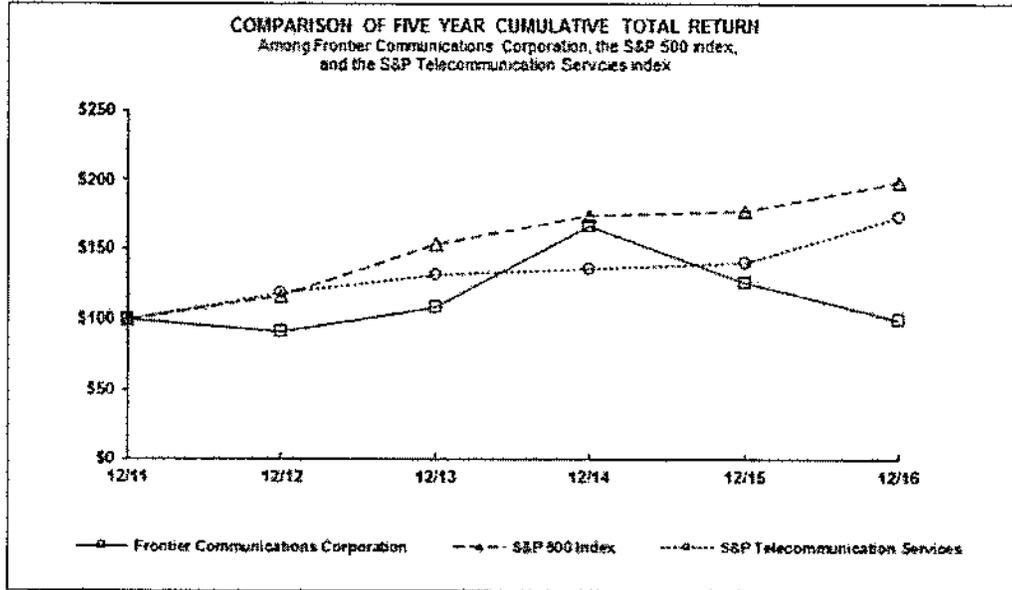
	2016			2015		
	High	Low	Dividend	High	Low	Dividend
First Quarter	\$ 5.85	\$ 3.81	\$ 0.105	\$ 8.46	\$ 6.36	\$ 0.105
Second Quarter	\$ 5.75	\$ 4.57	\$ 0.105	\$ 7.50	\$ 4.86	\$ 0.105
Third Quarter	\$ 5.22	\$ 4.07	\$ 0.105	\$ 5.64	\$ 4.19	\$ 0.105
Fourth Quarter	\$ 4.36	\$ 3.10	\$ 0.105	\$ 5.47	\$ 4.44	\$ 0.105

As of February 10, 2017, the approximate number of security holders of record of our common stock was 419,910. This information was obtained from our transfer agent, Computershare Inc.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

STOCKHOLDER RETURN PERFORMANCE GRAPH

The following performance graph compares the cumulative total return of our common stock to the S&P 500 Stock Index and to the S&P Telecommunication Services Index for the five-year period commencing December 31, 2011.



The graph assumes that \$100 was invested on December 31, 2011 in each of our common stock, the S&P 500 Stock Index and the S&P Telecommunication Services Index and that all dividends were reinvested.

Company / Index	Base Period	INDEXED RETURNS				
		12/11	12/12	12/13	12/14	12/15
Frontier Communications Corporation	100	91.18	108.83	166.51	126.17	100.44
S&P 500 Index	100	116.00	153.57	174.60	177.01	198.18
S&P Telecommunication Services	100	118.31	131.88	135.82	140.44	173.42

The foregoing performance graph and related information shall not be deemed "soliciting material" or to be "filed" with the SEC, nor shall such information be incorporated by reference into any future filings under the Securities Act of 1933 or the Securities Exchange Act of 1934, each as amended, except to the extent we specifically incorporate it by reference into such filing.

RECENT SALES OF UNREGISTERED SECURITIES, USE OF PROCEEDS FROM REGISTERED SECURITIES

There were no unregistered sales of equity securities during the fourth quarter of 2016.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

## ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased	Average Price Paid per Share
October 1, 2016 to October 31, 2016 Employee Transactions <sup>(1)</sup>	2,070	\$ 4.02
November 1, 2016 to November 30, 2016 Employee Transactions <sup>(1)</sup>	2,389	\$ 3.25
December 1, 2016 to December 31, 2016 Employee Transactions <sup>(1)</sup>	5,205	\$ 3.68
Totals October 1, 2016 to December 31, 2016 Employee Transactions <sup>(1)</sup>	9,664	\$ 3.64

<sup>(1)</sup> Includes restricted shares withheld (under the terms of grants under employee stock compensation plans) to offset minimum tax withholding obligations that occur upon the vesting of restricted shares. Frontier's stock compensation plans provide that the value of shares withheld shall be the average of the high and low price of our common stock on the date the relevant transaction occurs.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Item 6. Selected Financial Data**

The following tables present selected historical consolidated financial information of Frontier for the periods indicated. The selected historical consolidated financial information of Frontier as of and for each of the five fiscal years in the period ended December 31, 2016 has been derived from Frontier's historical consolidated financial statements. The selected historical consolidated financial information as of December 31, 2016 and 2015 and for each of the years in the three-year period ended December 31, 2016 is derived from the audited historical consolidated financial statements of Frontier included elsewhere in this Form 10-K. The selected historical consolidated financial information as of December 31, 2014, 2013 and 2012 and for each of the years ended December 31, 2013 and 2012 is derived from the audited historical consolidated financial statements of Frontier not included in this Form 10-K.

*(\$ in millions, except per share amounts)*

	Year Ended December 31, <sup>(1)</sup>				
	2016	2015	2014	2013	2012
Revenue	\$ 8,896	\$ 6,576	\$ 4,772	\$ 4,762	\$ 5,012
Operating Income	\$ 888	\$ 745	\$ 820	\$ 981	\$ 667
Net income (loss) <sup>(1)(2)(4)(5)</sup>	\$ (373)	\$ (196)	\$ 133	\$ 115	\$ 153
Net income (loss) attributable to Frontier common shareholders <sup>(2)(3)(4)(5)</sup>	\$ (587)	\$ (316)	\$ 133	\$ 113	\$ 137
Net income (loss) attributable to Frontier common shareholders per basic share <sup>(2)(3)(4)(5)</sup>	\$ (0.51)	\$ (0.29)	\$ 0.13	\$ 0.11	\$ 0.14
Net income (loss) attributable to Frontier common shareholders per diluted share <sup>(2)(3)(4)(5)</sup>	\$ (0.51)	\$ (0.29)	\$ 0.13	\$ 0.11	\$ 0.13
Cash dividends declared (and paid) per common share	\$ 0.42	\$ 0.42	\$ 0.40	\$ 0.40	\$ 0.40
Cash dividends declared (and paid) per share of Series A Preferred Stock	\$ 11.125	\$ 6.24 <sup>(6)</sup>	\$ -	\$ -	\$ -

*(\$ in millions)*

	As of December 31,				
	2016	2015	2014	2013	2012
Total assets	\$ 29,013	\$ 27,084	\$ 18,810	\$ 16,540	\$ 17,577
Long-term debt	\$ 17,560	\$ 15,508	\$ 9,393	\$ 7,810	\$ 8,324
Total shareholders' equity of Frontier	\$ 4,519	\$ 5,614	\$ 3,656	\$ 4,066	\$ 4,108

- (1) Operating results include activities for the CTF operations from the date of their acquisition from Verizon on April 1, 2016 and the Connecticut operations from the date of their acquisition from AT&T on October 24, 2014.
- (2) Operating results include the pre-tax impacts of losses on retirement of debt of \$160 million (\$99 million, or \$0.10 per share, after tax) and \$90 million (\$57 million, or \$0.06 per share, after tax) for 2013 and 2012, respectively.
- (3) Operating results include pre-tax acquisition and integration costs of \$436 million (\$283 million, or \$0.24 per share, after tax), \$236 million (\$133 million, or \$0.12 per share, after tax), \$142 million (\$91 million, or \$0.09 per share, after tax), \$10 million (\$6 million, or \$0.01 per share, after tax) and \$82 million (\$51 million, or \$0.05 per share, after tax) for 2016, 2015, 2014, 2013 and 2012, respectively.
- (4) Operating results include pre-tax restructuring costs and other charges of \$91 million (\$59 million, or \$0.05 per share, after tax), \$2 million (\$1 million after tax), \$2 million (\$1 million, after tax), \$12 million (\$7 million, or \$0.01 per share, after tax) and \$32 million (\$20 million, or \$0.02 per share, after tax) for 2016, 2015, 2014, 2013 and 2012, respectively.
- (5) Operating results include pre-tax pension settlement costs of \$44 million (\$27 million, or \$0.03 per share, after tax) for 2013.
- (6) Represents dividends on the 11.125% Mandatory Convertible Preferred Stock, Series A, from the issuance date of June 10, 2015 through December 31, 2015.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations****Introduction****(a) Results of Operations****2016 Compared to 2015**

On April 1, 2016, we completed our acquisition of Verizon's wireline properties in California, Texas, and Florida (the CTF Acquisition). Frontier's scope of operations and balance sheet changed materially as a result of the completion of the CTF Acquisition. Historical financial and operating data presented for Frontier includes the results of the CTF Operations that were acquired in the CTF Acquisition from the date of acquisition on April 1, 2016 and is not indicative of future operating results. The financial discussion below includes a comparative analysis of our results of operations on a historical basis for Frontier operations as of and for the years ended December 31, 2016 and 2015. Unless otherwise noted, the variance explanations discussed below are based upon an analysis of the 2016 financial data for Frontier legacy operations (excluding the CTF Operations) in comparison to 2015.

The sections below include tables that present customer counts, average monthly revenue per customer (ARPC) and residential customer churn which we define as the average of the amount of residential customer deactivations during the month divided by the number of residential customers at the beginning of the month. The following also categorizes revenue into customer revenue (residential and business) and regulatory revenue (switched access and subsidy). The decline in the number of customers was partially offset by increased penetration of additional higher revenue generating products and services sold to both residential and business customers, which has increased our average monthly revenue per customer in 2016 as compared to 2015. Similar to other wireline providers, we have experienced declines in the number of traditional voice customers, switched access minutes of use and rates per switched access minute of use, due to the FCC's intercarrier compensation reform, as a result of competition and the availability of substitutes, a trend which we expect will continue.

Management believes that residential customer counts and average monthly revenue per customer are important factors in evaluating our residential customer trends. Among the key services we provide to residential customers are voice service, data service and video service. We continue to explore the potential to provide additional services to our customer base, with the objective of meeting all of our customers' communications needs.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

## 2016 CUSTOMER RELATED METRICS COMPARED TO 2015

	As of or for the year ended December 31,		
	2016	% Increase (Decrease)	2015
<b>Customers (in thousands)</b>	5,383 <sup>(1)</sup>	58 %	3,413
<b>Residential customer metrics:</b>			
Customers (in thousands)	4,891 <sup>(2)</sup>	57 %	3,124
Average monthly residential revenue per customer	\$ 77.47	21 %	\$ 63.93
Customer monthly churn	1.98%	9 %	1.82%
<b>Business customer metrics:</b>			
Customers (in thousands)	502 <sup>(2)</sup>	74 %	289
Average monthly business revenue per customer	\$ 673.72	(2)%	\$ 690.88
Broadband subscribers (in thousands)	4,271 <sup>(2)</sup>	73 %	2,462
Video subscribers (in thousands)	1,419 <sup>(2)</sup>	156 %	554
Switched access minutes of use (in thousands)	19,450	27 %	15,327
Employees	28,332	48 %	19,160

<sup>(1)</sup>2,283,000 residential customers, 250,000 business customers and 2,533,000 total customers were acquired at the time of the April 2016 CTF Acquisition.

<sup>(2)</sup>2,052,000 broadband subscribers and 1,165,000 video subscribers were acquired at the time of the April 2016 CTF Acquisition.

Customer Trends

We provide service and product options in our residential and business offerings to the customer base in each of our markets which results in a better customer experience that allows us to maximize retention of existing customers and attract new customers. As of December 31, 2016, 63% of our residential broadband customers were subscribed to at least one other service offering.

During 2016, we gained approximately 2.0 million customers, net, as compared to a loss of 96,000 customers, net, in 2015. Although we added approximately 2.5 million customers in 2016 following the CTF Acquisition, we lost a net of approximately 553,000 customers across all of our markets. These customer losses were more heavily weighted in the newly acquired CTF markets due to transition disruptions following the acquisition, resulting in higher than normal customer churn, as well as the suspension of collection activities prior to and after the closing of the CTF Acquisition, and the suspension of marketing efforts for a period of time following the acquisition. These actions resulted in fewer additions than would otherwise have been achieved. Higher than normal customer losses are expected to continue into 2017 as collections efforts are caught-up for delinquent accounts and marketing efforts ramp up.

We had approximately 4.9 million and 3.1 million total residential customers as of December 31, 2016 and 2015, respectively. Although we added approximately 2.3 million total residential customers attributable to the CTF Acquisition in 2016, we lost approximately 516,000 residential customers, net, during 2016, composed of losses in both our legacy markets and in the CTF markets, principally driven by declines in voice customers. Our residential customer monthly churn was 1.98% for 2016. Average monthly residential revenue per customer (residential ARPC) increased \$13.54, or 21%, to \$77.47 during 2016 as compared to 2015. The overall increase in residential ARPC is a result of higher video revenue from our CTF Operations and improvements in data services revenue for our legacy operations, partially offset by lower voice services revenue. We expect to improve our video and data subscriber trends for our Frontier legacy and CTF operations. We anticipate continuing declines in voice services revenue as fewer residential customers subscribe to landline voice services. Frontier expects continuing increases in data services revenue, primarily driven by increased broadband subscribers, and continuing declines in voice services revenue.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

We had approximately 0.5 million and 0.3 million total business customers as of December 31, 2016 and 2015, respectively. Although we added 250,000 total business customers attributable to the CTF Acquisition in 2016, we lost approximately 38,000 business customers, net in 2016, composed of losses in both our legacy markets and in the CTF markets. Average monthly business revenue per customer (business ARPC) decreased \$17.16, or 2%, to \$673.72 during 2016 as compared to 2015. The business ARPC decrease is primarily attributable to our CTF markets having lower ARPC per SME (small business, medium business and larger enterprise customers) customer and proportionally fewer wholesale customers relative to total business customers as compared to our legacy markets. Frontier expects the declines in voice services revenue and wireless backhaul revenues from business customers to continue in 2017, mitigated, in part, by increases in data services revenue. We have seen modest increases in our revenues from small/medium/enterprise (SME) customers throughout 2016, and our Ethernet product revenues from our SME and carrier customers has grown by 8% for the Frontier legacy operations during 2016.

At December 31, 2016, we had approximately 1.8 million more broadband subscribers than we did at December 31, 2015. We added 2,052,000 subscribers as part of the CTF Acquisition; however, we lost approximately 243,000 net subscribers, primarily due to fewer gross activations and higher customer churn. At December 31, 2016, 57% of our consolidated residential broadband customers subscribed to speeds in excess of our 6 Mbps basic speed tier, up from 29% at December 31, 2015.

We offer video services under the Vantage brand to our customers in Connecticut, South Carolina, Minnesota, and Illinois and under the FiOS® brand in California, Texas, and Florida (and on a limited basis in Indiana, Oregon and Washington). We also offer satellite TV video service to our customers under an agency relationship with DISH® in all of our markets. During the year, we added 1,165,000 video subscribers in the CTF Acquisition. For the full year, we lost approximately 300,000 net video subscribers across all markets. At December 31, 2016, we had 1.14 million linear video subscribers that are served with FiOS or Vantage video service. In addition to our linear video subscribers, we have 274,000 DISH satellite video customers.

## 2016 REVENUE COMPARED TO 2015

(\$ in millions)	For the Year Ended December 31,					
	2016			2015		
	Consolidated Amount	CTF Operations	Frontier Legacy (excluding CTF Operations)			Amount
		Amount	\$ Increase (Decrease)	% Increase (Decrease)		
Voice services	\$ 2,886	\$ 1,077	\$ 1,809	\$ (213)	(11) %	\$ 2,022
Data and Internet services	3,693	1,366	2,327	(10)	(0) %	2,337
Video services	1,244	978	266	(19)	(7) %	285
Other	276	26	250	(5)	(2) %	255
Customer revenue	8,099	3,447	4,652	(247)	(5) %	4,899
Switched access and subsidy	797	175	622	(55)	(8) %	677
Total revenue	\$ 8,896	\$ 3,622	\$ 5,274	\$ (302)	(5) %	\$ 5,576

(\$ in millions)	For the Year Ended December 31,					
	2016			2015		
	Consolidated Amount	CTF Operations	Frontier Legacy (excluding CTF Operations)			Amount
		Amount	\$ Increase (Decrease)	% Increase (Decrease)		
Residential	\$ 4,383	\$ 2,092	\$ 2,291	\$ (141)	(6) %	\$ 2,432
Business	3,716	1,355	2,361	(106)	(4) %	2,467
Customer revenue	8,099	3,447	4,652	(247)	(5) %	4,899
Switched access and subsidy	797	175	622	(55)	(8) %	677
Total revenue	\$ 8,896	\$ 3,622	\$ 5,274	\$ (302)	(5) %	\$ 5,576

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

## REVENUE

We generate revenues primarily through either a monthly recurring fee or a fee based on usage, and revenue recognition is not dependent upon significant judgments by management, with the exception of a determination of a provision for uncollectible amounts.

Consolidated total revenue for 2016 increased \$3,320 million to \$8,896 million as compared to 2015. Excluding additional revenue of \$3,622 million in 2016 attributable to CTF operations, our revenue for 2016 decreased \$302 million, or 5%, as compared to 2015. This decline in 2016 is primarily the result of decreases in voice services revenues and lower switched and nonswitched access revenue, partially offset by an increase in data services revenue, each as described in more detail below.

Customer revenue for the year ended December 31, 2016 increased \$3,200 million to \$8,099 million as compared to 2015. Excluding additional customer revenue of \$3,447 million attributable to the CTF Operations, our customer revenue for 2016 decreased \$247 million, or 5%, as compared to 2015.

Consolidated residential customer revenue for the year ended December 31, 2016 increased \$1,951 million, or 80%, as compared to 2015. Consolidated residential customer revenue for the year ended December 31, 2016 included \$2,092 million of revenue attributable to the CTF Operations. Residential customer revenues for our legacy operations for the year ended December 31, 2016 decreased \$141 million, or 6%, compared to 2015, primarily as a result of decreases in voice services revenue, partially offset by increases in data services revenue. Similar to other wireline providers, we have experienced declines in the number of traditional voice customers and switched access minutes of use as a result of competition and the availability of substitutes, a trend we expect to continue. The consolidated monthly average revenue per customer (ARPC) for our residential customers increased 21% for the year ended December 31, 2016 as compared to 2015. The overall increase in residential ARPC is a result of higher video revenue from our CTF Operations and improvements in data services revenue for our legacy operations, partially offset by lower voice services revenue.

Consolidated business customer revenue for 2016 increased \$1,249 million, or 51%, as compared to 2015. Consolidated business customer revenue for 2016 included \$1,355 million of revenue attributable to the CTF Operations. Business customer revenue for our legacy operations declined \$106 million, or 4%, as compared to 2015, principally as a result of decreases in our voice services revenue and wireless backhaul revenue. The consolidated ARPC for our business customers decreased 2%, for the year ended December 31, 2016 as compared with 2015. The business ARPC decrease is primarily attributable to our CTF markets having lower ARPC per SME (small business, medium business and larger enterprise customers) customer and proportionally fewer wholesale customers relative to total business customers as compared to our legacy markets.

Consolidated switched access and subsidy revenue of \$797 million represented 9% of our revenues for 2016. Switched access revenue was \$170 million in 2016, or 2% of our revenues, down from \$177 million, or 3% of our revenues, in 2015. The Report and Order released by the FCC on November 18, 2011 (the 2011 Order) provided for the gradual elimination of terminating traffic charges by 2017 with a related decline in operating expenses. Switched access revenue declined sequentially in the third quarter of 2016, reflecting the rate reductions mandated by the 2011 Order, and we anticipate that we have experienced nearly all of the rate decline related to the 2011 Order. We have been able to recover a significant portion of these lost revenues through end user rates and other replacement support mechanisms, a trend we expect will continue throughout 2017. We expect declining revenue trends in switched access revenue to continue in 2017 in our legacy operations. Subsidy revenue, including CAF Phase II subsidies, was \$626 million in 2016, or 7% of our revenues, which increased from \$500 million, or 9% of our revenues, in 2015.

**We categorize our products, services and other revenues among the following five categories:**

Voice Services

Voice services include traditional local and long distance wireline services, data-based Voice over Internet Protocol (VoIP) services, as well as voice messaging services offered to our residential and business customers. Voice services also include the long distance voice origination and termination services that we provide to our business customers and other carriers.

Voice services revenue for 2016 decreased as compared with 2015, primarily due to the continued loss of voice customers and, to a lesser extent, decreases in individual feature packages, as well as long distance revenue among those customers that do not have a bundled long distance plan, partially offset by increased local voice charges to residential and business end users.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Data and Internet Services

Data and Internet services include broadband services for residential and business customers. We provide data transmission services to high volume business customers and other carriers with dedicated high capacity circuits ("nonswitched access") including services to wireless providers ("wireless backhaul"). In addition, we offer our Frontier Secure suite of products, including computer security, cloud backup and sharing, identity protection and equipment insurance. Frontier Secure also provides technical support services for businesses.

Data and Internet services revenue for 2016 decreased as compared with 2015. Data services revenues for 2016 increased \$45 million, or 3%, primarily due to higher Frontier Secure revenues. Nonswitched access revenues decreased \$55 million, or 6%, primarily due to lower monthly recurring revenues for wireless backhaul and other carrier services. We expect wireless data usage to continue to increase, which may drive the need for additional wireless backhaul capacity. Despite the need for additional capacity, in the near term, we anticipate that our overall wireless backhaul revenues (which comprise approximately 3% of our total revenues) will continue to be subject to decline in 2017, as our carrier customers migrate to Ethernet solutions at lower price points or migrate to our competitors.

Video Services

Video services include revenues generated from services provided directly to residential customers through the FIOS video and Vantage video brands, and through DISH satellite TV services.

Video services for 2016 decreased primarily due to a decrease in the total number of video subscribers.

Other

Other customer revenue includes sales of customer premise equipment to our business customers and directory services, less our provision for bad debts.

Other revenues for 2016 decreased primarily due to lower directory services revenue.

Switched Access and Subsidy

Switched access and subsidy revenues include revenues derived from allowing other carriers to use our network to originate and/or terminate their local and long distance voice traffic ("switched access"). These services are primarily billed on a minutes-of-use basis applying tariffed rates filed with the FCC or state agencies. We also receive cost subsidies from state and federal authorities, including the Connect America Fund.

Switched access and subsidy revenue for 2016 decreased as compared to 2015. Subsidy revenues decreased \$16 million, or 3% in 2016, primarily attributable to the one-time true-up payments and phasedown support recognized in 2015 in connection with the CAF Phase II program. Switched access revenue decreased \$39 million, or 22%, in 2016 primarily due to the impact of the decline in minutes of use related to access line losses and the displacement of minutes of use by wireless and other communications services, combined with the lower rates enacted by the FCC's intercarrier compensation.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

## 2016 OPERATING EXPENSES COMPARED TO 2015

## NETWORK ACCESS EXPENSE

(\$ in millions)	For the Year Ended December 31.					
			2016		2015	
	Consolidated Amount	CTF Operations	Frontier Legacy (excluding CTF Operations)		Amount	
			Amount	\$ Increase (Decrease)		
Network access expenses	\$ 1,470	\$ 852	\$ 618	\$ (22)	(3) %	\$ 640

Network access expenses include access charges and other third-party costs directly attributable to connecting customer locations to our network and video content costs. Such access charges and other third-party costs exclude network related expenses, depreciation and amortization, and employee related expenses.

Network access expenses for 2016 decreased in our legacy markets, primarily due to lower long distance costs and video content costs as a result of a decline in video customers, partially offset by increases in customer premise equipment costs, pole and conduit rental expense, and Frontier Secure costs.

## NETWORK RELATED EXPENSES

(\$ in millions)	For the Year Ended December 31.					
			2016		2015	
	Consolidated Amount	CTF Operations	Frontier Legacy (excluding CTF Operations)		Amount	
			Amount	\$ Increase (Decrease)		
Network related expenses	\$ 1,887	\$ 623	\$ 1,264	\$ (23)	(2) %	\$ 1,287

Network related expenses include expenses associated with the delivery of services to customers and the operation and maintenance of our network, such as facility rent, utilities, maintenance and other costs, as well as salaries, wages and related benefits associated with personnel who are responsible for the delivery of services, operation and maintenance of our network.

Network related expenses for 2016 decreased due to lower compensation costs, primarily related to decreased employee headcount, and certain benefits, including incentive compensation, pension and OPEB expense (as discussed below), and a reduction in rental costs for vehicles under operating leases that were modified during 2016, resulting in the classification as capital leases.

## SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

(\$ in millions)	For the Year Ended December 31.					
			2016		2015	
	Consolidated Amount	CTF Operations	Frontier Legacy (excluding CTF Operations)		Amount	
			Amount	\$ Increase (Decrease)		
Selling, general and administrative expenses	\$ 2,093	\$ 731	\$ 1,362	\$ 16	1 %	\$ 1,346

Selling, general and administrative expenses (SG&A expenses) include the salaries, wages and related benefits and the related costs of corporate and sales personnel, travel, insurance, non-network related rent, advertising and other administrative expenses.

SG&A expenses for 2016 increased due to higher costs for compensation, primarily related to increased employee headcount due to additional services provided by Frontier Secure, and certain benefits, including pension and OPEB expense (as discussed below), partially offset by lower incentive compensation for the year.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Pension and OPEB Costs**

Frontier allocates Pension and OPEB costs to network related expenses and SG&A expenses. Total consolidated pension and OPEB costs, excluding special termination benefits of \$26 million in 2016, for the years ended December 31, 2016 and 2015 were as follows:

(\$ in millions)	For the year ended December 31,	
	2016	2015
Total pension/OPEB expense	\$ 129	\$ 95
Less: capitalized into capital expenditures	(25)	(20)
Net pension/OPEB costs	\$ 104	\$ 75

**DEPRECIATION AND AMORTIZATION**

(\$ in millions)	For the year ended December 31,					
	Consolidated Amount	CTF Operations	2016		2015 Amount	
			Frontier Legacy (excluding CTF Operations) Amount	\$ Increase (Decrease)		% Increase (Decrease)
Depreciation expense	\$ 1,388	\$ 439	\$ 949	\$ (34)	(3) %	\$ 983
Amortization expense	643	361	282	(55)	(16) %	337
	\$ 2,031	\$ 800	\$ 1,231	\$ (89)	(7) %	\$ 1,320

Depreciation and amortization expense for 2016 decreased primarily due to the accelerated method of amortization related to the customer base that was acquired in our 2010 Acquisition with Verizon and in the Connecticut Acquisition, combined with changes in the remaining useful lives of certain plant assets and a lower net asset base.

**RESTRUCTURING COSTS AND OTHER CHARGES**

(\$ in millions)	For the year ended December 31,					
	Consolidated Amount	CTF Operations	2016		2015 Amount	
			Frontier Legacy (excluding CTF Operations) Amount	\$ Increase (Decrease)		% Increase (Decrease)
Restructuring costs and other charges	\$ 91	\$ 34	\$ 57	\$ 55	NM %	\$ 2

NM – Not Meaningful

Restructuring costs and other charges increased in 2016 compared to 2015 primarily due to a reduction in the workforce of approximately 1,950 employees resulting in an increase in severance and related expenses of \$30 million and pension/OPEB special termination benefit enhancements of \$25 million.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

## 2015 Compared to 2014

On October 24, 2014, Frontier completed the Connecticut Acquisition. The financial discussion below includes a comparative analysis of our results of operations on a historical basis for our Frontier operations as of and for the years ended December 31, 2015 and 2014. Unless otherwise noted, the variance explanations discussed below are based upon an analysis of the 2015 financial data for Frontier legacy operations (excluding the Connecticut Operations) in comparison to 2014 financial data for Frontier legacy operations (excluding the Connecticut Operations).

## 2015 CUSTOMER RELATED METRICS COMPARED TO 2014

	As of or for the year ended December 31,		
	2015	% Increase (Decrease)	2014
Customers (in thousands)	3,413	(3)%	3,510 <sup>(1)</sup>
<b>Residential customer metrics:</b>			
Customers (in thousands)	3,124	(3)%	3,205 <sup>(1)</sup>
Average monthly residential revenue per customer	\$ 63.93	5 %	\$ 61.11
Customer monthly churn	1.82%	5 %	1.73%
<b>Business customer metrics:</b>			
Customers (in thousands)	289	(5)%	305 <sup>(1)</sup>
Average monthly business revenue per customer	\$ 690.88	4 %	\$ 661.15
Broadband subscribers (in thousands)	2,462	4 %	2,360 <sup>(2)</sup>
Video subscribers (in thousands)	554	(5)%	582 <sup>(2)</sup>
Switched access minutes of use (in thousands)	15,327	1 %	15,193
Employees	19,160	10 %	17,354

<sup>(1)</sup>468,000 residential customers, 49,000 business customers and 517,000 total customers were acquired at the time of the October 2014 Connecticut Acquisition.

<sup>(2)</sup>385,000 broadband subscribers and 192,000 video subscribers were acquired at the time of the October 2014 Connecticut Acquisition.

Customer Trends

During 2015, we lost 96,000 customers, net, compared to a gain of 435,000 customers, net, in 2014. Although we added 517,000 customers in 2014 following the Connecticut Acquisition, we lost 82,000 customers, net, in 2014 across all of our markets.

We had approximately 3.1 million and 3.2 million total residential customers as of December 31, 2015 and 2014, respectively. Although we added 468,000 total residential customers attributable to the Connecticut Acquisition in 2014, we lost approximately 81,000 and 67,000 residential customers, net during 2015 and 2014, respectively, composed of losses in both our legacy markets and in the Connecticut markets, principally driven by declines in voice customers. Our residential customer monthly churn was 1.82% and 1.73% for 2015 and 2014, respectively. Residential ARPC increased \$2.82, or 5%, to \$63.93 during 2015 as compared to 2014. The overall increase in residential ARPC is due to a higher percentage of Frontier's residential customers who subscribe to our broadband services, the increase in our Frontier TV and FiOS-branded video customers, which is primarily attributable to our Connecticut Operations, and the increase in customers subscribed to multiple services.

We had approximately 0.3 million total business customers as of December 31, 2015 and 2014. Although we added 49,000 total business customers attributable to the Connecticut Acquisition in 2014, we lost approximately 16,000 and 15,000 business customers, net, during 2015 and 2014, respectively. Business ARPC increased \$29.73, or 4%, to \$690.88 during 2015 as compared to 2014. The overall increase in business ARPC is primarily due to declining customer counts for our small business customers that carry a lower ARPC.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

During 2015, Frontier added approximately 102,000 net broadband subscribers. During 2014, Frontier added approximately 493,000 (including 385,000 from the Connecticut Acquisition) net broadband subscribers. As of December 31, 2015, approximately 64% of our residential broadband customers subscribed to a bundle of services. As of December 31, 2015, we were able to offer broadband to approximately 7.9 million households, or 93% of the 8.5 million households in our markets. The increase in broadband subscribers contributed to our improved data services revenue performance. At December 31, 2015, 29% of our residential broadband customers subscribed to speeds in excess of our 6 Mbps basic speed tier, up from 24% at December 31, 2014. We offer FiOS-branded video services in three states, Frontier TV-branded video services in Connecticut and satellite video services through DISH throughout our territories. We lost 28,000 video subscribers, net during 2015 primarily due to the loss of DISH subscribers. At December 31, 2015, we had 554,000 video customers.

## 2015 REVENUE COMPARED TO 2014

	For the Year Ended December 31,											
	2015				2014							
	Consolidated		Connecticut		Frontier Legacy (excluding Connecticut Operations)		Consolidated		Connecticut		Frontier Legacy (excluding Connecticut Operations)	
(\$ in millions)	Amount	Operations	Amount	Amount	\$ Increase (Decrease)	% Increase (Decrease)	Amount	Operations	Amount	Amount	\$ Increase (Decrease)	% Increase (Decrease)
Voice services	\$ 2,022	\$ 353	\$ 1,669	\$ (208)	(11)%	\$ 1,951	\$ 74	\$ 1,877				
Data and Internet services	2,337	424	1,913	53	3%	1,949	88	1,860				
Video services	285	190	95	-	-	134	39	95				
Other	255	39	216	2	1%	220	6	214				
Customer revenue	4,899	1,006	3,893	(153)	(4)%	4,253	207	4,046				
Switched access and subsidy	677	43	634	124	24%	519	9	510				
Total revenue	\$ 5,576	\$ 1,049	\$ 4,527	\$ (29)	(1)%	\$ 4,772	\$ 216	\$ 4,556				

	For the Year Ended December 31,											
	2015				2014							
	Consolidated		Connecticut		Frontier Legacy (excluding Connecticut Operations)		Consolidated		Connecticut		Frontier Legacy (excluding Connecticut Operations)	
(\$ in millions)	Amount	Operations	Amount	Amount	\$ Increase (Decrease)	% Increase (Decrease)	Amount	Operations	Amount	Amount	\$ Increase (Decrease)	% Increase (Decrease)
Residential	\$ 2,432	\$ 531	\$ 1,901	\$ (75)	(4)%	\$ 2,092	\$ 116	\$ 1,976				
Business	2,467	475	1,992	(78)	(4)%	2,161	91	2,070				
Customer revenue	4,899	1,006	3,893	(153)	(4)%	4,253	207	4,046				
Switched access and subsidy	677	43	634	124	24%	519	9	510				
Total revenue	\$ 5,576	\$ 1,049	\$ 4,527	\$ (29)	(1)%	\$ 4,772	\$ 216	\$ 4,556				

## REVENUE

Consolidated total revenue for 2015 increased \$804 million to \$5,576 million as compared to 2014. Excluding revenues attributable to the Connecticut operations, our total revenue for 2015 decreased \$29 million, or 1%, as compared to 2014. This decline in 2015 is primarily the result of decreases in voice services revenues and lower switched and nonswitched access revenue, partially offset by an increase in data services revenue and subsidy revenue, each as described in more detail below.

Consolidated residential customer revenue for 2015 included \$531 million of revenue attributable to the Connecticut operations. Consolidated residential customer revenue for our Frontier legacy operations declined \$75 million, or

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

4%, as compared with 2014, primarily as a result of decreases in voice services revenue, partially offset by increases in data services revenue.

Consolidated business customer revenue for 2015 included \$475 million of revenue attributable to the Connecticut operations. Consolidated business customer revenue for our Frontier legacy operations declined \$78 million, or 4%, as compared with 2014, principally as a result of decreases in our voice services revenue and wireless backhaul revenue.

Consolidated switched access and subsidy revenue of \$677 million represented 12% of our revenues for 2015. Switched access revenue was \$177 million in 2015, or 3% of our revenues, down from \$201 million, or 4% of our revenues, in 2014. Subsidy revenue was \$500 million in 2015, or 9% of our revenues, which increased from \$319 million, or 7% of our revenues, in 2014.

Voice Services

Voice services revenues for 2015 decreased as compared with 2014, primarily due to \$180 million, or 12%, in lower local and enhanced services revenue. This decrease is primarily due to the continued loss of voice customers and, to a lesser extent, decreases in individual features packages, partially offset by increased local voice charges to residential and business end users. Long distance services revenue decreased \$28 million, or 8%, primarily due to a 10% decrease in minutes of use driven by fewer customers, partially offset by increased cost recovery surcharge rates.

Data and Internet Services

Data and Internet services revenues for 2015 increased as compared with 2014. Nonswitched access revenues decreased \$68 million, or 8%, primarily due to lower monthly recurring revenues for wireless backhaul and other carrier service revenues. These decreases were more than offset by increases in data services revenues of \$121 million, or 12%, primarily due to a 4% increase in the total number of broadband subscribers and higher Frontier Secure revenues.

Video Services

Video services revenue for 2015 remained the same as compared to 2014.

Other

Other revenues for 2015 remained relatively flat primarily due to changes in our provision for bad debts and increased customer premise equipment revenues, offset by lower directory services revenues.

Switched Access and Subsidy

Switched access and subsidy revenue for 2015 increased as compared to 2014. Subsidy revenues increased \$164 million, or 52% in 2015, primarily due to the additional CAF Phase II funding, which increased support by more than \$159 million in 2015. Switched access revenue decreased \$40 million, or 21%, in 2015 primarily due to the impact of a decline in minutes of use related to access line losses and the displacement of minutes of use by wireless and other communications services combined with the lower rates enacted by the FCC's intercarrier compensation reform in July 2013.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

## 2015 OPERATING EXPENSES COMPARED TO 2014

## NETWORK ACCESS EXPENSE

	For the Year Ended December 31,							
	2015					2014		
	Consolidated	Connecticut	Frontier Legacy (excluding Connecticut Operations)			Consolidated	Connecticut	Frontier Legacy (excluding Connecticut Operations)
(\$ in millions)	Amount	Operations	Amount	\$ Increase (Decrease)	% Increase (Decrease)	Amount	Operations	Amount
Network access expenses	\$ 640	\$ 220	\$ 420	\$ (6)	(1)%	\$ 465	\$ 39	\$ 426

Network access expenses for 2015 decreased, primarily due to lower long distance costs as a result of decreased minutes of use and lower pole rental costs, partially offset by an increase in network access expenses related to higher broadband subscriber counts and costs for providing new circuits to our markets.

## NETWORK RELATED EXPENSES

	For the Year Ended December 31,							
	2015					2014		
	Consolidated	Connecticut	Frontier Legacy (excluding Connecticut Operations)			Consolidated	Connecticut	Frontier Legacy (excluding Connecticut Operations)
(\$ in millions)	Amount	Operations	Amount	\$ Increase (Decrease)	% Increase (Decrease)	Amount	Operations	Amount
Network related expenses	\$ 1,287	\$ 182	\$ 1,105	\$ 38	4%	\$ 1,118	\$ 51	\$ 1,067

Network related expenses for 2015 increased due to higher costs for compensation, primarily due to storm-related costs, and certain benefits, including pension and OPEB expense (as discussed below), and increased fleet and facilities costs, partially offset by reduced installation and repair costs.

## SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

	For the Year Ended December 31,							
	2015					2014		
	Consolidated	Connecticut	Frontier Legacy (excluding Connecticut Operations)			Consolidated	Connecticut	Frontier Legacy (excluding Connecticut Operations)
(\$ in millions)	Amount	Operations	Amount	\$ Increase (Decrease)	% Increase (Decrease)	Amount	Operations	Amount
Selling, general and administrative expenses	\$ 1,346	\$ 246	\$ 1,100	\$ 44	4%	\$ 1,056	\$ 30	\$ 1,056

SG&A expenses for 2015 increased due to higher costs for compensation, primarily related to increased employee headcount due to additional services provided by Frontier Secure, and certain benefits, including pension and OPEB expense (as discussed above), partially offset by lower litigation and facilities costs.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Pension and OPEB Costs**

Frontier allocates Pension and OPEB costs to network related expenses and SG&A expenses. Total consolidated pension and OPEB costs for the years ended December 31, 2015 and 2014 were as follows:

(\$ in millions)	For the year ended December 31,	
	2015	2014
Total pension/OPEB expense	\$ 95	\$ 74
Less: capitalized into capital expenditures	(20)	(15)
Net pension/OPEB costs	\$ 75	\$ 59

**DEPRECIATION AND AMORTIZATION**

(\$ in millions)	For the Year Ended December 31,							
	2015				2014			
	Consolidated Amount	Connecticut Operations	Frontier Legacy (excluding Connecticut Operations)		Consolidated Amount	Connecticut Operations	Frontier Legacy (excluding Connecticut Operations)	
		Amount	\$ Increase (Decrease)	% Increase (Decrease)			Amount	
Depreciation expense	\$ 983	\$ 204	\$ 779	\$ (18)	(2) %	\$ 835	\$ 38	\$ 797
Amortization expense	337	97	240	(44)	(15) %	304	20	284
	\$ 1,320	\$ 301	\$ 1,019	\$ (62)	(6) %	\$ 1,139	\$ 58	\$ 1,081

Depreciation and amortization expense for 2015 decreased primarily due to the accelerated method of amortization related to the customer base that was acquired in the 2010 Acquisition with Verizon, changes in the remaining useful lives of certain plant assets and a lower net asset base.

**ACQUISITION AND INTEGRATION COSTS**

(\$ in millions)	For the year ended December 31,						
	2016			2015			2014
	Amount	\$ Increase (Decrease)	% Increase (Decrease)	Amount	\$ Increase (Decrease)	% Increase (Decrease)	Amount
CTF Acquisition	\$ 435	\$ 239	122 %	\$ 196	\$ 196	100 %	\$ -
Connecticut Acquisition	1	(39)	(98) %	40	(102)	(72) %	142
Total acquisition and integration costs	\$ 436	\$ 200	85 %	\$ 236	\$ 94	66 %	\$ 142

Acquisition costs include legal, financial advisory, accounting, regulatory and other related costs. Integration costs include expenses that are incremental and directly related to the acquisition, and were incurred to integrate the network and information technology platforms and to enable other integration initiatives.

We invested \$142 million and \$129 million in capital expenditures related to the CTF Acquisition during the years ended December 31, 2016 and 2015, respectively.

We also invested \$24 million and \$116 million in capital expenditures related to the Connecticut Acquisition during the years ended December 31, 2015 and 2014, respectively.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

## OTHER NON-OPERATING INCOME AND EXPENSE

(\$ in millions)	For the Year Ended December 31,						
	2016			2015			2014
	Amount	\$ Increase (Decrease)	% Increase (Decrease)	Amount	\$ Increase (Decrease)	% Increase (Decrease)	Amount
Investment and other income, net	\$ 20	\$ 13	186 %	\$ 7	\$ (32)	(82) %	\$ 39
Interest expense	\$ 1,531	\$ 418	38 %	\$ 1,113	\$ 417	60 %	\$ 696
Income tax expense (benefit)	\$ (250)	\$ (85)	52 %	\$ (165)	\$ (195)	NM %	\$ 30

NM – Not Meaningful

**Investment and Other Income, Net**

Investment and other income, net for 2016 increased \$13 million for a gain on expiration/settlement of customer advances combined with higher interest and dividend income of \$6 million, primarily due to interest earned on restricted cash during the first quarter of 2016, partially offset by a decrease of \$7 million due to a loss on debt exchanges.

Investment and other income, net for 2015 decreased due to a \$25 million gain on the sale of our minority interest in a wireless partnership and a \$12 million gain on the sale of an intangible asset in 2014, partially offset by higher interest and dividend income of \$5 million in 2015.

**Interest expense**

Interest expense for 2016 increased, primarily due to additional interest of \$755 million in 2016 on the \$6 billion senior notes offering and the \$1,625 million term loan facility related to the CTF Acquisition. We incurred commitment fees of \$10 million and \$184 million for the Verizon Bridge Facility (as defined below) related to the CTF Acquisition during 2016 and 2015, respectively. Our composite average borrowing rate as of December 31, 2016 and 2015 was 8.55% and 8.99%, respectively.

Interest expense for 2015 increased primarily due to interest on the \$6.6 billion senior notes offering completed in September 2015, as well as \$184 million in commitment fees for the Verizon Bridge Facility (as defined below) related to the CTF Acquisition as compared to the commitment fees of \$23 million on the bridge loan facility related to the Connecticut Acquisition during 2014. We also incurred additional interest in 2015 on the \$1,900 million debt financing related to the Connecticut Acquisition.

**Income tax expense (benefit)**

Income tax benefit for 2016 increased compared to 2015, primarily due to the increase in pretax loss. The effective tax rate on our pretax loss for 2016 was 40.2% as compared with 45.8% for 2015. Income taxes for 2016 include the impact of \$36 million of tax benefits resulting primarily from the adjustment of deferred tax balances due to the CTF Acquisition in 2016.

Income tax expense (benefit) for 2015 was an income tax benefit of \$165 million compared to income tax expense of \$30 million for 2014. The change in income tax expense (benefit) was primarily due to the change from pretax income to pretax loss. Our effective tax rate was 45.8% for 2015 compared with 18.7% for 2014. Income taxes for 2015 include the impact of a \$3 million benefit arising from the adjustment of deferred tax balances and a \$5 million benefit from the federal research and development credit.

We received \$120 million in tax refunds in 2016 as compared to net cash taxes paid of \$28 million and \$70 million in 2015 and 2014, respectively.

**Net income (loss) attributable to Frontier common shareholders**

Net income (loss) attributable to Frontier common shareholders for 2016 was a net loss of \$587 million, or \$0.51 per share, as compared to a net loss of \$316 million, or \$0.29 per share, in 2015 and net income of \$133 million, or \$0.13 per share, in 2014.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**(b) Liquidity and Capital Resources****Analysis of Cash Flows**

As of December 31, 2016, we had cash and cash equivalents aggregating \$522 million. Our primary source of funds during 2016 was restricted and unrestricted cash, additional borrowings, along with cash generated from operations. In 2016, we used cash flow from operations, restricted cash, and cash on hand to principally fund all of our cash investing and financing activities, primarily the CTF Acquisition, capital expenditures, dividends, and debt repayments. On April 1, 2016, we used the restricted cash obtained from net proceeds of the September 2015 senior notes offering and June 2015 equity offerings, along with additional borrowings and cash on hand, to finance the CTF Acquisition.

At December 31, 2016, we had a working capital deficit of \$788 million, including \$363 million of long-term debt due within one year, as compared to a working capital surplus of \$8,238 million at December 31, 2015. The decline in working capital is primarily due to a reduction in restricted cash and unrestricted cash and cash equivalents of \$8,858 million, primarily related to funding the CTF Acquisition, and an increase in current liabilities of \$551 million.

**Cash Flows provided by Operating Activities**

Cash flows provided by operating activities increased \$365 million, or 28%, to \$1,666 million in 2016 as compared to 2015. The increase was primarily the result of the addition of our CTF operations, partially offset by unfavorable changes in working capital along with higher interest expense and acquisition and integration costs.

We received \$120 million in tax refunds in 2016 as compared to net cash taxes paid of \$28 million and \$70 million in 2015 and 2014, respectively.

In connection with the CTF Acquisition, Frontier recognized acquisition and integration costs of \$436 million during 2016 compared to \$196 million during 2015. Interest expense of \$755 million was incurred during 2016 related to the September 2015 debt offering and the 2015 Credit Agreement (as defined below) compared to \$189 million in interest expense during 2015. Additionally, Frontier incurred \$10 million of interest expense related to the Verizon Bridge Facility in 2016 compared to \$184 million during 2015.

In connection with the Connecticut Acquisition, Frontier recognized \$40 million and \$142 million of acquisition and integration costs incurred in 2015 and 2014, respectively, and \$23 million of interest expense in 2014, in connection with the bridge loan facility related to the Connecticut Acquisition.

**Cash Flows used by Investing Activities****Capital Expenditures**

In 2016, 2015 and 2014, our capital expenditures were, respectively, \$1,401 million, \$863 million and \$688 million (including \$142 million, \$153 million and \$116 million of integration-related capital expenditures in 2016, 2015 and 2014, respectively, associated with the CTF Acquisition and the Connecticut Acquisition). Frontier received a total of \$133 million during the 2012-2014 period from the Connect America Fund (CAF) Phase I Program to support broadband deployment in unserved and underserved high-cost areas. In addition to the capital expenditures mentioned above, network expansion funded by the previously received CAF Phase I funds amounted to \$22 million and \$56 million in 2015 and 2014, respectively. Capital expenditures related to CAF Phase II are included in our reported amounts for capital expenditures. We anticipate capital expenditures for business operations to be approximately \$1.00 billion to \$1.25 billion in 2017, as compared to \$1,259 million in 2016.

**CTF Acquisition**

On April 1, 2016, Frontier acquired the wireline operations of Verizon in California, Texas and Florida for a purchase price of \$10,540 million in cash and assumed debt (the CTF Acquisition), pursuant to the February 5, 2015 Securities Purchase Agreement, as amended. In addition, Frontier and Verizon settled the working capital and net debt adjustments with \$15 million paid to Frontier in October 2016.

**Connecticut Acquisition**

On October 24, 2014, Frontier acquired the wireline properties of AT&T in Connecticut. After including the working capital adjustment payment of \$18 million, the total purchase price for the Connecticut Acquisition was \$2,018 million.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Cash Flows used by and provided from Financing ActivitiesDebt Financings

Refer to the below discussion under Capital Resources – Term Loan Facilities.

Financing the CTF Acquisition

On September 25, 2015, Frontier completed a private offering of \$6,600 million aggregate principal amount of senior unsecured notes, as follows: \$1,000 million of 8.875% Senior Notes due 2020; \$2,000 million of 10.50% Senior Notes due 2022; and \$3,600 million of 11.00% Senior Notes due 2025. Each was issued at a price equal to 100% of its principal amount. Frontier used the net proceeds from the offering (after deducting underwriting fees) to finance a portion of the cash consideration paid in connection with the CTF Acquisition and to pay related fees and expenses. The net proceeds of the debt offering of \$6,485 million were included in "Restricted cash" in the consolidated balance sheet as of December 31, 2015. In April 2016, we completed an exchange offer of registered senior notes for the privately placed senior notes.

Financing the Connecticut Acquisition

On September 17, 2014, Frontier completed a registered debt offering of \$775 million aggregate principal amount of 6.25% Senior Notes due 2021 and \$775 million aggregate principal amount of 6.875% Senior Notes due 2025. We received net proceeds, after deducting underwriting fees, of \$1,519 million from the offering. Frontier used the net proceeds from the offering of the notes, together with borrowings of \$350 million under the 2014 CoBank Credit Agreement, as defined below, and cash on hand to finance the Connecticut Acquisition, which closed on October 24, 2014.

During 2015 and 2014, we also entered into secured financings totaling \$3 million and \$11 million, respectively, with four year terms and no stated interest rate for certain equipment purchases.

Debt Reduction

During 2016, 2015 and 2014, we retired an aggregate principal amount of \$453 million, \$298 million and \$260 million, respectively, of debt consisting of \$23 million, \$295 million and \$257 million, respectively, of senior unsecured debt and \$1 million during 2015 and 2014, of rural utilities service loan contracts. Additionally, we retired \$430 million, \$3 million and \$2 million of secured debt during 2016, 2015 and 2014, respectively.

Additionally, during 2016 we completed non-cash debt exchanges including related accrued interest, of \$397 million of our 8.25% Notes due April 2017 for approximately \$147 million of our 8.50% Notes due April 2020, \$66 million of our 8.875% Notes due September 2020 and \$188 million of our 10.50% Notes due September 2022. A pre-tax loss of approximately \$7 million was recognized and included in "Investment and other income, net" in our consolidated statement of operations for the year ended December 31, 2016.

Subject to limitations contained in our indentures and credit facilities, we may from time to time make repurchases of our debt in the open market, through tender offers, by exercising rights to call or in privately negotiated transactions. We may also refinance existing debt or exchange existing debt for newly issued debt obligations.

Common Stock Offering

On June 10, 2015, we completed a registered offering of 150,000,000 shares of our common stock, par value \$0.25 per share, at an offering price of \$5 per share. On June 24, 2015, Frontier issued an additional 15,000,000 shares of common stock in connection with the over-allotment option that was exercised in full by the underwriters. Aggregate net proceeds were approximately \$799 million after deducting commissions and expenses. We used the net proceeds from this offering to fund a portion of the acquisition price of the CTF Acquisition and for related fees and expenses.

Mandatory Convertible Preferred Stock (Series A) Offering

On June 10, 2015, we also completed a registered offering of 17,500,000 shares of our 11.125% Mandatory Convertible Preferred Stock, Series A, par value \$0.01 per share (the "Series A Preferred Stock"), at an offering price of \$100 per share. On June 24, 2015, Frontier issued an additional 1,750,000 shares of Series A Preferred Stock in connection with the over-allotment option that was exercised in full by the underwriters. Aggregate net proceeds of the offering were \$1,866 million after deducting commissions and expenses. We used the net proceeds from this offering to fund a portion of the acquisition price of the CTF Acquisition and for related fees and expenses.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Capital Resources**

We believe our operating cash flows, existing cash balances, existing revolving credit facility and access to the capital markets, as necessary, will be adequate to finance our working capital requirements, fund capital expenditures, make required debt interest and principal payments, pay taxes, pay dividends to our stockholders, and support our short-term and long-term operating strategies for the next twelve months. A number of factors, including but not limited to, losses of customers, pricing pressure from increased competition, lower subsidy and switched access revenues, and the impact of economic conditions may negatively affect our cash generated from operations. As of December 31, 2016, we had \$363 million and \$733 million of debt maturing in 2017 and 2018, respectively.

**Bridge Facilities**

On February 5, 2015, we entered into a commitment for a bridge loan facility (the Verizon Bridge Facility) and recognized related interest expense of \$10 million and \$184 million for the years ended December 31, 2016 and 2015, respectively. The Verizon Bridge Facility terminated in accordance with its terms on September 25, 2015.

On December 16, 2013, we signed a commitment letter for a bridge loan facility (the Connecticut Bridge Facility) to finance the Connecticut Acquisition and recognized interest expense related to this commitment of \$23 million during the year ended December 31, 2014. The Connecticut Bridge Facility terminated in accordance with its terms on September 17, 2014.

**Term Loan Facilities**

Borrowings under each of Frontier's term loan credit agreements are secured by a pledge of the stock of Frontier North Inc., a wholly owned subsidiary, primarily representing Frontier operations in Illinois, Indiana, Michigan, Ohio, and Wisconsin.

On August 12, 2015, Frontier entered into a credit agreement with JPMorgan Chase Bank, N.A., as administrative agent, and the lenders party thereto, for a \$1,500 million senior secured delayed-draw term loan facility (the 2015 Credit Agreement). Frontier exercised its right under the 2015 Credit Agreement to obtain additional commitments and increased the size of the facility to \$1,625 million. On April 1, 2016, in connection with the closing of the CTF Acquisition, Frontier drew \$1,550 million under that facility, with the additional \$75 million drawn subsequently. The final maturity date is March 31, 2021. Repayment of the outstanding principal balance will be made in quarterly installments, initially in the amount of \$20 million per installment, which commenced on June 30, 2016. The quarterly installments will increase to \$41 million, beginning with the 13th quarterly installment. The remaining outstanding principal balance will be repaid on the final maturity date. Borrowings under the term loan will bear interest based on margins over the Base Rate (as defined in the 2015 Credit Agreement) or LIBOR, at the election of Frontier. Interest rate margins under the facility (ranging from 0.75% to 1.75% for Base Rate borrowings and 1.75% to 2.75% for LIBOR borrowings) are subject to adjustment based on Frontier's Total Leverage Ratio (as defined in the 2015 Credit Agreement).

Frontier has a credit agreement with CoBank, ACB, as administrative agent, lead arranger and a lender, and the other lenders party thereto, for a \$350 million senior unsecured term loan facility (the 2014 CoBank Credit Agreement). The facility was drawn upon closing of the Connecticut Acquisition with proceeds used to partially finance the acquisition. The maturity date is October 24, 2019. Repayment of the outstanding principal balance will be made in quarterly installments of \$9 million, which commenced on March 31, 2015 with the remaining outstanding principal balance to be repaid on the maturity date. Borrowings under the 2014 CoBank Credit Agreement will bear interest based on the margins over the Base Rate (as defined in the 2014 CoBank Credit Agreement) or LIBOR, at the election of Frontier. Interest rate margins under the facility (ranging from 0.875% to 2.875% for Base Rate borrowings and 1.875% to 3.875% for LIBOR borrowings) are subject to adjustments based on our Total Leverage Ratio, as such term is defined in the 2014 CoBank Credit Agreement. The interest rate on this facility at December 31, 2016 was LIBOR plus 3.375%.

Frontier has two senior secured credit agreements with CoBank, ACB, as administrative agent, lead arranger and a lender, and the other lenders party thereto: the first, for a \$350 million senior term loan facility drawn in 2014 (the 2014 CoBank Credit Agreement), matures on October 24, 2019, and the second, for a \$315 million senior term loan facility drawn in October 2016 (the 2016 CoBank Credit Agreement), matures on October 12, 2021. We refer to the 2014 CoBank Credit Agreement and the 2016 CoBank Credit Agreement collectively as the CoBank Credit Agreements.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Repayment of the outstanding principal balance under each of the CoBank Credit Agreements is being made in quarterly installments (\$9 million, with respect to the 2014 CoBank Credit Agreement, and \$8 million, with respect to the 2016 CoBank Credit Agreement), in each case with the remaining outstanding principal balance to be repaid on the applicable maturity date. Borrowings under each of the CoBank Credit Agreements bear interest based on the margins over the Base Rate (as defined in the applicable CoBank Credit Agreement) or LIBOR, at the election of Frontier. Interest rate margins under the facilities (ranging from 0.875% to 2.875% for Base Rate borrowings and 1.875% to 3.875% for LIBOR borrowings) are subject to adjustments based on our Total Leverage Ratio, as such term is defined in the applicable CoBank Credit Agreement. The interest rate on these facilities at December 31, 2016 was LIBOR plus 3.375%.

**Revolving Credit Facility**

Borrowings under Frontier's Revolving Credit Agreement are secured by a pledge of the stock of Frontier North Inc.

Frontier has a revolving credit agreement with JPMorgan Chase Bank, N.A., as administrative agent, the lenders party thereto and the other parties named therein (the Revolving Credit Agreement), for a \$750 million revolving credit facility (the Revolving Credit Facility) with a scheduled termination date of May 31, 2018. As of December 31, 2016, the Revolving Credit Facility was fully available and no borrowings had been made thereunder. Associated commitment fees under the Revolving Credit Facility will vary from time to time depending on our debt rating (as defined in the Revolving Credit Agreement) and were 0.45% per annum as of December 31, 2016. During the term of the Revolving Credit Facility, Frontier may borrow, repay and reborrow funds, and may obtain letters of credit, subject to customary borrowing conditions. Loans under the Revolving Credit Facility will bear interest based on the alternate base rate or the adjusted LIBO Rate (each as determined in the Revolving Credit Agreement), at our election, plus a margin based on our debt rating (ranging from 0.50% to 1.50% for alternate base rate borrowings and 1.50% to 2.50% for adjusted LIBO Rate borrowings). The interest rate on this facility would have been the alternate base rate plus 1.50% or the adjusted LIBO Rate plus 2.50%, respectively, as of December 31, 2016. Letters of credit issued under the Revolving Credit Facility will also be subject to fees that vary depending on our debt rating. The Revolving Credit Facility is available for general corporate purposes but may not be used to fund dividend payments.

On February 27, 2017, Frontier amended and restated its April 2011 term loan and its revolving credit facility, combining them into a single credit agreement and unifying the covenants. The amended and restated credit agreement provides Frontier with more flexible terms, increases the revolving credit facility to \$850 million and extends the maturity of the revolving credit facility from 2018 to 2022. The determination of interest rates remains unchanged. The most significant change in the covenants is an increase of the maximum Leverage Ratio (as defined) to 5.25 to 1.0 initially, migrating to 5.0 to 1.0 beginning in the second quarter of 2018, 4.75 to 1.0 in the second quarter of 2019, and 4.5 to 1.0 in the second quarter of 2020. In addition, under the amended and restated credit agreement, Frontier will be expanding the security package to include pledges of the equity interests in certain Frontier subsidiaries and guaranties by certain Frontier subsidiaries.

**Letters of Credit Facility**

Frontier has a Continuing Agreement for Standby Letters of Credit with Deutsche Bank AG New York Branch (the LC Agreement). As of December 31, 2016, \$105 million of undrawn Standby Letters of Credit had been issued under the LC Agreement. Borrowings under the LC Agreement are secured by a pledge of Frontier North Inc.

**Covenants**

The terms and conditions contained in our indentures, the CoBank Credit Agreements, the 2015 Credit Agreement and the Revolving Credit Agreement include the timely payment of principal and interest when due, the maintenance of our corporate existence, keeping proper books and records in accordance with GAAP, restrictions on the incurrence of liens on our assets securing indebtedness and our subsidiaries' assets, restrictions on the incurrence of indebtedness by our subsidiaries and restrictions on asset sales and transfers, mergers and other changes in corporate control subject to important qualifications and exceptions. We would be restricted from declaring dividends by the CoBank Credit Agreements, the 2015 Credit Agreement and the Revolving Credit Agreement if an event of default occurred and was continuing at the time or would result from the dividend declaration. In addition, under the Certificate of Designations of our 11.125% Mandatory Convertible Preferred Stock, Series A, we would be restricted from paying dividends on our common stock if we failed to declare and pay dividends on our Series A Preferred Stock.

The CoBank Credit Agreements, the 2015 Credit Agreement, and the Revolving Credit Agreement each contain a maximum leverage ratio covenant. Under those covenants, we are required to maintain a ratio of (i) total

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

indebtedness minus cash and cash equivalents in excess of \$50 million to (ii) consolidated adjusted EBITDA (as each such term is defined in the agreements) over the last four quarters not to exceed 4.50 to 1.

Indentures for our senior unsecured debt obligations limit our ability to create liens on our assets securing indebtedness and our subsidiaries' assets or merge or consolidate with other companies, our subsidiaries' ability to borrow funds and to engage in change of control transactions, subject to important exceptions and qualifications. The indentures for our 8.875% Senior Notes due 2020, our 10.50% Senior Notes due 2022, and our 11.00% Senior Notes due 2025 contain covenants that are customary for similarly rated issuers. Among other things, these covenants limit our ability to incur additional indebtedness if our leverage ratio exceeds 4.5 to 1 (as defined in the indentures), limits liens and subsidiary debt to 1.25 times EBITDA (as defined in the indentures), limits cumulative restricted payments, including dividends, to cumulative EBITDA less 1.4 times cumulative interest expense (as defined in the indentures), if our leverage ratio does not exceed 4 to 1, and limits cumulative restricted payments, including dividends, to a lesser amount during periods, if any, in which our leverage ratio exceeds 4 to 1, and restricts our ability to divest substantially all of the assets of Frontier.

As of December 31, 2016, we were in compliance with all of our indenture and credit facility covenants.

**Dividends**

We intend to continue to pay regular quarterly dividends on our common and preferred stock. Our ability to fund a regular quarterly dividend will be impacted by our ability to generate cash from operations. Holders of the Series A Preferred Stock are entitled to receive cumulative dividends at an annual rate of 11.125% of the initial liquidation preference of \$100 per share, or \$11.125 per year per share. Series A Preferred Stock dividends of \$214 million and \$120 million were paid during 2016 and 2015, respectively.

The declaration and payment of future dividends on our common stock is at the discretion of our Board of Directors, and will depend upon many factors, including our financial condition, results of operations, growth prospects, funding requirements, payment of cumulative dividends on Series A Preferred Stock, applicable law, restrictions in agreements governing our indebtedness and other factors our Board of Directors deem relevant.

**Off-Balance Sheet Arrangements**

We do not maintain any off-balance sheet arrangements, transactions, obligations or other relationships with unconsolidated entities that would be expected to have a material current or future effect upon our financial statements.

**Future Contractual Obligations and Commitments**

A summary of our future contractual obligations and commercial commitments as of December 31, 2016 is as follows:

(\$ in millions)	Total	Payments due by period					Thereafter
		2017	2018	2019	2020	2021	
Long-term debt obligations, excluding interest	\$ 18,178	\$ 363	\$ 733	\$ 818	\$ 2,429	\$ 2,554	\$ 11,281
Interest on long-term debt	11,263	1,533	1,527	1,465	1,378	1,146	4,214
Operating lease obligations	247	91	18	18	23	21	76
Capital lease obligations	147	39	37	26	15	9	21
Financing lease obligations	105	9	9	9	9	9	60
Purchase obligations	108	42	41	7	6	2	10
Liability for uncertain tax positions	17	8	3	3	3	-	-
Total	\$ 30,085	\$ 2,085	\$ 2,368	\$ 2,346	\$ 3,863	\$ 3,741	\$ 15,662

During 2016, we increased our outstanding performance letters of credit from \$50 million to \$125 million at December 31, 2016.

On April 29, 2015, the FCC released its right of first refusal offer of support to price cap carriers under the CAF Phase II program, which is intended to provide long-term support for broadband in high-cost unserved or underserved areas. In June 2015, Frontier accepted the CAF Phase II offer, which provides for \$332 million in annual support, including \$49 million in annual support related to the properties acquired in the CTF Acquisition,

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

through 2020 to make available 10 Mbps downstream/1 Mbps upstream broadband service to approximately 774,000 households across certain of the 29 states where we now operate.

To the extent we do not enable the required number of households with 10 Mbps downstream/1 Mbps upstream broadband service by the end of the CAF Phase II term, we will be required to return a portion of the funds previously received.

**Critical Accounting Policies and Estimates**

The preparation of our financial statements requires management to make estimates and assumptions. There are inherent uncertainties with respect to such estimates and assumptions; accordingly, it is possible that actual results could differ from those estimates and changes to estimates could occur in the near term. The estimates which require the most significant judgment are listed below.

These critical accounting estimates have been reviewed with our independent registered public accounting firm and with the Audit Committee of our Board of Directors. For a discussion of these and other accounting policies, see Note 1 of the Notes to Consolidated Financial Statements.

**Allowance for Doubtful Accounts**

We maintain an allowance for doubtful accounts based on our estimate of our ability to collect accounts receivable. Our estimates are based on assumptions and other considerations, including payment history, customer financial performance, carrier billing disputes and aging analysis. Our estimation process includes general and specific reserves and varies by customer category. In 2016 and 2015, we had no "critical estimates" related to bankruptcies of communications companies or any other significant customers. See Notes 1 and 4 of the Notes to Consolidated Financial Statements for additional discussion.

**Indefinite-lived Intangibles**

Our indefinite-lived intangibles consist of goodwill and trade name, which were generated as a result of business combinations. We test for impairment of these assets annually as of December 31, or more frequently, whenever events occur or facts and circumstances change that would more likely than not reduce the fair value of an operating segment below its carrying amount. Events that might indicate impairment include, but are not limited to, strategic decisions made in response to economic and competitive conditions, the impact of the economic environment on our customer base, material negative changes in relationships with significant customers, and/or a significant decline in our stock price for a sustained period.

We perform the two-step goodwill impairment test to identify potential goodwill impairment and measure the amount of a goodwill impairment loss to be recognized, if any. The first step in the goodwill impairment test compares the carrying value of net assets of the operating segment to its fair value. If the fair value exceeds the carrying value, no further testing is required. However, if the fair value is less than the carrying value, an indication of impairment exists and a second step is performed. These tests are performed at the reporting unit level, which at December 31, 2016, was our seven regional operating segments. In early 2017, we will evaluate changes to the management reporting that our chief operating decision makers review from this regional construct to a functional construct including consumer, commercial, operations and engineering, which may lead to different operating segments.

We use a market multiples approach to determine fair value. Marketplace company comparisons and analyst reports have historically supported a range of fair values of multiples between 5.0x and 7.9x annualized EBITDA. For the purpose of the goodwill impairment test we define 2016 EBITDA as operating income, net of acquisition and integration costs, non-cash pension and OPEB costs, and restructuring costs and other charges, plus depreciation and amortization. We estimated the enterprise fair value using a multiple of 5.8x EBITDA. Once determined, this estimate of enterprise fair value is then allocated to the operating segments based upon each unit's relative share of consolidated EBITDA. The result of this first step indicated that fair values of each operating segment exceed their carrying values. As a result, the second step of the goodwill impairment test was not required. As an additional step to corroborate the results of the first step of the impairment test, we complete a reconciliation of our market capitalization and overall enterprise value to the fair value of all of our operating segments.

The enterprise fair value is sensitive to the amount of EBITDA generated by Frontier and the EBITDA multiple used in the calculation. Significant changes in the assumptions or estimates used in our impairment analyses, such as a reduction in profitability and/or cash flows, could result in a non-cash goodwill and indefinite-lived intangible asset impairment charge and materially affect our operating results. If the assumptions for either of our EBITDA or EBITDA multiple were to decrease by 10% there would be an indication of impairment. Declines in our stock price

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

could also affect the reconciliation of our market capitalization and overall enterprise value to the fair value of all of our operating segments and indicate impairment. For more information on goodwill, see Note 6 of the Notes to Consolidated Financial Statements.

*Depreciation and Amortization*

The calculation of depreciation and amortization expense is based upon the estimated useful lives of the underlying property, plant and equipment and identifiable finite-lived intangible assets. Depreciation expense is principally based on the composite group method for substantially all of our property, plant and equipment assets. The estimates for remaining lives of the various asset categories are determined annually, based on an independent study. Among other considerations, these studies include models that consider actual usage, replacement history and assumptions about technology evolution for each category of asset. The latest study was completed in the fourth quarter of 2016 and did not result in any significant changes in remaining lives for any of our asset categories. A one year decrease in the estimated useful lives of our property, plant and equipment would result in an increase of approximately \$157 million to depreciation expense.

Our finite-lived intangibles consist principally of customer base; \$2,428 million from the 2010 Acquisition, \$570 million from the Connecticut Acquisition and \$2,090 million from the recently completed CTF Acquisition. These customer bases are being amortized on an accelerated method because this method most closely resembles the projected underlying revenue streams. In assigning lives, which range from between eight and 12 years, a separate evaluation and determination is made for residential and business customers.

See Notes 5 and 6 of the Notes to Consolidated Financial Statements for additional discussion.

*Asset Impairments*

We review long-lived assets to be held and used, including customer lists and long-lived assets to be disposed of for impairment at least annually or whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Recoverability of assets to be held and used is measured by comparing the carrying amount of the asset to the estimated fair value, which is based on the future undiscounted net cash flows expected to be generated by the asset. Recoverability of assets held for sale is measured by comparing the carrying amount of the assets to their estimated fair market value. If any assets are considered to be impaired, the impairment is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value. Also, we periodically reassess the useful lives of our tangible and intangible assets to determine whether any changes are required.

*Pension and Other Postretirement Benefits*

We sponsor a defined benefit pension plan covering a significant number of our current and former employees as well as other postretirement benefit plans that provide medical, dental, life insurance and other benefits for covered retired employees and their beneficiaries and covered dependents. As of December 31, 2016, the unfunded benefit obligation for these plans recorded on our consolidated balance sheet was \$1,625 million. During 2016, we contributed \$28 million to these plans and recorded \$155 million of expense before capitalization, including \$26 million of special termination benefits. Pension and other postretirement benefit costs and obligations are dependent upon various actuarial assumptions, the most significant of which are the discount rate and the expected long-term rate of return on plan assets.

Our discount rate assumption is determined annually with assistance from our actuaries based on the pattern of expected future benefit payments and the prevailing rates available on long-term, high quality corporate bonds with durations approximate to that of our benefit obligation. As of December 31, 2016 and 2015, we utilized an estimation technique that is based upon a settlement model (Bond:Link) that permits us to closely match cash flows to the expected payments to participants. This rate can change from year-to-year based on market conditions that affect corporate bond yields.

We are utilizing a discount rate of 4.10% as of December 31, 2016 for our qualified pension plan, compared to rates of 4.50% and 4.10% in 2015 and 2014, respectively. The discount rate for postretirement plans as of December 31, 2016 was a range of 4.10% to 4.30% compared to a range of 4.50% to 4.70% in 2015 and 4.10% to 4.20% in 2014.

In the following table, we show the estimated sensitivity of our pension and other postretirement benefit plan liabilities to a 25 basis point change in the discount rate as of December 31, 2016:

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

<i>(\$ in millions)</i>	Increase in Discount Rate of 25 bps	Decrease in Discount Rate of 25 bps
Pension plans		
Projected benefit obligation	\$ (81)	\$ 84
Other postretirement plans		
Accumulated postretirement benefit obligation	\$ (33)	\$ 34

In developing the expected long-term rate of return assumption, we considered published surveys of expected market returns, 10 and 20 year actual returns of various major indices, and our own historical 5 year, 10 year and 20 year investment returns. The expected long-term rate of return on plan assets is based on an asset allocation assumption of 40% in long-duration fixed income securities, and 60% in equity securities and other investments. We review our asset allocation at least annually and make changes when considered appropriate. Our asset return assumption is made at the beginning of our fiscal year. In 2016, 2015 and 2014, our expected long-term rate of return on plan assets was 7.50%, 7.75% and 7.75%, respectively. Our actual return on plan assets in 2016 was 10.39%. For 2017, we will assume a rate of return of 7.50%. Our pension plan assets are valued at fair value as of the measurement date.

For additional information regarding our pension and other postretirement benefits see Note 17 to the Notes to Consolidated Financial Statements.

**Income Taxes**

We file a consolidated federal income tax return. We utilize the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred income taxes are recorded for the tax effect of temporary differences between the financial statement basis and the tax basis of assets and liabilities using tax rates expected to be in effect when the temporary differences are expected to reverse. Actual income taxes could vary from these estimates due to future changes in governing law or review by taxing authorities.

We use a "more likely than not" threshold to the recognition and derecognition of uncertain tax positions either taken or expected to be taken in Frontier's income tax returns. The total amount of our gross tax liability for tax positions that may not be sustained under a "more likely than not" threshold amounts to \$17 million as of December 31, 2016 including interest of \$1 million. For additional information regarding our accounting for income taxes see Note 12 of the Notes to Consolidated Financial Statements.

**Business Combinations**

We allocate the total cost of an acquisition to the underlying net assets based on their respective estimated fair values. As part of this allocation process, we identify and attribute values and estimated lives to the intangible assets acquired. These determinations involve significant estimates and assumptions about several highly subjective variables, including future cash flows, discount rates, and asset lives. There are also different valuation models for each component, the selection of which requires considerable judgment. Our estimates and assumptions may be based, in part, on the availability of listed market prices or other transparent market data. These determinations will affect the amount of amortization expense recognized in future periods. We base our fair value estimates on assumptions we believe are reasonable, but recognize that the assumptions are inherently uncertain. Depending on the size of the purchase price of a particular acquisition and the mix of intangible assets acquired, the purchase price allocation could be materially impacted by applying a different set of assumptions and estimates. Frontier allocated \$9,871 million and \$2,018 million in total consideration to the "fair market value" of the assets and liabilities acquired in the CTF Acquisition and the Connecticut Acquisition, respectively. The estimates of the fair values assigned to property, plant and equipment, customer list and goodwill, are more fully described in Note 3 of the Notes to Consolidated Financial Statements.

**Recent Accounting Pronouncements**

See Note 2 of the Notes to Consolidated Financial Statements included in Part IV of this report for additional information related to recent accounting pronouncements.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Item 7A. Quantitative and Qualitative Disclosures about Market Risk**

We are exposed to market risk in the normal course of our business operations due to ongoing investing and funding activities, including those associated with our pension plan assets. Market risk refers to the potential change in fair value of a financial instrument as a result of fluctuations in interest rates and equity prices. We do not hold or issue derivative instruments, derivative commodity instruments or other financial instruments for trading purposes. As a result, we do not undertake any specific actions to cover our exposure to market risks, and we are not party to any market risk management agreements other than in the normal course of business. Our primary market risk exposures from interest rate risk and equity price risk are as follows:

**Interest Rate Exposure**

Our exposure to market risk for changes in interest rates relates primarily to the interest-bearing portion of our pension investment portfolio and the related actuarial liability for pension obligations, as well as our floating rate indebtedness. As of December 31, 2016, 88% of our long-term debt had fixed interest rates. We had no interest rate swap agreements related to our fixed rate debt in effect at December 31, 2016 and 2015. We believe that our currently outstanding obligation exposure to interest rate changes is minimal.

Our objectives in managing our interest rate risk are to limit the impact of interest rate changes on earnings and cash flows and to lower our overall borrowing costs. To achieve these objectives, only \$2,151 million of our outstanding borrowings at December 31, 2016 have floating interest rates. Our undrawn \$750 million revolving credit facility has interest rates that float with the LIBO Rate, as defined. Consequently, we have limited material future earnings or cash flow exposures from changes in interest rates on our debt. An adverse change in interest rates would increase the amount that we pay on our variable rate obligations and could result in fluctuations in the fair value of our fixed rate obligations. Based upon our overall interest rate exposure at December 31, 2016, a near-term change in interest rates would not materially affect our consolidated financial position, results of operations or cash flows.

At December 31, 2016, the fair value of our long-term debt was estimated to be approximately \$17.5 billion, based on prevailing interest rates, our overall weighted average borrowing rate of 8.55% and our overall weighted average maturity of approximately eight years. As of December 31, 2016, there has been no significant change in the weighted average maturity applicable to our obligations since December 31, 2015.

**Equity Price Exposure**

Our exposure to market risks for changes in equity security prices as of December 31, 2016 is limited to our pension plan assets. We have no other security investments of any significant amount.

Our pension plan assets increased from \$1,572 million at December 31, 2015 to \$2,766 million at December 31, 2016, an increase of \$1,194 million, or 76%. This increase was a result of cash transfers and accounts receivable from Verizon and the Verizon pension plan trusts of \$1,125 million related to the CTF Acquisition, positive investment returns of \$195 million, net of investment management and administrative fees, and contributions of \$28 million, partially offset by benefit payments of \$154 million.

**Item 8. Financial Statements and Supplementary Data**

The following documents are filed as part of this Report:

1. Financial Statements - See Index on page F-1.
2. Supplementary Data - Quarterly Financial Data is included in the Financial Statements (see 1. above).

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**Item 9A. Controls and Procedures****(i) Evaluation of Disclosure Controls and Procedures**

We carried out an evaluation, under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, regarding the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended). Based upon this evaluation, our principal executive officer and principal financial officer concluded, as of the end of the period covered by this report, December 31, 2016, that our disclosure controls and procedures were effective.

**(ii) Internal Control Over Financial Reporting****(a) Management's annual report on internal control over financial reporting**

Our management report on internal control over financial reporting appears on page F-2.

**(b) Report of registered public accounting firm**

The report of KPMG LLP, our independent registered public accounting firm, on internal control over financial reporting appears on page F-4.

**(c) Changes in internal control over financial reporting**

We reviewed our internal control over financial reporting at December 31, 2016. There have been no changes in our internal control over financial reporting identified in an evaluation thereof that occurred during the last fiscal quarter of 2016 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Item 9B. Other Information**

None.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

**PART III****Item 10. Directors, Executive Officers and Corporate Governance**

Certain of the information required by this Item is incorporated by reference from our definitive proxy statement for the 2017 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2016.

**Executive Officers of the Registrant**

Our Executive Officers as of February 10, 2017 were:

<u>Name</u>	<u>Age</u>	<u>Current Position and Officer</u>
Kenneth A. Arndt	52	Executive Vice President, Commercial Sales Operations
Donald Daniels	49	Senior Vice President and Controller
Steve Gable	43	Executive Vice President and Chief Technology Officer
John J. Lass	60	Executive Vice President, Customer Operations
R. Perley McBride	51	Executive Vice President and Chief Financial Officer
Daniel J. McCarthy	52	President and Chief Executive Officer and a Director
Cecilia K. McKenney	54	Executive Vice President and Chief Customer Officer
Mark D. Nielsen	52	Executive Vice President and Chief Legal Officer
Tim Travaille	59	Executive Vice President, Operational Transformation
Kathleen Weslock	61	Executive Vice President and Chief People Officer

There is no family relationship between the directors or executive officers. The term of office of each of the foregoing officers of Frontier is annual and will continue until a successor (if any) has been elected and qualified.

KENNETH A. ARNDT has been with Frontier since 2003 and was appointed Executive Vice President, Commercial Sales Operations, in December 2016. Mr. Arndt previously had oversight of Frontier's operations in Connecticut, New York, Ohio, Pennsylvania and West Virginia. Before joining Frontier, Mr. Arndt served as Vice President of Marketing for Lucent Technologies and Vice President of Sales and Marketing for Commonwealth Telephone Company in Pennsylvania.

DONALD DANIELS joined Frontier in July 2014 as Senior Vice President and Controller. From October 2002 to July 2014 he held various positions with JetBlue Airways Corporation, including Corporate Controller, Chief Accounting Officer, Vice President and Controller, Assistant Controller, and Director of Financial Reporting. Prior to that Mr. Daniels held various positions of increasing responsibility at Delta Air Lines and Deloitte and Touche, LLP. Mr. Daniels is a veteran of the United States Army and a certified public accountant.

STEVE GABLE became Executive Vice President and Chief Technology Officer of Frontier in April 2015. He joined Frontier in November 2012 as Senior Vice President and Chief Information Officer. Prior to Frontier, Mr. Gable was Executive Vice President/CTO of Tribune Company while also serving as President of Tribune Digital. Before Tribune, Mr. Gable served as Vice President of Technology for Clear Channel Radio.

JOHN J. LASS has been with Frontier since 1980 and was appointed Executive Vice President, Customer Operations, in November 2016. Previously, Mr. Lass was Executive Vice President, Field Operations. He has also served as President of Frontier's Central Region (comprising Illinois, Indiana, Iowa, Michigan, Minnesota and Nebraska), Vice President of Revenue Assurance and as Regional Operations Vice President at Frontier, Vice President and General Manager of Citizens Utilities Vermont Electric Division, and has held operations positions in New York and the Midwest with Frontier, GTE and Contel.

R. PERLEY MCBRIDE became Chief Financial Officer and Executive Vice President of Frontier on November 4, 2016. Prior to joining Frontier, Mr. McBride was the Chief Financial Officer of Cable & Wireless Communications Plc until its May 2016 acquisition by Liberty Global plc. Previously, Mr. McBride served as Chief Financial Officer at Leap Wireless International from December 2012 through May 2014 and was part of the Executive team that led the business through its acquisition by AT&T Inc. Prior to Leap Wireless, he served as Executive Vice President of Finance at The Weather Company, owner of The Weather Channel among other assets, between 2010 and 2012. He also served in several senior financial management roles at Frontier between 1999 and 2010, and also between 1994 and 1997.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

DANIEL J. MCCARTHY has been with Frontier since December 1990 and is the President and Chief Executive Officer. Prior to becoming President and Chief Executive Officer in April 2015, Mr. McCarthy held other positions of responsibility at Frontier, including President and Chief Operating Officer, from April 2012 to April 2015, Executive Vice President and Chief Operating Officer, from January 2006 to April 2012, and Senior Vice President, Field Operations, from December 2004 to December 2005. Mr. McCarthy serves as a Trustee of Sacred Heart University in Fairfield, Connecticut, and of Foundations in Education for the Diocese of Bridgeport, Connecticut. He is a member of the Board of Directors of the Western Connecticut Health Network, the Board of Directors of the Business Council of Fairfield County, and a member of the Business Roundtable. He is also a director of Constellation Brands, Inc.

CECILIA K. MCKENNEY has been with Frontier since February 2006. She is currently Executive Vice President and Chief Customer Officer. Before this, she was Executive Vice President, Frontier Secure and Administration. Previously, she was Executive Vice President, Human Resources and Sales Operations from May 2012 to January 2013, Executive Vice President, Human Resources and Call Center Sales & Service from February 2008 to May 2012 and Senior Vice President, Human Resources from February 2006 to February 2008. Prior to joining Frontier, she was Group Vice President, Headquarters Human Resources, of The Pepsi Bottling Group (PBG) from 2004 to 2005. Previously at PBG Ms. McKenney was Vice President, Headquarters Human Resources from 2000 to 2004.

MARK D. NIELSEN joined Frontier in March 2014 and is Executive Vice President and Chief Legal Officer. Prior to joining Frontier, he was Associate General Counsel and Chief Compliance Officer for Praxair Inc. and Vice President and Assistant General Counsel of Raytheon Company. Before that, Mr. Nielsen served as Chief Legal Counsel, and then Chief of Staff, to Massachusetts Governor Mitt Romney from 2004 to 2007.

TIM TRAVAILLE has been with Frontier since 2010 and is Executive Vice President, Operational Transformation. Previously, he held other positions at Frontier, including Senior Vice President of Integration, Chief Information Officer and General Manager for Frontier in Washington State.

KATHLEEN WESLOCK joined Frontier as Executive Vice President and Chief People Officer in July 2015. Previously, she had worked as Senior Vice President/Chief Human Resources Officer at Cisco Systems, Inc. and Senior Vice President, Chief Human Resources Officer & Internal Communications, at SunGard Data Systems. She has also worked as Director of Human Resources, Financial Advisory Services, at Deloitte and Director of Global Human Resources at the global law firm Shearman & Sterling.

**Item 11. Executive Compensation**

The information required by this Item is incorporated by reference from our definitive proxy statement for the 2017 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2016.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The information required by this Item is incorporated by reference from our definitive proxy statement for the 2017 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2016.

**Item 13. Certain Relationships and Related Transactions, and Director Independence**

The information required by this Item is incorporated by reference from our definitive proxy statement for the 2017 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2016.

**Item 14. Principal Accountant Fees and Services**

The information required by this Item is incorporated by reference from our definitive proxy statement for the 2017 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2016.

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

PART IV**Item 15. Exhibits and Financial Statement Schedules**

List of Documents Filed as a Part of This Report:

## (1) Index to Consolidated Financial Statements:

Reports of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2016 and 2015

Consolidated Statements of Operations for the years ended December 31, 2016, 2015 and 2014

Consolidated Statements of Comprehensive Loss for the years ended December 31, 2016, 2015 and 2014

Consolidated Statements of Equity for the years ended December 31, 2016, 2015 and 2014

Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015 and 2014

Notes to Consolidated Financial Statements

All other schedules have been omitted because the required information is included in the consolidated financial statements or the notes thereto, or is not applicable or not required.

## (2) Index to Exhibits:

All documents referenced below were filed pursuant to the Securities Exchange Act of 1934 by Frontier, file number 001-11001, unless otherwise indicated.

<u>Exhibit No.</u>	<u>Description</u>
2.1	Stock Purchase Agreement, dated as of December 16, 2013, by and between AT&T Inc. and Frontier (filed as Exhibit 2.1 to Frontier's Current Report on Form 8-K filed on December 17, 2013).*
2.2	Securities Purchase Agreement, dated as of February 5, 2015, by and between Verizon Communications Inc. and Frontier (filed as Exhibit 2.1 to Frontier's Current Report on Form 8-K filed on February 5, 2015).*
3.1	Restated Certificate of Incorporation (filed as Exhibit 3.200.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2000).*
3.2	Certificate of Amendment of Restated Certificate of Incorporation, effective July 31, 2008 (filed as Exhibit 3.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2008).*
3.3	Certificate of Amendment of Restated Certificate of Incorporation, effective June 28, 2010 (filed as Exhibit 99.2 to Frontier's Current Report on Form 8-K filed July 1, 2010).*
3.4	By-laws, as amended February 6, 2009 (filed as Exhibit 99.1 to Frontier's Current Report on Form 8-K filed on February 6, 2009).*
3.5	Certificate of Designations of 11.125% Mandatory Convertible Preferred Stock, Series A (filed as Exhibit 3.5 to the Current Report on Form 8-K filed on June 10, 2015).*
4.1	Indenture of Securities, dated as of August 15, 1991, between Frontier and JPMorgan Chase Bank, N.A. (as successor to Chemical Bank), as Trustee (the "August 1991 Indenture") (filed as Exhibit 4.100.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 1991).*
4.2	Fourth Supplemental Indenture to the August 1991 Indenture, dated October 1, 1994, between Frontier and JPMorgan Chase Bank, N.A. (as successor to Chemical Bank), as Trustee, with respect to 7.68% Debentures due 2034 (filed as Exhibit 4.100.7 to Frontier's Current Report on Form 8-K filed on January 3, 1995).*
4.3	Fifth Supplemental Indenture to the August 1991 Indenture, dated as of June 15, 1995, between Frontier and JPMorgan Chase Bank, N.A. (as successor to Chemical Bank), as Trustee, with respect to 7.45% Debentures due 2035 (filed as Exhibit 4.100.8 to Frontier's Current Report on Form 8-K filed on March 29, 1996 (the "March 29, 1996 8-K")).*
4.4	Sixth Supplemental Indenture to the August 1991 Indenture, dated as of October 15, 1995, between Frontier and JPMorgan Chase Bank, N.A. (as successor to Chemical Bank), as Trustee, with respect to 7% Debentures due 2025 (filed as Exhibit 4.100.9 to the March 29, 1996 8-K).*

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

- 4.5 Seventh Supplemental Indenture to the August 1991 Indenture, dated as of June 1, 1996, between Frontier and JPMorgan Chase Bank, N.A. (as successor to Chemical Bank), as Trustee, with respect to 6.8% Debentures due 2026 (filed as Exhibit 4.100.11 to Frontier's Annual Report on Form 10-K for the year ended December 31, 1996 (the "1996 10-K")).\*
- 4.6 Eighth Supplemental Indenture to the August 1991 Indenture, dated as of December 1, 1996, between Frontier and JPMorgan Chase Bank, N.A. (as successor to Chemical Bank), as Trustee, with respect to 7.05% Debentures due 2046 (filed as Exhibit 4.100.12 to the 1996 10-K).\*
- 4.7 Indenture, dated as of August 16, 2001, between Frontier and JPMorgan Chase Bank, N.A. (as successor to The Chase Manhattan Bank), as Trustee, with respect to 9% Senior Notes due 2031 (including the form of note attached thereto) (filed as Exhibit 4.1 of Frontier's Current Report on Form 8-K filed on August 22, 2001).\*
- 4.8 Indenture, dated as of December 22, 2006, between Frontier and The Bank of New York, as Trustee, with respect to 7.875% Senior Notes due 2027 (including the form of note attached thereto) (filed as Exhibit 4.1 to Frontier's Current Report on Form 8-K filed on December 29, 2006).\*
- 4.9 Indenture dated as of March 23, 2007 by and between Frontier and The Bank of New York with respect to the 7.125% Senior Notes due 2019 (including the form of such note attached thereto) (filed as Exhibit 4.2 to the March 27, 2007 8-K).\*
- 4.10 Indenture dated as of April 9, 2009, between Frontier and The Bank of New York Mellon, as Trustee (the "April 2009 Indenture") (filed as Exhibit 4.1 to Frontier's Current Report on Form 8-K filed on April 9, 2009 (the "April 9, 2009 8-K")).\*
- 4.11 Second Supplemental Indenture to the April 2009 Indenture, dated as of October 1, 2009, between Frontier and The Bank of New York Mellon, as Trustee, with respect to 8.125% Senior Notes due 2018 (including the form of note attached thereto) (filed as Exhibit 4.1 to Frontier's Current Report on Form 8-K filed on October 1, 2009).\*
- 4.12 Third Supplemental Indenture to the April 2009 Indenture, dated as of May 22, 2012, between Frontier and The Bank of New York Mellon, as Trustee, with respect to 9.25% Senior Notes due 2021 (filed as Exhibit 4.1 to Frontier's Current Report on Form 8-K filed on May 22, 2012 (the "May 22, 2012 8-K")).\*
- 4.13 Form of Senior Note due 2021 (filed as Exhibit 4.2 to the May 22, 2012 8-K).\*
- 4.14 Fourth Supplemental Indenture to the April 2009 Indenture, dated as of August 15, 2012, between Frontier and The Bank of New York Mellon, as Trustee, with respect to 7.125% Senior Notes due 2023 (the "Fourth Supplement to April 2010 Indenture") (filed as Exhibit 4.1 to Frontier's Current Report on Form 8-K filed on August 15, 2012 (the "August 15, 2012 8-K")).\*
- 4.15 Form of Senior Note due 2023 (filed as Exhibit 4.2 to the August 15, 2012 8-K).\*
- 4.16 First Amendment to the Fourth Supplement to April 2009 Indenture, dated as of October 1, 2012, between Frontier and The Bank of New York Mellon, as Trustee, with respect to 7.125% Senior Notes due 2023 (filed as Exhibit 4.1 to Frontier's Current Report on Form 8-K filed on October 1, 2012).\*
- 4.17 Fifth Supplemental Indenture to the April 2009 Indenture, dated as of April 10, 2013, between Frontier and The Bank of New York Mellon, as Trustee, with respect to 7.625% Senior Notes due 2024 (filed as Exhibit 4.1 to Frontier's Current Report on Form 8-K filed on April 10, 2013 (the "April 10, 2013 8-K")).\*
- 4.18 Sixth Supplemental Indenture to the April 2009 Indenture, dated as of September 17, 2014, between Frontier Communications Corporation and The Bank of New York Mellon, as Trustee (including the form of 6.250% Senior Notes due 2021) (filed as Exhibit 4.1 to Frontier's Current Report on Form 8-K filed on September 17, 2014 (the "September 17, 2014 8-K")).\*
- 4.19 Seventh Supplemental Indenture to the April 2009 Indenture, dated as of September 17, 2014, between Frontier Communications Corporation and The Bank of New York Mellon, as Trustee, with respect to 6.875% Senior Notes due 2025 (including the form of notes attached thereto) (filed as Exhibit 4.2 to the September 17, 2014 8-K).\*
- 4.20 Form of Senior Note due 2024 (filed as Exhibit 4.2 to the April 10, 2013 8-K).\*
- 4.21 Indenture, dated as of April 12, 2010 (the "April 2010 Indenture"), as amended, between New Communications Holdings Inc. ("Spinco") and The Bank of New York Mellon, as Trustee (including the forms of notes attached thereto) (filed as Exhibit 4.22 to Spinco's Registration Statement on Form 10 filed on April 20, 2010 (File No. 000-53950) (the "Spinco Form 10")).\*
- 4.22 First Supplemental Indenture to the April 2010 Indenture, dated as of July 1, 2010, between Frontier and The Bank of New York Mellon, as Trustee, with respect to 7.875% Senior Notes due 2015, 8.25% Senior Notes due 2017, 8.5% Senior Notes due 2020, and 8.75% Senior Notes due 2022 (filed as Exhibit 4.2 to Frontier's Registration Statement on Form S-4 filed on July 2, 2010 (File No. 333-167962)).\*
- 4.23 Indenture, dated as of January 1, 1994, between Frontier North Inc. (formerly GTE North Incorporated) and Bank of New York Mellon (as successor to The First National Bank of Chicago), as Trustee (the "Frontier North Indenture") (filed as Exhibit 4.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2010).\*

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

- 4.24 First Supplemental Indenture to the Frontier North Indenture, dated as of May 1, 1996, between Frontier North Inc. (formerly GTE North Incorporated) and Bank of New York Mellon (as successor to The First National Bank of Chicago), as Trustee (filed as Exhibit 4.2 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2010).\*
- 4.25 Form of Debenture under the Frontier North Indenture (filed as Exhibit 4.24 to Frontier's Annual Report on Form 10-K for the year ended December 31, 2011 (the "2011 10-K")).\*
- 4.26 Base Indenture, dated as of September 25, 2015 (the "2015 Base Indenture"), between Frontier Communications Corporation and The Bank of New York Mellon, as trustee (filed as Exhibit 4.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 2015 (the "September 30, 2015 10-Q")).\*
- 4.27 First Supplemental Indenture to the 2015 Base Indenture, dated as of September 25, 2015, between Frontier Communications Corporation and The Bank of New York Mellon, as trustee, with respect to 8.875% Senior Notes due 2020 (including the forms of notes attached thereto) (filed as Exhibit 4.2 to the September 30, 2015 10-Q).\*
- 4.28 Second Supplemental Indenture to the 2015 Base Indenture, dated as of September 25, 2015, between Frontier Communications Corporation and The Bank of New York Mellon, as trustee, with respect to 10.500% Senior Notes due 2022 (including the forms of notes attached thereto) (filed as Exhibit 4.3 to the September 30, 2015 10-Q).\*
- 4.29 Third Supplemental Indenture to the 2015 Base Indenture, dated as of September 25, 2015, between Frontier Communications Corporation and The Bank of New York Mellon, as trustee, with respect to 11.000% Senior Notes due 2025 (including the forms of notes attached thereto) (filed as Exhibit 4.4 to the September 30, 2015 10-Q).\*
- 4.30 Restated Indenture, dated as of March 25, 2008, between Southwestern Associated Telephone Company and First National Bank in Dallas, as trustee (filed as Exhibit 4.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2016 (the "June 30, 2016 10-Q")).\*
- 4.31 Indenture, dated as of December 1, 1993, between GTE California Incorporated and Bank of America National Trust and Savings Association, as trustee (the "California Indenture") (filed as Exhibit 4.2 to the June 30, 2016 10-Q).\*
- 4.32 First Supplemental Indenture to the California Indenture dated as of April 15, 1996, between GTE California Incorporated and First Trust of California, National Association, as trustee (filed as Exhibit 4.3 to the June 30, 2016 10-Q).\*
- 4.33 Indenture, dated as of November 1, 1993, between GTE Florida Incorporated and Nations Bank of Georgia, National Association, as trustee (the "Florida Indenture") (filed as Exhibit 4.4 to the June 30, 2016 10-Q).\*
- 4.34 First Supplemental Indenture to the Florida Indenture dated as of January 1, 1998, between GTE Florida Incorporated and the Bank of New York, as trustee (filed as Exhibit 4.5 to the June 30, 2016 10-Q).\*
- 10.1 Credit Agreement, dated as of June 2, 2014, by and among Frontier, as the Borrower, and the Lenders party thereto and CoBank, ACB, as Administrative Agent (filed as Exhibit 10.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2014 (the "June 30, 2014 10-Q") (the "2014 CoBank Credit Agreement")).\*
- 10.2 Second Amendment, dated as of March 5, 2015, to the 2014 CoBank Credit Agreement, among Frontier, as the Borrower, and CoBank, ACB, as the Administrative Agent and the Lenders referred to therein (filed as Exhibit 10.2 to the March 5, 2015 8-K).\*
- 10.3 Credit Agreement, dated as of October 12, 2016, by and among Frontier, as the Borrower, the Lenders party thereto and CoBank, ACB, as the Administrative Agent (filed as Exhibit 10 to Frontier's Current Report on Form 8-K filed on October 12, 2016).\*
- 10.4 First Amended and Restated Credit Agreement, dated as of February 27, 2017, among Frontier, the Lenders party thereto and JPMorgan Chase Bank, N.A., as Administrative Agent (filed as Exhibit 10 to Frontier's Current Report on Form 8-K filed on February 28, 2017).\*
- 10.5 Tax Sharing Agreement, dated as of May 13, 2009, by and among Verizon Communications Inc. ("Verizon"), New Communications Holdings Inc. ("Spinco") and Frontier, (filed as Exhibit 10.3 to Frontier's Current Report on Form 8-K filed on May 15, 2009).\*
- 10.6 Agreement Regarding Intellectual Property Matters, dated as of March 23, 2010, among Frontier, Spinco and Verizon (filed as Exhibit 10.12 to the Spinco Form 10).\*
- 10.7 Non-Employee Directors' Deferred Fee Equity Plan, as amended and restated December 29, 2008 (filed as Exhibit 10.7 to Frontier's Annual Report on Form 10-K for the year ended December 31, 2008 (the "2008 10-K")).\*
- 10.8 Non-Employee Directors' Equity Incentive Plan, as amended and restated December 29, 2008 (filed as Exhibit 10.8 to the 2008 10-K).\*

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

10.9	Separation Agreement between Frontier and Leonard Tow effective July 10, 2004 (filed as Exhibit 10.2.4 of Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2004).*
10.10	1996 Equity Incentive Plan, as amended and restated December 29, 2008 (filed as Exhibit 10.11 to the 2008 10-K).*
10.11	2013 Frontier Bonus Plan (filed as Appendix A to Frontier's Proxy Statement dated March 25, 2013 (the "2013 Proxy Statement")).*
10.12	Amended and Restated 2000 Equity Incentive Plan, as amended and restated December 29, 2008 (filed as Exhibit 10.13 to the 2008 10-K).*
10.13	2009 Equity Incentive Plan (filed as Appendix A to Frontier's Proxy Statement dated April 6, 2009).*
10.14	2013 Equity Incentive Plan (filed as Appendix B to the 2013 Proxy Statement).*
10.15	Separation Agreement and Release, dated September 14, 2016, between Frontier and John M. Jurellier (filed as Exhibit 10.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 2016 (the "September 30, 2016 10-Q")).*
10.16	Offer of Employment Letter, dated September 1, 2016, between Frontier and R. Perley McBride (filed as Exhibit 10.2 to the September 30, 2016 10-Q). *
10.17	Change in Control Letter Agreement, dated April 27, 2012, between Frontier and Daniel J. McCarthy (filed as Exhibit 10.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2012).*
10.18	Offer of Employment Letter, dated February 25, 2015, between Frontier and Daniel J. McCarthy (filed as Exhibit 10.1 to Frontier's Current Report on Form 8-K filed on March 3, 2015 (the "March 3, 2015 8-K")).*
10.19	Offer of Employment Letter, dated January 13, 2006, between Frontier and Cecilia K. McKenney ("McKenney Offer Letter") (filed as Exhibit 10.1 to Frontier's Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2008).*
10.20	Amendment, dated May 31, 2012, to Offer of Employment Letter, dated January 13, 2006, between Frontier and Cecilia K. McKenney (filed as Exhibit 10.5 to the June 30, 2012 10-Q).*
10.21	Amended and Restated Employment Agreement, dated as of March 8, 2013, between Frontier and Mary Agnes Wilderotter (filed as Exhibit 10.1 to Frontier's Current Report on Form 8-K filed on March 13, 2013 (the "Wilderotter Employment Agreement")).*
10.22	Amendment to the Wilderotter Employment Agreement, dated as of February 25, 2015, between Frontier and Mary Agnes Wilderotter (filed as Exhibit 10.2 to the March 3, 2015 8-K).*
10.23	Offer of Employment Letter, dated January 15, 2014, between Frontier and Mark D. Nielsen (filed as Exhibit 10.1 to the June 30, 2014 10-Q).*
10.24	Offer of Employment Letter, dated June 9, 2014, between Frontier and Donald W. Daniels, Jr. (filed as Exhibit 10.3 to the June 30, 2014 10-Q).*
10.25	Form of Restricted Stock Agreement for CEO (filed as Exhibit 10.32 to Frontier's Annual Report on Form 10-K for the year ended December 31, 2009 (the "2009 10-K")).*
10.26	Form of Restricted Stock Agreement for named executive officers other than CEO (filed as Exhibit 10.33 to the 2009 10-K).*
10.27	Form of LTIP Agreement for CEO (filed as Exhibit 10.32 to the 2012 10-K).*
10.28	Form of LTIP Agreement for named executive officers other than CEO (filed as exhibit 10.33 to the 2012 10-K).*
10.29	Summary of Non-Employee Directors' Compensation Arrangements Outside of Formal Plans.
12	Computation of ratio of earnings to fixed charges (this item is included herein for the sole purpose of incorporation by reference).
21	Subsidiaries of the Registrant.
23	Consent of Independent Registered Public Accounting Firm.
31.1	Certification of Principal Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934 (the "1934 Act").
31.2	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) under the 1934 Act.
32	Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.PRE	XBRL Taxonomy Presentation Linkbase Document.
101.CAL	XBRL Taxonomy Calculation Linkbase Document.
101.LAB	XBRL Taxonomy Label Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.

Exhibits 10.7 through 10.29 are management contracts or compensatory plans or arrangements.

\* Incorporated by reference.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

FRONTIER COMMUNICATIONS CORPORATION  
(Registrant)

By: /s/ Daniel J. McCarthy  
Daniel J. McCarthy  
President and Chief Executive Officer

February 28, 2017

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on the 28<sup>th</sup> day of February 2017.

<u>Signature</u>	<u>Title</u>
<u>/s/ Leroy T. Barnes, Jr.</u> (Leroy T. Barnes, Jr.)	Director
<u>/s/ Peter C. B. Bynoe</u> (Peter C. B. Bynoe)	Director
<u>/s/ Donald Daniels</u> (Donald Daniels)	Senior Vice President & Controller (Principal Accounting Officer)
<u>/s/ Diana S. Ferguson</u> (Diana S. Ferguson)	Director
<u>/s/ Edward Fraioli</u> (Edward Fraioli)	Director
<u>/s/ R. Perley McBride</u> (R. Perley McBride)	Executive Vice President and Chief Financial Officer (Principal Financial Officer)
<u>/s/ Daniel J. McCarthy</u> (Daniel J. McCarthy)	Director, President and Chief Executive Officer (Principal Executive Officer)
<u>/s/ Pamela D.A. Reeve</u> (Pamela D.A. Reeve)	Director
<u>/s/ Virginia P. Ruesterholz</u> (Virginia P. Ruesterholz)	Director
<u>/s/ Howard L. Schrott</u> (Howard L. Schrott)	Director
<u>/s/ Lorraine D. Segil</u> (Lorraine D. Segil)	Director
<u>/s/ Mark Shapiro</u> (Mark Shapiro)	Director
<u>/s/ Myron A. Wick III</u> (Myron A. Wick III)	Director

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Index to Consolidated Financial Statements

<u>Item</u>	<u>Page</u>
Management's Report on Internal Control Over Financial Reporting	F-2
Reports of Independent Registered Public Accounting Firm	F-3 and F-4
Consolidated Balance Sheets as of December 31, 2016 and 2015	F-5
Consolidated Statements of Operations for the years ended December 31, 2016, 2015 and 2014	F-6
Consolidated Statements of Comprehensive Loss for the years ended December 31, 2016, 2015 and 2014	F-6
Consolidated Statements of Equity for the years ended December 31, 2016, 2015 and 2014	F-7
Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015 and 2014	F-8
Notes to Consolidated Financial Statements	F-9

F-1

**Management's Report On Internal Control Over Financial Reporting**

The Board of Directors and Shareholders  
Frontier Communications Corporation:

The management of Frontier Communications Corporation and subsidiaries is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f).

Under the supervision and with the participation of our management, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control-Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on our evaluation, our management concluded that our internal control over financial reporting was effective as of December 31, 2016.

Our independent registered public accounting firm, KPMG LLP, has audited the consolidated financial statements included in this report and, as part of their audit, has issued their report, included herein, on the effectiveness of our internal control over financial reporting.

/s/ Daniel J. McCarthy

\_\_\_\_\_  
Daniel J. McCarthy  
President and Chief Executive Officer

/s/ R. Perley McBride

\_\_\_\_\_  
R. Perley McBride  
Executive Vice President and Chief Financial Officer

Norwalk, Connecticut  
February 28, 2017

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
Frontier Communications Corporation:

We have audited the accompanying consolidated balance sheets of Frontier Communications Corporation and subsidiaries as of December 31, 2016 and 2015, and the related consolidated statements of operations, comprehensive loss, equity and cash flows for each of the years in the three-year period ended December 31, 2016. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Frontier Communications Corporation and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Frontier Communications Corporation and subsidiaries internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 28, 2017 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ KPMG LLP

Stamford, Connecticut  
February 28, 2017

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
Frontier Communications Corporation:

We have audited Frontier Communications Corporation and subsidiaries' internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Frontier Communications Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report On Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Frontier Communications Corporation and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control – Integrated Framework (2013) issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Frontier Communications Corporation and subsidiaries as of December 31, 2016 and 2015, and the related consolidated statements of operations, comprehensive loss, equity and cash flows for each of the years in the three-year period ended December 31, 2016, and our report dated February 28, 2017 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP

Stamford, Connecticut  
February 28, 2017

## FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS  
AS OF DECEMBER 31, 2016 AND 2015

(\$ in millions and shares in thousands, except for per-share amounts)

	2016	2015
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 522	\$ 936
Accounts receivable, less allowances of \$131 and \$57, respectively	938	571
Restricted cash	-	8,444
Prepaid expenses	88	100
Income taxes and other current assets	108	80
Total current assets	<u>1,656</u>	<u>10,131</u>
Property, plant and equipment, net	14,902	8,493
Goodwill	9,674	7,166
Other intangibles, net	2,662	1,143
Other assets	119	151
Total assets	<u>\$ 29,013</u>	<u>\$ 27,084</u>
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Long-term debt due within one year	\$ 363	\$ 384
Accounts payable	698	467
Advanced billings	301	160
Accrued other taxes	134	87
Accrued interest	437	403
Pension and other postretirement benefits	23	33
Other current liabilities	488	359
Total current liabilities	<u>2,444</u>	<u>1,893</u>
Deferred income taxes	2,516	2,666
Pension and other postretirement benefits	1,602	1,163
Other liabilities	372	240
Long-term debt	17,560	15,508
Equity:		
Preferred stock, \$0.01 par value (50,000 authorized shares, 11.125%, Series A, 19,250 shares issued and outstanding)	-	-
Common stock, \$0.25 par value (1,750,000 authorized shares, 1,192,986 issued, and 1,172,553 and 1,168,200 outstanding, at December 31, 2016 and 2015, respectively)	298	298
Additional paid-in capital	5,283	6,034
Accumulated deficit	(460)	(87)
Accumulated other comprehensive loss, net of tax	(387)	(353)
Treasury common stock	(215)	(278)
Total equity	<u>4,519</u>	<u>5,614</u>
Total liabilities and equity	<u>\$ 29,013</u>	<u>\$ 27,084</u>

The accompanying Notes are an integral part of these Consolidated Financial Statements.

**FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
**FOR THE YEARS ENDED DECEMBER 31, 2016, 2015 AND 2014**  
(\$ in millions and shares in thousands, except for per-share amounts)

	2016	2015	2014
Revenue	\$ 8,896	\$ 5,576	\$ 4,772
Operating expenses:			
Network access expenses	1,470	540	465
Network related expenses	1,887	1,287	1,118
Selling, general and administrative expenses	2,093	1,346	1,066
Depreciation and amortization	2,031	1,320	1,139
Acquisition and integration costs	436	236	142
Restructuring costs and other charges	91	2	2
Total operating expenses	8,008	4,831	3,952
Operating income	888	745	820
Investment and other income, net	20	7	39
Interest expense	1,531	1,113	696
Income (loss) before income taxes	(623)	(361)	163
Income tax expense (benefit)	(250)	(185)	30
Net income (loss)	(373)	(196)	133
Less: Dividends on preferred stock	214	120	-
Net income (loss) attributable to Frontier common shareholders	\$ (587)	\$ (316)	\$ 133
Basic and diluted net income (loss) per share attributable to Frontier common shareholders	\$ (0.51)	\$ (0.29)	\$ 0.13
Total weighted average shares outstanding - basic	1,164,099	1,084,606	994,418
Total weighted average shares outstanding - diluted	1,164,099	1,084,606	998,162

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS**  
**FOR THE YEARS ENDED DECEMBER 31, 2016, 2015 AND 2014**  
(\$ in millions)

	2016	2015	2014
Net income (loss)	\$ (373)	\$ (196)	\$ 133
Other comprehensive income (loss), net of tax	(34)	51	(143)
Comprehensive loss	\$ (407)	\$ (145)	\$ (10)

The accompanying Notes are an integral part of these Consolidated Financial Statements.

**FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF EQUITY**  
**FOR THE YEARS ENDED DECEMBER 31, 2016, 2015 AND 2014**  
(\$ in millions and shares in thousands)

	Preferred Stock		Common Stock		Additional Paid-In Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Loss	Treasury Common Stock		Total Equity
	Shares	Amount	Shares	Amount				Shares	Amount	
Balance December 31, 2013	-	\$ -	1,027,986	\$ 257	\$ 4,321	\$ 76	\$ (261)	(28,524)	\$ (336)	\$ 4,055
Stock plans	-	-	-	-	(30)	-	-	3,007	44	14
Dividends on common stock	-	-	-	-	(301)	(100)	-	-	-	(401)
Net income	-	-	-	-	-	133	-	-	-	133
Other comprehensive loss, net of tax	-	-	-	-	-	-	(143)	-	-	(143)
Balance December 31, 2014	-	-	1,027,986	257	3,990	109	(404)	(25,517)	(294)	3,658
Issuance of common stock	-	-	165,000	41	758	-	-	-	-	799
Issuance of preferred stock	19,250	-	-	-	1,866	-	-	-	-	1,866
Stock plans	-	-	-	-	(4)	-	-	731	16	12
Dividends on common stock	-	-	-	-	(456)	-	-	-	-	(456)
Dividends on preferred stock	-	-	-	-	(120)	-	-	-	-	(120)
Net loss	-	-	-	-	-	(196)	-	-	-	(196)
Other comprehensive income, net of tax	-	-	-	-	-	-	51	-	-	51
Balance December 31, 2015	19,250	-	1,192,986	298	6,034	(87)	(353)	(24,786)	(278)	5,814
Stock plans	-	-	-	-	(44)	-	-	4,353	63	19
Dividends on common stock	-	-	-	-	(493)	-	-	-	-	(493)
Dividends on preferred stock	-	-	-	-	(214)	-	-	-	-	(214)
Net loss	-	-	-	-	-	(373)	-	-	-	(373)
Other comprehensive loss, net of tax	-	-	-	-	-	-	(34)	-	-	(34)
Balance December 31, 2016	19,250	\$ -	1,192,986	\$ 298	\$ 5,283	\$ (460)	\$ (387)	(20,433)	\$ (215)	\$ 4,519

The accompanying Notes are an integral part of these Consolidated Financial Statements.

**FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2016, 2015 AND 2014**  
**(\$ in millions)**

	2016	2015	2014
Cash flows provided from (used by) operating activities:			
Net income (loss)	\$ (373)	\$ (196)	\$ 133
Adjustments to reconcile net income (loss) to net cash provided from operating activities:			
Depreciation and amortization	2,031	1,320	1,139
Loss on debt exchanges	7	-	-
Pension/OPEB costs	79	10	(18)
Special Termination Benefits	26	-	-
Stock based compensation expense	24	27	23
Gains on sale of assets	-	-	(37)
Amortization of deferred financing costs	46	191	10
Other non-cash adjustments	(12)	-	22
Deferred income taxes	(206)	(167)	(78)
Change in accounts receivable	(18)	62	(61)
Change in accounts payable and other liabilities	(22)	102	90
Change in prepaid expenses, income taxes and other current assets	85	(48)	47
Net cash provided from operating activities	1,668	1,301	1,270
Cash flows provided from (used by) investing activities:			
Cash paid for CTF Acquisition	(9,871)	-	-
Cash paid for Connecticut Acquisition	-	-	(2,018)
Capital expenditures - Business operations	(1,259)	(710)	(572)
Capital expenditures - Integration activities	(142)	(153)	(116)
Network expansion funded by Connect America Fund - Phase 1	-	(22)	(56)
Grant funds received for network expansion from Connect America Fund - Phase 1	-	-	4
Proceeds on sale of assets	6	22	39
Cash paid for an acquisition, net of cash acquired	-	(17)	-
Other	5	2	32
Net cash used by investing activities	(11,259)	(878)	(2,687)
Cash flows provided from (used by) financing activities:			
Proceeds from long-term debt borrowings	1,040	6,603	1,911
Financing costs paid	(39)	(119)	(40)
Long-term debt payments	(453)	(296)	(260)
Proceeds from issuance of common stock, net	-	799	-
Proceeds from issuance of preferred stock, net	-	1,866	-
Dividends paid on common stock	(493)	(458)	(401)
Dividends paid on preferred stock	(214)	(120)	-
Other	(6)	-	(2)
Net cash provided from financing activities	735	8,275	1,208
Increase/(Decrease) in cash, cash equivalents and restricted cash	(8,856)	8,698	(209)
Cash, cash equivalents and restricted cash at January 1,	9,380	682	891
Cash, cash equivalents and restricted cash at December 31,	\$ 522	\$ 9,380	\$ 682
Supplemental cash flow information:			
Cash paid (received) during the period for:			
Interest	\$ 1,467	\$ 728	\$ 656
Income taxes (refunds), net	\$ (120)	\$ 28	\$ 70
Non-cash investing and financing activities:			
Financing obligation for contributions of real property to pension plan	\$ 15	\$ -	\$ -
Reduction of pension obligation	\$ 15	\$ -	\$ -
Decrease in capital expenditures due to changes in accounts payable	\$ (60)	\$ (56)	\$ (15)
Conversion of operating leases to capital leases	\$ 111	\$ -	\$ -

The accompanying Notes are an integral part of these Consolidated Financial Statements

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements(1) Description of Business and Summary of Significant Accounting Policies:(a) Description of Business:

Frontier Communications Corporation (Frontier) is the fourth largest Incumbent Local Exchange Carrier (ILEC) in the United States, with approximately 5.4 million customers, 4.3 million broadband subscribers and 28,300 employees, operating in 29 states. Frontier was incorporated in 1935, originally under the name of Citizens Utilities Company and was known as Citizens Communications Company until July 31, 2008. Frontier and its subsidiaries are referred to as "we," "us," "our," "Frontier," or the "Company" in this report.

Effective April 1, 2016, Frontier's scope of operations and balance sheet changed materially as a result of the completion of the CTF Acquisition, as described in Note 3 - Acquisitions. Historical financial data presented for Frontier is not indicative of the future financial position or operating results for Frontier, and includes the results of the CTF Operations, as defined in Note 3 - Acquisitions, from the date of acquisition on April 1, 2016.

(b) Basis of Presentation and Use of Estimates:

Our consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). Certain reclassifications of amounts previously reported have been made to conform to the current presentation. All significant intercompany balances and transactions have been eliminated in consolidation.

For our financial statements as of and for the period ended December 31, 2016, we evaluated subsequent events and transactions for potential recognition or disclosure through the date that we filed this Form 10-K with the Securities and Exchange Commission (SEC).

The preparation of our financial statements in conformity with GAAP requires management to make estimates and assumptions that affect (i) the reported amounts of assets and liabilities at the date of the financial statements, (ii) the disclosure of contingent assets and liabilities, and (iii) the reported amounts of revenue and expenses during the reporting period. Actual results may differ from those estimates. Estimates and judgments are used when accounting for the allowance for doubtful accounts, asset impairments, indefinite-lived intangibles, depreciation and amortization, income taxes, business combinations, and pension and other postretirement benefits, among others.

(c) Cash Equivalents:

We consider all highly liquid investments with an original maturity of three months or less to be cash equivalents.

(d) Revenue Recognition:

Revenue is recognized when services are provided or when products are delivered to customers. Revenue that is billed in advance includes monthly recurring network access services (including data services), special access services and monthly recurring voice, video and related charges. The unearned portion of these fees is initially deferred as a component of "Advanced billings" on our consolidated balance sheet and recognized as revenue over the period that the services are provided. Revenue that is billed in arrears includes non-recurring network access services (including data services), switched access services and non-recurring voice and video services. The earned but unbilled portion of these fees is recognized as revenue in our consolidated statements of operations and accrued in "Accounts Receivable" on our consolidated balance sheet in the period that the services are provided. Excise taxes are recognized as a liability when billed. Installation fees and their related direct and incremental costs are initially deferred and recognized as revenue and expense over the average term of a customer relationship. We recognize as current period expense the portion of installation costs that exceeds installation fee revenue.

We maintain an allowance for doubtful accounts based on an estimate of our ability to collect accounts receivable. At December 31, 2016, our accounts receivable balances, including balances for delinquent accounts, were higher than usual as a result of planned delays in collection efforts for certain new customers acquired in the CTF Acquisition. These payment delays are customary for us after large acquisitions in order

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

to allow for resolution of any service or billing issues for new customers. Our allowance for doubtful accounts was adjusted to reflect our best estimate of collectability.

Frontier collects various taxes from its customers and subsequently remits these taxes to governmental authorities. Substantially all of these taxes are recorded through the consolidated balance sheet and presented on a net basis in our consolidated statements of operations. We also collect Universal Service Fund (USF) surcharges from customers (primarily federal USF) that we have recorded on a gross basis in our consolidated statements of operations and included within "Revenue" and "Network related expenses" of \$217 million, \$151 million and \$125 million for the years ended December 31, 2016, 2015 and 2014, respectively.

In 2015 we accepted the FCC's Connect America Fund (CAF) Phase II offer of support, which is a successor to and augments the USF frozen high cost support that we had been receiving pursuant to a 2011 FCC order. Upon completion of the CTF Acquisition, Frontier assumed the CAF Phase II support and related obligations that Verizon had previously accepted with regard to California and Texas. CAF Phase II funding is a program intended to subsidize the high cost of establishing and delivering communications services to certain unserved or underserved areas. We are recognizing these subsidies into revenue on a straight line basis, which is consistent with how the costs related to these subsidies are being and are expected to be incurred. CAF Phase II is a multi-year program which requires us to deploy broadband to a specified number of households in each of the states where funding was accepted. Failure to meet our deployment obligations at the end of the program in 2020 will result in a return of a portion of the funding received. We regularly evaluate our ability to meet our broadband deployment obligations and adjust revenue accordingly.

We categorize our products, services and other revenues among the following five categories:

- *Voice services* include traditional local and long distance wireline services, Voice over Internet Protocol (VoIP) services, as well as a number of unified messaging services offered to our residential and business customers. Voice services also include the long distance voice origination and termination services that we provide to our business customers and other carriers;
- *Data and Internet services* include broadband services for residential and business customers. We provide data transmission services to high volume business customers and other carriers with dedicated high capacity circuits ("nonswitched access") including services to wireless providers ("wireless backhaul");
- *Video services* include revenues generated from services provided directly to residential customers through the FiOS® and Vantage video brands, and through DISH® satellite TV services;
- *Other customer revenue* includes sales of customer premise equipment to our business customers and directory services, less our provision for bad debts; and
- *Switched Access and Subsidy* revenues include revenues derived from allowing other carriers to use our network to originate and/or terminate their local and long distance voice traffic ("switched access"). These services are primarily billed on a minutes-of-use basis applying tariffed rates filed with the FCC or state agencies. We also receive cost subsidies from state and federal authorities, including the Connect America Fund Phase II.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

The following table provides a summary of revenues from external customers by the categories of Frontier's products and services:

(\$ in millions)	For the year ended December 31,		
	2016	2015	2014
Voice services	\$ 2,866	\$ 2,022	\$ 1,951
Data and Internet services	3,693	2,337	1,948
Video services	1,244	285	134
Other	276	255	220
Customer revenue	8,099	4,899	4,253
Switched access and subsidy	797	677	519
Total revenue	\$ 8,896	\$ 5,576	\$ 4,772

(e) Property, Plant and Equipment:

Property, plant and equipment are stated at original cost, including capitalized interest, or fair market value as of the date of acquisition for acquired properties. Maintenance and repairs are charged to operating expenses as incurred. The gross book value of routine property, plant and equipment retirements is charged against accumulated depreciation.

(f) Goodwill and Other Intangibles:

Goodwill represents the excess of purchase price over the fair value of identifiable tangible and intangible net assets acquired. We undertake studies to determine the fair values of assets and liabilities acquired and allocate purchase prices to assets and liabilities, including property, plant and equipment, goodwill and other identifiable intangibles. We examine the carrying value of our goodwill and trade name annually as of December 31, or more frequently, as circumstances warrant, to determine whether there are any impairment losses. We test for goodwill impairment at the "operating segment" level, as that term is defined in GAAP. During the second quarter of 2016, Frontier reorganized into seven regional operating segments, which are aggregated into one reportable segment. In conjunction with the reorganization of our operating segments, effective with the second quarter of 2016, we reassigned goodwill to our regional operating segments (reporting units) using a relative fair value allocation approach.

Frontier amortizes finite-lived intangible assets over their estimated useful lives on the accelerated method of sum of the years digits. We review such intangible assets at least annually as of December 31 to assess whether any potential impairment exists and whether factors exist that would necessitate a change in useful life and a different amortization period.

(g) Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of:

We review long-lived assets to be held and used, including customer lists, and long-lived assets to be disposed of for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Recoverability of assets to be held and used is measured by comparing the carrying amount of the asset to the future undiscounted net cash flows expected to be generated by the asset. Recoverability of assets held for sale is measured by comparing the carrying amount of the assets to their estimated fair market value. If any assets are considered to be impaired, the impairment is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value. Also, we periodically reassess the useful lives of our tangible and intangible assets to determine whether any changes are required.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

(h) Income Taxes and Deferred Income Taxes:

We file a consolidated federal income tax return. We utilize the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred income taxes are recorded for the tax effect of temporary differences between the financial statement basis and the tax basis of assets and liabilities using tax rates expected to be in effect when the temporary differences are expected to reverse.

(i) Stock Plans:

We have various stock-based compensation plans. Awards under these plans are granted to eligible employees and directors. Awards may be made in the form of incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units or other stock-based awards, including awards with performance, market and time-vesting conditions. Our general policy is to issue shares from treasury upon the grant of restricted shares, earning of performance shares and the exercise of options.

The compensation cost recognized is based on awards ultimately expected to vest. GAAP requires forfeitures to be estimated and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

(j) Net Income (Loss) Per Share Attributable to Frontier Common Shareholders:

Basic net income (loss) per common share is computed using the weighted average number of common shares outstanding during the period being reported on, excluding unvested restricted stock awards. The impact of dividends paid on unvested restricted stock awards have been deducted in the determination of basic and diluted net income (loss) per share attributable to Frontier common shareholders. Except when the effect would be antidilutive, diluted net income per common share reflects the dilutive effect of certain common stock equivalents, as described further in Note 13 – Net Income (Loss) Per Common Share.

(2) Recent Accounting Pronouncements:***Recently Adopted Accounting Pronouncements******Business Combinations – Measurement Period Adjustments***

In September 2015, the FASB issued ASU No. 2015-16, "Business Combinations – Simplifying the Accounting for Measurement Period Adjustments." This ASU requires that an acquirer recognizes adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The amendments in this Update require that the acquirer record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. The amendments in this Update require an entity to present separately on the face of the income statement or disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. The new guidance was effective for Frontier on January 1, 2016 and has been applied to the measurement period adjustments related to our CTF Acquisition during 2016.

***Employee Benefit Plans***

In July 2015, the FASB issued ASU No. 2015-12, "Plan Accounting: Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), and Health and Welfare Benefit Plans (Topic 965)": There are three parts to the ASU that aim to simplify the accounting and presentation of plan accounting. Part I of this ASU requires fully benefit-responsive investment contracts to be measured at contract value instead of the current fair value measurement. Part II of this ASU requires investments (both participant-directed and nonparticipant-directed investments) of employee benefit plans be grouped only by general type, eliminating the need to disaggregate the investments in multiple ways. Part III of this ASU provides a similar measurement date practical expedient for employee benefit plans as available in ASU No. 2015-04, "Compensation – Retirement Benefits (Topic 715)," which allows employers to measure defined benefit plan assets on a month-end date that is nearest to the year's fiscal year-end when the fiscal period does not coincide with a month-end. Parts I and II of the new guidance should be applied on a retrospective basis. Part III of the new guidance

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

should be applied on a prospective basis. The new guidance was effective for Frontier on January 1, 2016 and Frontier has applied the new guidance in its reporting for defined benefit plans completed in 2016.

**Cash Flows -- Classification of Certain Cash Receipts and Cash Payments**

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows -- Classification of Certain Cash Receipts and Cash Payments." This ASU addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. The amendments in this ASU provide guidance on the following cash flow issues: 1) debt prepayment or debt extinguishment costs; 2) settlement of zero-coupon debt instruments; 3) contingent consideration payments made after a business combination; 4) proceeds from the settlement of insurance claims; 5) proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; 6) distributions received from equity method investees; 7) beneficial interests in securitization transactions; and 8) separately identifiable cash flows and application of the predominance principle. The new guidance was early adopted by Frontier in 2016 and Frontier has retrospectively applied the new guidance in our Statement of Cash Flows for 2014, 2015, and 2016.

**Statement of Cash Flows -- Restricted Cash**

In November 2016, the FASB issued ASU No. 2016-18, "Statement of Cash Flows -- Restricted Cash Flows." This ASU requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The amendments in this Update do not provide a definition of restricted cash or restricted cash equivalents. The new guidance was early adopted by Frontier in 2016 and Frontier has retrospectively applied the new guidance in our Statement of Cash Flows for 2014, 2015, and 2016.

**Recent Accounting Pronouncements Not Yet Adopted**

**Revenue Recognition**

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, "Revenue from Contracts with Customers." This standard, along with its related amendments, requires companies to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which Frontier expects to be entitled in exchange for those goods or services. This new standard is effective for annual and interim reporting periods beginning after December 15, 2017. Companies are also permitted to voluntarily adopt the new standard as of the original effective date that was for annual reporting periods beginning after December 15, 2016, however, Frontier does not intend to early adopt. Companies are permitted to either apply the requirements retrospectively to all prior periods presented, or apply the requirements in the year of adoption, through a cumulative adjustment. Frontier has not yet selected a transition method and is currently evaluating the guidance and developing an implementation plan.

**Leases**

In February 2016, the FASB issued ASU No. 2016 - 02, "Leases (Topic 842)." This standard establishes the principles to report transparent and economically neutral information about the assets and liabilities that arise from leases. Upon implementation, lessees will need to recognize almost all leases on their balance sheet as a right-of-use asset and a lease liability. It will be critical to identify leases embedded in a contract to avoid misstating the lessee's balance sheet. For income statement purposes, the FASB retained a dual model, requiring leases to be classified as either operating or finance. Classification will be based on criteria that are largely similar to those applied in current lease accounting, but without explicit bright lines. Lessor accounting is similar to the current model, but updated to align with certain changes to the lessee model and the new revenue recognition standard. Existing sale-leaseback guidance, including guidance for real estate, is replaced with a new model applicable to both lessees and lessors. The new guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted. Frontier is currently evaluating the impact of adopting the new standard, but has not yet determined the impact of adoption on its consolidated financial statements.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial StatementsCompensation – Stock Compensation

In March 2016, the FASB issued ASU No. 2016-09, "Improvements to Employee Share-Based Payment Accounting," to amend ASC Topic 718, "Compensation – Stock Compensation." The ASU is part of the FASB's ongoing simplification initiative, which is designed to reduce cost and complexity while maintaining or improving the usefulness of the information provided to the users of financial statements. The proposed simplifications address a variety of areas for public entities, including the following: 1) accounting for income taxes, 2) classification of excess tax benefits on the statement of cash flows, 3) forfeitures, 4) minimum statutory tax withholding requirements, 5) classifications of employee taxes paid on the statement of cash flows when an employer withholds shares for tax withholding purposes, and 6) classification of awards with repurchase features. The new guidance is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Frontier has determined that the impact of adoption is immaterial to its consolidated financial statements.

Intangibles – Goodwill

In January 2017, the FASB issued ASU No. 2017-04, "Simplifying the Test for Goodwill Impairment." This standard was established to simplify how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. Under the amendments in this Update, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. Additionally, an entity should consider income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss, if applicable. The Board also eliminated the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. Therefore, the same impairment assessment applies to all reporting units. An entity is required to disclose the amount of goodwill allocated to each reporting unit with a zero or negative carrying amount of net assets. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The new guidance is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. Frontier is currently evaluating the impact of adopting the new standard and has not yet determined the impact of adoption on its consolidated financial statements.

(3) Acquisitions:The CTF Acquisition

On April 1, 2016, Frontier acquired the wireline operations of Verizon Communications, Inc. in California, Texas and Florida for a purchase price of \$10,540 million in cash and assumed debt (the CTF Acquisition), pursuant to the February 5, 2015 Securities Purchase Agreement, as amended. In addition, Frontier and Verizon settled the working capital and net debt adjustments with \$15 million paid to Frontier in October 2016. As a result of the CTF Acquisition, Frontier now operates these former Verizon properties, which included approximately 2.5 million total customers, 2.1 million broadband subscribers, and 1.2 million FiOS video subscribers as of April 1, 2016 (the CTF Operations).

Our consolidated statement of operations for the year ended December 31, 2016 includes \$3,622 million of revenue and \$582 million of operating income related to the nine months of operating results of the CTF Operations since April 1, 2016.

The allocation of the purchase price presented below, which is preliminary and subject to change, represents the effect of recording the estimates of the fair value of assets acquired and liabilities assumed as of the date of the CTF Acquisition, based on the total transaction cash consideration of \$9,886 million at December 31, 2016, as adjusted for the \$15 million settlement payment discussed above. These current estimates will be revised in future periods for information that is currently not available to us, primarily related to certain legal and tax accruals and contingencies; accounts receivable; property, plant and equipment; customer base and

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

other intangibles; deferred income tax assets and liabilities; pension assets and liabilities, as well as other assumed postretirement benefit obligations, pending completion of actuarial studies and the related transfer of pension assets. The revisions may affect the presentation of our consolidated financial results. Any changes to the initial estimates of the fair value of the assets and liabilities will be recorded as adjustments to those assets and liabilities and residual amounts will be allocated to goodwill.

*(\$ in millions)*

Current assets	\$	350
Property, plant & equipment		6,236
Goodwill		2,508
Other intangibles - primarily customer base		2,152
Current liabilities		(518)
Long-term debt		(544)
Other liabilities		(323)
Total net assets acquired	\$	<u>9,871</u>

The total consideration exceeded the net estimated fair value of the assets acquired and liabilities assumed by \$2,508 million, which we recognized as goodwill. This goodwill is attributable to strategic benefits, including enhanced financial and operational scale, market diversification and leveraged combined networks that we expect to realize. This amount of goodwill associated with the CTF Acquisition will be deductible for income tax purposes.

The Securities Purchase Agreement provides for a post-closing adjustment for both pension liabilities and pension assets. Frontier and Verizon have not finalized the results of these calculations. Such calculations will be completed in accordance with the terms of the Securities Purchase Agreement.

The following unaudited pro forma financial information presents the combined results of operations of Frontier and the CTF Operations as if the CTF Acquisition had occurred as of January 1, 2015. The pro forma information is not necessarily indicative of what the financial position or results of operations actually would have been had the CTF Acquisition been completed as of January 1, 2015. In addition, the unaudited pro forma financial information is not indicative of, nor does it purport to project, the future financial position or operating results of Frontier. The unaudited pro forma financial information excludes acquisition and integration costs and does not give effect to any estimated and potential cost savings or other operating efficiencies that may result from the CTF Acquisition.

<i>(\$ in millions, except per share amounts)</i>	(Unaudited)			
	For the year ended December 31,			
	2016		2015	
Revenue	\$	10,255	\$	11,157
Operating income	\$	1,433	\$	1,529
Net loss attributable to Frontier common shareholders	\$	262	\$	(192)
Basic and diluted net loss per share attributable to Frontier common shareholders	\$	(0.23)	\$	(0.17)

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

During 2015, we completed our financing activities associated with the CTF Acquisition, which included: 1) a private debt offering of \$6,600 million of unsecured senior notes in September 2015, 2) the 2015 Credit Agreement (as defined below) for a senior secured delayed-draw term loan facility in August 2015 and 3) a registered offering of \$2,750 million of preferred and common stock in June 2015. Net proceeds from these debt and equity offerings together with the proceeds received from the delayed draw term loan facility and cash on hand were used to fund the CTF Acquisition and pay related fees and expenses.

The Connecticut Acquisition

On October 24, 2014, Frontier acquired the wireline properties of AT&T Inc. (AT&T) in Connecticut (the Connecticut Acquisition) for a purchase price of \$2,018 million in cash, pursuant to the stock purchase agreement dated December 16, 2013, as amended. Following the Connecticut Acquisition, Frontier now owns and operates the wireline business and fiber optic network servicing residential, commercial and wholesale customers in Connecticut. Frontier also acquired the AT&T U-verse® video (Vantage) and DISH® satellite TV customers in Connecticut. See Note 7 for further discussion related to financing the Connecticut Acquisition.

Our consolidated statements of operations for the years ended December 31, 2015 and 2014 include \$1,049 million and \$216 million of revenue, respectively, and \$100 million and \$38 million of operating income, respectively, related to the results of the Connecticut operations.

The final allocation of the purchase price presented below represents the effect of recording the fair value of assets acquired, liabilities assumed and related deferred income taxes as of the date of the Connecticut Acquisition, based on the total transaction consideration of \$2,018 million.

(\$ in millions)

Current assets	\$	69
Property, plant & equipment		1,459
Goodwill		815
Other intangibles - customer base		570
Current liabilities		(94)
Deferred income taxes		(576)
Other liabilities		(225)
Total net assets acquired	\$	<u>2,018</u>

The total consideration exceeded the net estimated fair value of the assets acquired and liabilities assumed by \$815 million, which we recognized as goodwill. This goodwill is attributable to strategic benefits, including enhanced financial and operational scale, market diversification and leveraged combined networks that we expect to realize. Of this amount, goodwill associated with the Connecticut Acquisition of \$75 million is deductible for income tax purposes.

The following unaudited pro forma financial information presents the combined results of operations of Frontier and the Connecticut operations as if the Connecticut Acquisition had occurred as of January 1, 2014. The pro forma information is not necessarily indicative of what the financial position or results of operations actually would have been had the Connecticut Acquisition been completed as of January 1, 2014. In addition, the unaudited pro forma financial information is not indicative of, nor does it purport to project, the future financial position or operating results of Frontier. The unaudited pro forma financial information excludes acquisition and integration costs and does not give effect to any estimated and potential cost savings or other operating efficiencies that may result from the Connecticut Acquisition.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

<i>(\$ in millions, except per share amounts)</i>	(Unaudited) For the year ended December 31,	
	2014	
Revenue	\$	5,775
Operating income	\$	985
Net income attributable to Frontier common shareholders	\$	191
Basic and diluted net income per share attributable to Frontier common shareholders	\$	0.19

**Acquisition and Integration Costs**

Acquisition costs include legal, financial advisory, accounting, regulatory and other related costs. Integration costs include expenses that are incremental and directly related to the acquisition, and were incurred to integrate the network and information technology platforms and to enable other integration initiatives.

Frontier incurred operating expenses related to the CTF Acquisition and the Connecticut Acquisition, as follows:

<i>(\$ in millions)</i>	For the Year Ended		
	2016	2015	2014
Acquisition costs:			
CTF Acquisition	\$ 23	\$ 44	\$ -
Connecticut Acquisition	-	1	15
	23	45	15
Integration costs:			
CTF Acquisition	412	152	-
Connecticut Acquisition	1	39	127
	413	191	127
Total acquisition and integration costs	\$ 436	\$ 236	\$ 142

We also invested \$142 million and \$129 million in capital expenditures related to the CTF Acquisition during the years ended December 31, 2016 and 2015, respectively. In connection with the Connecticut Acquisition, Frontier invested \$24 million and \$116 million in capital expenditures during the years ended December 31, 2015 and 2014, respectively.

**FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES**  
Notes to Consolidated Financial Statements

**(4) Accounts Receivable:**

The components of accounts receivable, net at December 31, 2016 and 2015 are as follows.

<i>(\$ in millions)</i>	2016	2015
Retail and Wholesale	\$ 979	\$ 569
Other	90	59
Less: Allowance for doubtful accounts	(131)	(57)
Accounts receivable, net	<u>\$ 938</u>	<u>\$ 571</u>

An analysis of the activity in the allowance for doubtful accounts for the years ended December 31, 2016, 2015 and 2014 is as follows:

<i>(\$ in millions)</i>	Balance at beginning of Period	Charged to Other Revenue	Charged (Credited) to Switched and Nonswitched Revenue and Other Accounts	Write-offs, net of Recoveries	Balance at end of Period
2014	\$ 71	\$ 61	\$ -	\$ (60)	\$ 72
2015	\$ 72	\$ 67	\$ (17)	\$ (65)	\$ 57
2016	\$ 57	\$ 164	\$ 15	\$ (105)	\$ 131

We maintain an allowance for doubtful accounts based on our estimate of our ability to collect accounts receivable. The provision for uncollectible amounts was \$179 million, \$50 million, and \$61 million for the years ended December 31, 2016, 2015 and 2014, respectively. Our allowance for doubtful accounts declined in 2015, primarily as a result of the resolution of a principal carrier dispute. Our allowance for doubtful accounts increased in 2016 primarily as a result of the customer account balances related to the CTF Operations subsequent to the CTF Acquisition.

**(5) Property, Plant and Equipment:**

Property, plant and equipment, net at December 31, 2016 and 2015 are as follows:

<i>(\$ in millions)</i>	Estimated Useful Lives	2016	2015
Land	N/A	\$ 235	\$ 151
Buildings and leasehold improvements	41 years	2,300	1,327
General support	5 to 17 years	1,495	1,146
Central office/electronic circuit equipment	5 to 18 years	7,683	6,244
Poles	30 years	995	712
Cable, fiber and wire	15 to 25 years	10,267	7,280
Conduit	55 years	1,611	515
Other	12 to 25 years	52	47
Construction work in progress		903	379
Property, plant and equipment		<u>25,541</u>	<u>17,801</u>
Less: Accumulated depreciation		<u>(10,639)</u>	<u>(9,308)</u>
Property, plant and equipment, net		<u>\$ 14,902</u>	<u>\$ 8,493</u>

Property, plant, and equipment includes approximately \$154 million and \$43 million of fixed assets recognized under capital leases as of December 31, 2016 and 2015, respectively.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

Depreciation expense is principally based on the composite group method. Depreciation expense was as follows:

(\$ in millions)	For the Year Ended		
	2016	2015	2014
Depreciation expense	\$ 1,388	\$ 983	\$ 835

We adopted new estimated remaining useful lives for certain plant assets as of October 1, 2016, as a result of an annual independent study of the estimated remaining useful lives of our plant assets, with an insignificant impact to depreciation expense. In addition, the estimated useful lives for assets acquired in the CTF Acquisition were adopted for such assets based on a similar study performed as of October 1, 2015 and were effective April 1, 2016

(6) Goodwill and Other Intangibles:

The activity in our goodwill from January 1, 2015 through December 31, 2016 is as follows:

(\$ in millions)	Goodwill	
Balance at January 1, 2015	\$	7,205
Connecticut Acquisition Adjustment		(53)
Other Acquisition		14
Balance at December 31, 2015		7,166
CTF Acquisition (Note 3)		2,508
Balance at December 31, 2016	\$	9,674

The components of other intangibles at December 31, 2016 and 2015 are as follows:

(\$ in millions)	2016			2015		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Other Intangibles:						
Customer base	\$ 5,088	\$ (2,604)	\$ 2,484	\$ 2,998	\$ (1,977)	\$ 1,021
Trade name	122	-	122	122	-	122
Royalty agreement	72	(16)	56	-	-	-
Total other intangibles	\$ 5,282	\$ (2,620)	\$ 2,662	\$ 3,120	\$ (1,977)	\$ 1,143

Amortization expense was as follows:

(\$ in millions)	For the Year Ended		
	2016	2015	2014
Amortization expense	\$ 643	\$ 337	\$ 304

Amortization expense primarily represents the amortization of our customer base acquired as a result of the CTF Acquisition, the Connecticut Acquisition and the acquisition of certain Verizon properties in 2010 with each based on a useful life of 8 to 12 years on an accelerated method. The approximate weighted average remaining life of our customer base is 7 years and for our royalty agreement is 4 years. Amortization expense

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

based on our current estimate of useful lives, is estimated to be approximately \$663 million in 2017, \$552 million in 2018, \$439 million in 2019, \$342 million in 2020, and \$251 million in 2021.

(7) Long-Term Debt:

The activity in our long-term debt from January 1, 2016 to December 31, 2016 is summarized as follows.

(\$ in millions)	Year ended December 31, 2016					December 31, 2016	Interest Rate at December 31, 2016*
	January 1, 2016	Payments and Retirements	New Borrowings	Debt Assumed	Reclassifications		
Senior & Subsidiary							
Unsecured Debt	\$ 16,055	\$ (419)	\$ 401	\$ 500	\$ (637)	\$ 15,900	9.18%
Senior Secured Debt	-	(426)	1,940	-	637	2,151	3.88%
Secured Subsidiary Debt	-	-	-	100	-	100	8.50%
Secured Debt	23	(4)	-	-	-	19	4.50%
Rural Utilities Service Loan Contracts	8	-	-	-	-	8	6.15%
Total Long-Term Debt	\$ 16,086	\$ (849)	\$ 2,341	\$ 600	\$ -	\$ 18,178	8.55%
Less: Debt Issuance Costs	(196)					(209)	
Less: Debt Premium (Discount)	.2					(46)	
Less: Current Portion	(384)					(363)	
	\$ 15,508					\$ 17,560	

\* Interest rate includes amortization of debt issuance costs and debt premiums or discounts. The interest rates at December 31, 2016 represent a weighted average of multiple issuances.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

Additional information regarding our senior unsecured debt, senior secured debt and subsidiary debt at December 31, 2016 and 2015 is as follows:

(\$ in millions)	2016		2015	
	Principal Outstanding	Interest Rate	Principal Outstanding	Interest Rate
<b>Senior Unsecured Debt Due:</b>				
4/15/2017	\$ 210	8.250%	\$ 607	8.250%
10/1/2018	583	8.125%	583	8.125%
3/15/2019	434	7.125%	434	7.125%
4/15/2020	1,169	8.500%	1,022	8.500%
9/15/2020	1,066	8.875%	1,000	8.875%
7/1/2021	500	9.250%	500	9.250%
9/15/2021	775	6.250%	775	6.250%
4/15/2022	500	8.750%	500	8.750%
9/15/2022	2,188	10.500%	2,000	10.500%
1/15/2023	850	7.125%	850	7.125%
4/15/2024	750	7.625%	750	7.625%
1/15/2025	775	6.875%	775	6.875%
9/15/2025	3,600	11.000%	3,600	11.000%
11/1/2025	138	7.000%	138	7.000%
8/15/2026	2	6.800%	2	6.800%
1/15/2027	346	7.875%	346	7.875%
8/15/2031	945	9.000%	945	9.000%
10/1/2034	1	7.880%	1	7.680%
7/1/2035	125	7.450%	125	7.450%
10/1/2046	193	7.050%	193	7.050%
	<u>15,150</u>		<u>15,146</u>	
<b>Senior Secured Debt Due:</b>				
10/14/2016 <sup>(a)</sup>	-	-	344	2.805% (Variable)
10/24/2019 <sup>(b)</sup>	280	4.145% (Variable)	315	3.805% (Variable)
3/31/2021 <sup>(c)</sup>	1,564	3.270% (Variable)	-	-
10/12/2021 <sup>(d)</sup>	307	4.145% (Variable)	-	-
	<u>2,151</u>		<u>659</u>	
<b>Subsidiary Debentures Due:</b>				
5/15/2027	200	6.750%	-	-
2/1/2028	300	6.860%	-	-
2/15/2028	200	6.730%	200	6.730%
10/15/2029	50	8.400%	50	8.400%
11/15/2031	100	8.500%	-	-
	<u>850</u>		<u>250</u>	
<b>Total</b>	<u>\$ 18,151</u>	<u>8.30%</u> <sup>(e)</sup>	<u>\$ 16,055</u>	<u>8.74%</u> <sup>(e)</sup>

<sup>(a)</sup> Represents borrowings under the 2011 CoBank Credit Agreement, as defined below, that became secured as of April 1, 2016.

<sup>(b)</sup> Represents borrowings under the 2014 CoBank Credit Agreement, as defined below, that became secured as of April 1, 2016.

<sup>(c)</sup> Represents borrowings under the 2015 Credit Agreement, as defined below.

<sup>(d)</sup> Represents borrowings under the 2016 CoBank Credit Agreement, as defined below.

<sup>(e)</sup> Interest rate represents a weighted average of the stated interest rates of multiple issuances.

During 2016, we completed non-cash debt exchanges including related accrued interest, of \$397 million of our 8.25% Notes due April 2017 for approximately \$147 million of our 8.50% Notes due April 2020, \$66 million of our 8.875% Notes due September 2020, and \$188 million of our 10.50% Notes due September 2022. A pretax loss of approximately \$7 million was recognized and included in "Investment and other income, net" in our consolidated statement of operations for the year ended December 31, 2016.

On September 25, 2015, Frontier completed a private offering of \$6,600 million aggregate principal amount of unsecured Senior Notes, as follows: \$1,000 million of 8.875% Senior Notes due 2020; \$2,000 million of 10.50%

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

Senior Notes due 2022; and \$3,600 million of 11.00% Senior Notes due 2025. Each was issued at a price equal to 100% of its principal amount. Frontier used the net proceeds from the offering (after deducting underwriting fees) to finance a portion of the cash consideration paid in connection with the CTF Acquisition and to pay related fees and expenses. The net proceeds of the debt offering of \$6,485 million were included in "Restricted cash" in the consolidated balance sheet as of December 31, 2015. In June 2016, we completed an exchange offer of registered senior notes for the privately placed senior notes.

On August 12, 2015, Frontier entered into a credit agreement with JPMorgan Chase Bank, N.A., as administrative agent, and the lenders party thereto, for a \$1,500 million senior secured delayed-draw term loan facility (the 2015 Credit Agreement). Frontier exercised its right under the 2015 Credit Agreement to obtain additional commitments and increased the size of the facility to \$1,625 million. On April 1, 2016, in connection with the closing of the CTF Acquisition, Frontier drew \$1,550 million under that facility, with the additional \$75 million drawn subsequently. The final maturity date is March 31, 2021. Repayment of the outstanding principal balance will be made in quarterly installments, initially in the amount of \$20 million per installment, which commenced on June 30, 2016. The quarterly installments will increase to \$41 million, beginning with the 13th quarterly installment. The remaining outstanding principal balance will be repaid on the final maturity date. Borrowings under the term loan will bear interest based on margins over the Base Rate (as defined in the 2015 Credit Agreement) or LIBOR, at the election of Frontier. Interest rate margins under the facility (ranging from 0.75% to 1.75% for Base Rate borrowings and 1.75% to 2.75% for LIBOR borrowings) are subject to adjustment based on Frontier's Total Leverage Ratio (as defined in the 2015 Credit Agreement). Borrowings under the 2015 Credit Agreement are secured by a pledge of the stock of Frontier North Inc., a wholly owned subsidiary, primarily representing Frontier operations in the states of Illinois, Indiana, Michigan, Ohio and Wisconsin.

Upon completion of the CTF Acquisition on April 1, 2016, we assumed additional debt of \$600 million, including \$200 million aggregate principal amount of 6.75% Senior Notes due May 15, 2027, \$300 million aggregate principal amount of 6.86% Senior Notes due February 1, 2028 and \$100 million aggregate principal amount of 8.50% Senior Notes due November 15, 2031.

On February 5, 2015, we entered into a commitment for a bridge loan facility (the Verizon Bridge Facility) and recognized related interest expense of \$10 million and \$184 million for the years ended December 31, 2016 and 2015, respectively. The accrued liabilities related to the Verizon Bridge Facility of \$184 million were paid after the closing of the CTF Acquisition and were included in "Other current liabilities" in the consolidated balance sheet as of December 31, 2015. The Verizon Bridge Facility terminated, in accordance with its terms, on September 25, 2015.

Frontier has a credit agreement with CoBank, ACB, as administrative agent, lead arranger and a lender, and the other lenders party thereto, for a \$350 million senior unsecured term loan facility (the 2014 CoBank Credit Agreement). The facility was drawn upon closing of the Connecticut Acquisition with proceeds used to partially finance the acquisition. The maturity date is October 24, 2019. Repayment of the outstanding principal balance will be made in quarterly installments of \$9 million, which commenced on March 31, 2015 with the remaining outstanding principal balance to be repaid on the maturity date. Borrowings under the 2014 CoBank Credit Agreement will bear interest based on the margins over the Base Rate (as defined in the 2014 CoBank Credit Agreement) or LIBOR, at the election of Frontier. Interest rate margins under the facility (ranging from 0.875% to 2.875% for Base Rate borrowings and 1.875% to 3.875% for LIBOR borrowings) are subject to adjustments based on our Total Leverage Ratio, as such term is defined in the 2014 CoBank Credit Agreement. The interest rate on this facility at December 31, 2016 was LIBOR plus 3.375%.

Frontier has two senior secured credit agreements with CoBank, ACB, as administrative agent, lead arranger and a lender, and the other lenders party thereto: the first, drawn in 2011 (the 2011 CoBank Credit Agreement), was refinanced in October 2016 with a similar facility for \$315 million, maturing on October 12, 2021 (the 2016 CoBank Credit Agreement), and the second, drawn in 2014 (the 2014 CoBank Credit Agreement), matures on October 24, 2019. We refer to the 2011 CoBank Credit Agreement, the 2014 CoBank Credit Agreement and the 2016 CoBank Credit Agreement collectively as the CoBank Credit Agreements. Borrowings under the CoBank Credit Agreements are secured by a pledge of the stock of Frontier North, Inc.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

Repayment of the outstanding principal balance for the 2016 CoBank Credit Agreement is being made in quarterly installments of approximately \$8 million which began on December 31, 2016. Any remaining outstanding principal balance will be repaid on the final maturity date. Borrowings under the term loan will bear interest based on margins over the Base Rate (as defined in the 2016 CoBank Credit Agreement) or LIBOR, at the election of Frontier. Interest rate margins under the facility (ranging from 0.875% to 2.875% for Base Rate borrowings and 1.875% to 3.875% for LIBOR borrowings) are subject to adjustment based on Frontier's Total Leverage Ratio (as defined in the 2016 CoBank Credit Agreement). The term loan under the 2016 CoBank Credit Agreement is secured by a pledge of the stock of Frontier North Inc.

Frontier has a revolving credit agreement with JPMorgan Chase Bank, N.A., as administrative agent, the lenders party thereto and the other parties named therein (the Revolving Credit Agreement), for a \$750 million revolving credit facility (the Revolving Credit Facility) with a scheduled termination date of May 31, 2018. As of December 31, 2016, the Revolving Credit Facility was fully available and no borrowings had been made thereunder. Associated commitment fees under the Revolving Credit Facility will vary from time to time depending on our debt rating (as defined in the Revolving Credit Agreement) and were 0.45% per annum as of December 31, 2016. During the term of the Revolving Credit Facility, Frontier may borrow, repay and reborrow funds, and may obtain letters of credit, subject to customary borrowing conditions. Loans under the Revolving Credit Facility will bear interest based on the alternate base rate or the adjusted LIBO Rate (each as determined in the Revolving Credit Agreement), at our election, plus a margin based on our debt rating (ranging from 0.50% to 1.50% for alternate base rate borrowings and 1.50% to 2.50% for adjusted LIBO Rate borrowings). The interest rate on this facility would have been the alternate base rate plus 1.50% or the adjusted LIBO Rate plus 2.50%, respectively, as of December 31, 2016. Letters of credit issued under the Revolving Credit Facility will also be subject to fees that vary depending on our debt rating. The Revolving Credit Facility is available for general corporate purposes but may not be used to fund dividend payments.

On February 27, 2017, Frontier amended and restated its April 2021 term loan and its revolving credit facility, combining them into a single credit agreement and unifying the covenants. The amended and restated credit agreement provides Frontier with more flexible terms, increases the revolving credit facility to \$850 million and extends the maturity of the revolving credit facility from 2018 to 2022. The determination of interest rates remains unchanged. The most significant change in the covenants is an increase of the maximum Leverage Ratio (as defined) to 5.25 to 1.0 initially, migrating to 5.0 to 1.0 beginning in the second quarter of 2018, 4.75 to 1.0 in the second quarter of 2019, and 4.5 to 1.0 in the second quarter of 2020. In addition, under the amended and restated credit agreement, Frontier will be expanding the security package to include pledges of the equity interests in certain Frontier subsidiaries and guaranties by certain Frontier subsidiaries.

Upon the drawdown of the term loan under the 2015 Credit Agreement in connection with the closing of the CTF Acquisition, borrowings under the 2014 CoBank Credit Agreement, the 2011 CoBank Credit Agreement and the Revolving Credit Facility became secured debt. These borrowings are secured, equally and ratably with borrowings under the 2015 Credit Agreement, by a pledge of the stock of Frontier North Inc., a wholly owned subsidiary.

On September 17, 2014, Frontier completed a registered debt offering of \$775 million aggregate principal amount of 6.250% senior unsecured notes due 2021, and \$775 million aggregate principal amount of 6.875% senior unsecured notes due 2025. We received net proceeds, after deducting underwriting fees, of \$1,519 million from the offering. Frontier used the net proceeds from the offering of the notes, together with borrowings under the 2014 CoBank Credit Agreement, as defined above, and cash on hand, to finance the Connecticut Acquisition, which closed on October 24, 2014. See Note 3 for further discussion of the Connecticut Acquisition.

During 2015 and 2014, we also entered into secured financings totaling \$3 million and \$11 million, respectively, with four year terms and no stated interest rate for certain equipment purchases.

As of December 31, 2016, we were in compliance with all of our debt and credit facility covenants.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

Our scheduled principal payments are as follows as of December 31, 2016:

<u>(\$ in millions)</u>	<u>Principal Payments</u>	
2017	\$	363
2018	\$	733
2019	\$	818
2020	\$	2,429
2021	\$	2,554
Thereafter	\$	11,281

Other Obligations

During 2016, Frontier contributed a real estate property with a fair value of \$15 million for the purpose of funding a portion of its contribution obligations to its qualified defined benefit pension plan. The pension plan obtained independent appraisals of the property and, based on these appraisals, the pension plan recorded the contribution at its fair value of \$15 million. Frontier has entered into a lease for the contributed property with initial terms of 15 years at a combined aggregate annual rent of approximately \$2 million. The property is managed on behalf of the pension plan by an independent fiduciary, and the terms of the lease were negotiated with the fiduciary on an arm's-length basis.

The contribution and leaseback of the property was treated as a financing transaction and, accordingly, Frontier continues to depreciate the carrying value of the property in its financial statements and no gain or loss was recognized. An obligation of \$15 million was recorded in our consolidated balance sheet within "Other liabilities" and the liability is reduced annually by a portion of the lease payments made to the pension plan.

During 2016, Frontier modified certain operating leases for vehicles which resulted in the classification as capital leases. These agreements have lease terms of 1 to 7 years. These capital lease obligations are included in our consolidated balance sheet within "Other liabilities" and "Other current liabilities".

In 2012, Frontier entered into a sale and leaseback arrangement for a facility in Everett, Washington and entered into a capital lease for the use of fiber in the state of Minnesota. These agreements have lease terms of 12 and 23 years, respectively. These capital lease obligations are included in our consolidated balance sheet within "Other liabilities" and "Other current liabilities."

Future minimum payments for finance lease obligations and capital lease obligations as of December 31, 2016 are as follows:

<u>(\$ in millions)</u>	<u>Finance Lease Obligations</u>		<u>Capital Lease Obligations</u>	
Year ending December 31:				
2017	\$	9	\$	39
2018		9		37
2019		9		26
2020		9		15
2021		9		9
Thereafter		60		21
Total future payments		105		147
Less: Amounts representing interest		(57)		(18)
Present value of minimum lease payments	\$	48	\$	129

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

**(8) Restructuring Costs**

As of December 31, 2016, restructuring related liabilities of \$47 million pertaining to employee separation charges are included in "Other current liabilities" in our consolidated balance sheet.

During 2016, restructuring costs and other charges, primarily consisting of severance and other employee-related costs of \$65 million, and pension/OPEB benefit enhancements of \$26 million, totaling \$91 million in connection with workforce reductions, are included in "Restructuring costs and other charges" in our consolidated statement of operations for the year ended December 31, 2016.

The following is a summary of the changes in the liabilities established for restructuring programs at December 31, 2016:

*(\$ in millions)*

	Restructuring Liability	
Balance, January 1, 2016	\$	1
Severance costs		65
Cash payments during the period		(19)
Balance, December 31, 2016	\$	47

**(9) Investment and Other Income, Net:**

The components of investment and other income, net for the years ended December 31, 2016, 2015 and 2014 are as follows:

*(\$ in millions)*

	2016		2015		2014	
Interest and dividend income	\$	13	\$	7	\$	2
Loss on debt exchanges		(7)		-		-
Gain on sale of Fairmount Cellular LLC		-		-		25
Gain on sale of 700 MHz spectrum		-		-		12
Gain on expiration/settlement of customer advances		13		-		-
All other, net		1		-		-
Total investment and other income, net	\$	20	\$	7	\$	39

During 2016 and 2015, we received \$13 million and \$7 million, respectively, in interest and dividend income, primarily due to interest earned on restricted cash.

During 2016, we recognized income of \$13 million in connection with certain retained liabilities that have terminated, associated with customer advances for construction from our disposed water properties.

During 2014, we sold assets that were unrelated to Frontier's operations and recognized a gain of \$25 million associated with the sale of our interest in Fairmount Cellular LLC and recognized a gain of \$12 million related to the sale of our 700 MHz spectrum.

**(10) Capital Stock:**

We are authorized to issue up to 1,750,000,000 shares of common stock and 50,000,000 shares of preferred stock. The amount and timing of dividends payable on common and preferred stock are, subject to applicable law, within the sole discretion of our Board of Directors.

**Common Stock Offering**

On June 10, 2015, we completed a registered offering of 150,000,000 shares of our common stock, par value \$0.25 per share, at an offering price of \$5 per share. On June 24, 2015, Frontier issued an additional 15,000,000 shares of common stock in connection with the over-allotment option that was exercised in full by the underwriters. Aggregate net proceeds were approximately \$799 million after deducting commissions and

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

estimated expenses. We used the net proceeds from this offering to fund a portion of the acquisition price of the CTF Acquisition and related fees and expenses.

Mandatory Convertible Preferred Stock (Series A) Offering

On June 10, 2015, we also completed a registered offering of 17,500,000 shares of our 11.125% Mandatory Convertible Preferred Stock, Series A, par value \$0.01 per share (the "Series A Preferred Stock"), at an offering price of \$100 per share. On June 24, 2015, Frontier issued an additional 1,750,000 shares of Series A Preferred Stock in connection with the over-allotment option that was exercised in full by the underwriters. Aggregate net proceeds of the offering were \$1,866 million after deducting commissions and estimated expenses. We used the net proceeds from this offering to fund a portion of the acquisition price of the CTF Acquisition and related fees and expenses.

Unless converted earlier, each share of the Series A Preferred Stock will automatically convert on June 29, 2018 into common stock, (between 17.0213 and 20.0000 shares) depending on the applicable market value of our common stock, subject to anti-dilution adjustments. Subject to certain restrictions, at any time prior to June 29, 2018, holders of the Series A Preferred Stock may elect to convert all or a portion of their shares into common stock at the minimum conversion rate then in effect.

Dividends on shares of the Series A Preferred Stock are payable on a cumulative basis when, as and if declared by our Board of Directors (or an authorized committee thereof) at an annual rate of 11.125% on the liquidation preference of \$100.00 per share, on the last business day of March, June, September and December of each year, commencing on September 30, 2015 to, and including, the mandatory conversion date. Series A Preferred Stock dividends of \$214 million and \$120 million were paid in 2016 and 2015, respectively.

Pursuant to the terms of the CTF Acquisition, \$1,955 million of the \$2,665 million in net proceeds from the equity offerings were deposited into escrow and were included in "Restricted cash" in the consolidated balance sheet as of December 31, 2015. Upon closing of the CTF Acquisition, the funds were released and used to fund a portion of the purchase price.

(11) Stock Plans:

At December 31, 2016, we had six stock-based compensation plans under which grants were made and awards remained outstanding. No further awards may be granted under five of the plans: the 1996 Equity Incentive Plan (the 1996 EIP), the Amended and Restated 2000 Equity Incentive Plan (the 2000 EIP), the 2009 Equity Incentive Plan (the 2009 EIP), the Non-Employee Directors' Deferred Fee Equity Plan (the Deferred Fee Plan), and the Non-Employee Directors' Equity Incentive Plan (the Directors' Equity Plan and together with the Deferred Fee Plan, the Director Plans). At December 31, 2016, there were 20,000,000 shares authorized for grant and 7,324,000 shares available for grant under the 2013 Equity Incentive Plan (the 2013 EIP and together with the 1996 EIP, the 2000 EIP and the 2009 EIP, the EIPs). Our general policy is to issue shares from treasury upon the grant of restricted shares and the exercise of options.

1996, 2000, 2009 and 2013 Equity Incentive Plans

Since the expiration dates of the 1996 EIP, the 2000 EIP and the 2009 EIP on May 22, 2006, May 14, 2009 and May 8, 2013, respectively, no awards have been or may be granted under the 1996 EIP, the 2000 EIP and the 2009 EIP. Under the 2013 EIP, awards of our common stock may be granted to eligible employees in the form of incentive stock options, non-qualified stock options, SARs, restricted stock, performance shares or other stock-based awards. As discussed under the Non-Employee Directors' Compensation Plans below, prior to May 25, 2006 non-employee directors received an award of stock options under the 2000 EIP upon commencement of service. No awards may be granted more than 10 years after the effective date (May 8, 2013) of the 2013 EIP plan. The exercise price of stock options and SARs under the EIPs generally are equal to or greater than the fair market value of the underlying common stock on the date of grant. Stock options are not ordinarily exercisable on the date of grant but vest over a period of time (generally four years). Under the terms of the EIPs, subsequent stock dividends and stock splits have the effect of increasing the option shares outstanding, which correspondingly decrease the average exercise price of outstanding options.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial StatementsPerformance Shares

On February 15, 2012, Frontier's Compensation Committee, in consultation with the other non-management directors of Frontier's Board of Directors and the Committee's independent executive compensation consultant, adopted the Frontier Long-Term Incentive Plan (the LTIP). LTIP awards are granted in the form of performance shares. The LTIP is currently offered under Frontier's 2009 EIP and 2013 EIP, and participants consist of senior vice presidents and above. The LTIP awards have performance, market and time-vesting conditions.

Beginning in 2012, during the first 90 days of a three-year performance period (a Measurement Period), a target number of performance shares are awarded to each LTIP participant with respect to the Measurement Period. The performance metrics under the LTIP are (1) annual targets for operating cash flow based on a goal set during the first 90 days of each year in the three-year Measurement Period and (2) an overall performance "modifier" set during the first 90 days of the Measurement Period, based on Frontier's total return to stockholders (i.e., Total Shareholder Return or TSR) relative to the Integrated Telecommunications Services Group (GICS Code 50101020) for the three-year Measurement Period. Operating cash flow performance is determined at the end of each year and the annual results will be averaged at the end of the three-year Measurement Period to determine the preliminary number of shares earned under the LTIP award. The TSR performance measure is then applied to decrease or increase payouts based on Frontier's three year relative TSR performance. LTIP awards, to the extent earned, will be paid out in the form of common stock shortly following the end of the three-year Measurement Period.

On February 17, 2014, the Compensation Committee granted approximately 1,028,000 performance shares under the LTIP and set the operating cash flow performance goal for 2014, which applies to the first year in the 2014-2016 Measurement Period, the second year of the 2013-2015 Measurement Period and the third year of the 2012-2014 Measurement Period. On February 25, 2015, the Compensation Committee granted approximately 665,000 performance shares under the LTIP and set the operating cash flow performance goal for 2015, which applies to the first year in the 2015-2017 measurement period, the second year of the 2014-2016 measurement period and the third year of the 2013-2015 measurement period. On February 11, 2016, the Compensation Committee granted approximately 1,669,000 performance shares under the LTIP and set the operating cash flow performance goal for 2016, which applies to the first year in the 2016-2018 measurement period, the second year of the 2015-2017 measurement period and the third year of the 2014-2016 measurement period. The number of shares of common stock earned at the end of each three-year Measurement Period may be more or less than the number of target performance shares granted as a result of operating cash flow and TSR performance. An executive must maintain a satisfactory performance rating during the Measurement Period and must be employed by Frontier at the end of the three-year Measurement Period in order for the award to vest. The Compensation Committee will determine the number of shares earned for each three year Measurement Period in February of the year following the end of the Measurement Period.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

The following summary presents information regarding LTIP target performance shares as of December 31, 2016 and changes during the three years then ended with regard to LTIP shares awarded under the 2009 EIP and the 2013 EIP:

	Number of Shares (in thousands)
Balance at January 1, 2014	1,749
LTIP target performance shares granted	1,037
LTIP target performance shares forfeited	(104)
Balance at December 31, 2014	2,682
LTIP target performance shares granted	738
LTIP target performance shares earned	(743)
LTIP target performance shares forfeited	(152)
Balance at December 31, 2015	2,525
LTIP target performance shares granted	1,669
LTIP target performance shares earned	(887)
LTIP target performance shares forfeited	(448)
Balance at December 31, 2016	2,859

For purposes of determining compensation expense, the fair value of each performance share is measured at the end of each reporting period and, therefore, will fluctuate based on the price of Frontier common stock as well as performance relative to the targets. Frontier recognized an expense, included in "Selling, general, and administrative expenses" of \$6 million, \$7 million, and \$4 million during 2016, 2015 and 2014, respectively, for the LTIP.

Restricted Stock

The following summary presents information regarding unvested restricted stock as of December 31, 2016 and changes during the three years then ended with regard to restricted stock under the 2009 EIP and the 2013 EIP:

	Number of Shares (in thousands)	Weighted Average Grant Date Fair Value (per share)	Aggregate Fair Value (in millions)
Balance at January 1, 2014	6,234	\$ 4.80	\$ 29
Restricted stock granted	4,314	\$ 4.91	\$ 29
Restricted stock vested	(2,372)	\$ 5.22	\$ 16
Restricted stock forfeited	(369)	\$ 4.55	
Balance at December 31, 2014	7,807	\$ 4.75	\$ 52
Restricted stock granted	2,815	\$ 7.92	\$ 13
Restricted stock vested	(3,215)	\$ 4.89	\$ 15
Restricted stock forfeited	(359)	\$ 5.10	
Balance at December 31, 2015	7,048	\$ 5.93	\$ 33
Restricted stock granted	5,936	\$ 4.36	\$ 20
Restricted stock vested	(3,720)	\$ 5.26	\$ 13
Restricted stock forfeited	(908)	\$ 5.11	
Balance at December 31, 2016	8,356	\$ 5.20	\$ 28

For purposes of determining compensation expense, the fair value of each restricted stock grant is estimated based on the average of the high and low market price of a share of our common stock on the date of grant. Total remaining unrecognized compensation cost associated with unvested restricted stock awards that is deferred at December 31, 2016 was \$26 million and the weighted average vesting period over which this cost is expected to be recognized is approximately 1.3 years.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

We have granted restricted stock awards to employees in the form of our common stock. None of the restricted stock awards may be sold, assigned, pledged or otherwise transferred, voluntarily or involuntarily, by the employees until the restrictions lapse, subject to limited exceptions. The restrictions are time-based. Compensation expense, recognized in "Selling, general and administrative expenses", of \$18 million, \$20 million and \$16 million, for the years ended December 31, 2016, 2015 and 2014, respectively, has been recorded in connection with these grants.

Stock Options

The number of options exercisable under the EIPs at December 31, 2016, 2015 and 2014 were 40,000, 50,000 and 83,000, with a weighted average exercise price of \$8.81, \$13.40, and \$13.23, respectively. No stock options were granted or exercised during 2016, 2015 or 2014. There is no remaining unrecognized compensation cost associated with stock options at December 31, 2016.

Non-Employee Directors' Compensation Plans

As of October 1, 2013, stock units are credited to the director's account in an amount that is determined as follows: the total cash value of the fees payable to the director is divided by the closing price of Frontier common stock on the grant date of the units. Units are credited to the director's account quarterly. Directors must also elect to convert the units to either common stock (convertible on a one-to-one basis) or cash upon retirement or death.

Dividends are paid on stock units held by directors at the same rate and at the same time as we pay dividends on shares of our common stock. Dividends on stock units are paid in the form of additional stock units.

There were 10 directors participating in the Director Plans during all or part of 2016. The total plan units earned were 444,277, 334,188, and 237,607 in 2016, 2015 and 2014, respectively.

To the extent directors elect to receive the distribution of their stock unit account in cash, they are considered liability-based awards. To the extent directors elect to receive the distribution of their stock unit accounts in common stock, they are considered equity-based awards. Compensation expense for stock units that are considered equity-based awards is based on the market value of our common stock at the date of grant. Compensation expense for stock units that are considered liability-based awards is based on the market value of our common stock at the end of each period.

In connection with the Director Plans, there were no compensation costs associated with the issuance of stock units in 2016, (\$1) million in 2015, and \$4 million in 2014. Cash compensation associated with the Director Plans was \$1 million in 2016, 2015 and 2014, respectively. These costs are recognized in "Selling, general and administrative expenses".

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

(12) Income Taxes:

The following is a reconciliation of the provision for income taxes computed at the federal statutory rate to income taxes computed at the effective rates for the years ended December 31, 2016, 2015 and 2014:

	2016	2015	2014
Consolidated tax provision at federal statutory rate	35.0 %	35.0 %	35.0 %
State income tax provisions, net of federal income tax benefit	(0.1)	8.7	1.6
Tax reserve adjustment	0.6	(0.3)	6.9
Domestic production activities deduction	(1.9)	-	(8.7)
Changes in certain deferred tax balances	5.8	0.8	(14.1)
Federal research and development credit	1.0	1.5	(3.3)
Non-deductible transaction costs	-	0.4	1.0
All other, net	(0.2)	(0.3)	0.3
Effective tax rate	40.2 %	45.8 %	18.7 %

Income taxes for 2016 include the impact of \$36 million of tax benefits resulting primarily from the adjustment of deferred tax balances due to the CTF Acquisition, the impact of \$6 million in benefits from the Federal research and development credits, along with a \$12 million reversal of benefits related to the domestic production activities deduction.

Income taxes for 2015 include the impact of a \$3 million benefit arising from the adjustment of deferred tax balances and a \$5 million benefit from the federal research and development credit.

Income taxes for 2014 include the impact of a \$23 million benefit from the reduction in deferred tax liabilities arising primarily from the inclusion of the Connecticut operations in the state unitary filings, a \$14 million benefit from the domestic production activities deduction and a \$5 million benefit from federal research and development credits, partially offset by the impact of a charge of \$11 million resulting from an increase in tax reserves and a charge of \$2 million resulting from non-deductible transaction costs.

As a result of the retrospective implementation of Accounting Standards Update No. 2015-17, *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*, Frontier offset all deferred tax liabilities and assets, as well as any related valuation allowance, and is presenting them as a single non-current amount within Deferred income taxes in the consolidated balance sheet as of December 31, 2016 and 2015.

Amounts pertaining to income tax related accounts of \$55 million and \$50 million are included in "Income taxes and other current assets" in the consolidated balance sheets as of December 31, 2016 and 2015, respectively.

In 2016, we received federal and state income tax refunds totaling \$120 million.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

The components of the net deferred income tax liability (asset) at December 31 are as follows:

<i>(\$ in millions)</i>	2016	2015
<b><u>Deferred income tax liabilities:</u></b>		
Property, plant and equipment basis differences	\$ 2,751	\$ 2,401
Intangibles	878	960
Deferred revenue/expense	14	-
Other, net	12	15
	<u>\$ 3,655</u>	<u>\$ 3,376</u>
<b><u>Deferred income tax assets:</u></b>		
Pension liability	273	222
Tax operating loss carryforward	687	295
Employee benefits	255	262
Accrued expenses	44	50
Lease obligations	75	-
Tax credit	30	-
Allowance for doubtful accounts	44	10
Other, net	2	48
	<u>1,410</u>	<u>887</u>
Less: Valuation allowance	<u>(271)</u>	<u>(177)</u>
Net deferred income tax asset	<u>1,139</u>	<u>710</u>
Net deferred income tax liability	<u>\$ 2,516</u>	<u>\$ 2,666</u>

Our federal net operating loss carryforward as of December 31, 2016 is estimated at \$1.0 billion. The federal loss carryforward will expire in 2036, unless otherwise used.

Our state tax operating loss carryforward as of December 31, 2016 is estimated at \$6.7 billion. A portion of our state loss carryforward will continue to expire annually through 2036, unless otherwise used.

Our federal research and development credit and alternative minimum tax credit as of December 31, 2016 is estimated at \$13 million and \$4 million, respectively. The federal research and development credit will expire between 2034 and 2036, unless otherwise used.

Our various state credits as of December 31, 2016 are estimated at \$19 million. The state credits will expire between 2018 and 2021, unless otherwise used.

As of December 31, 2016, Frontier has a valuation allowance of \$271 million to reduce deferred tax assets to an amount more likely than not to be realized. This valuation allowance is related to state net operating losses and state tax credits. In evaluating Frontier's ability to realize its deferred tax assets, management considers whether it is more likely than not that some or all of the deferred tax assets will not be realized. Management also considered the projected reversal of deferred tax liabilities and projected future taxable income in making this assessment. Based upon this assessment, management believes it is more likely than not Frontier will realize the benefits of these deductible differences, net of valuation allowance. There was a valuation allowance of \$177 million recorded as of December 31, 2015.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

The provision (benefit) for federal and state income taxes, as well as the taxes charged or credited to equity of Frontier, includes amounts both payable currently and deferred for payment in future periods as indicated below:

<i>(\$ in millions)</i>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Income tax expense (benefit):			
Current:			
Federal	\$ (52)	\$ 8	\$ 98
State	7	(6)	10
Total Current	<u>(45)</u>	<u>2</u>	<u>108</u>
Deferred:			
Federal	(145)	(126)	(34)
State	(60)	(41)	(44)
Total Deferred	<u>(205)</u>	<u>(167)</u>	<u>(78)</u>
Total income tax expense (benefit)	<u>(250)</u>	<u>(165)</u>	<u>30</u>
Income taxes charged (credited) to equity of Frontier:			
Utilization of the benefits arising from restricted stock	(5)	-	-
Deferred income taxes (benefits) arising from the recognition of additional pension/OPEB liability	<u>(21)</u>	<u>36</u>	<u>(90)</u>
Total income taxes charged (credited) to equity of Frontier	<u>(26)</u>	<u>36</u>	<u>(90)</u>
Total income taxes	<u>\$ (276)</u>	<u>\$ (129)</u>	<u>\$ (60)</u>

U.S. GAAP requires applying a "more likely than not" threshold to the recognition and derecognition of uncertain tax positions either taken or expected to be taken in Frontier's income tax returns. The total amount of our gross tax liability for tax positions that may not be sustained under a "more likely than not" threshold amounts to \$17 million as of December 31, 2016 including interest of \$1 million. The amount of our uncertain tax positions, for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease during the next twelve months, and which would affect our effective tax rate, is \$8 million as of December 31, 2016.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

Frontier's policy regarding the classification of interest and penalties is to include these amounts as a component of income tax expense. This treatment of interest and penalties is consistent with prior periods. We are subject to income tax examinations generally for the years 2012 forward for federal and 2008 forward for state filing jurisdictions. We also maintain uncertain tax positions in various state jurisdictions.

The following table sets forth the changes in Frontier's balance of unrecognized tax benefits for the years ended December 31, 2016 and 2015:

<i>(\$ in millions)</i>	2016	2015
Unrecognized tax benefits - beginning of year	\$ 19	\$ 19
Gross increases - prior year tax positions	3	-
Gross increases - current year tax positions	3	2
Gross decreases - FIN 48 liability release	(9)	-
Gross decreases - expired statute of limitations	-	(2)
Unrecognized tax benefits - end of year	<u>\$ 16</u>	<u>\$ 19</u>

The amounts above exclude \$1 million of accrued interest as of December 31, 2016 and 2015, respectively, that we have recorded and would be payable should Frontier's tax positions not be sustained.

**(13) Net Income (Loss) Per Common Share:**

The reconciliation of the net income (loss) per common share calculation for the years ended December 31, 2016, 2015 and 2014 is as follows:

<i>(\$ in millions and shares in thousands, except per share amounts)</i>	2016	2015	2014
<u>Net income (loss) used for basic and diluted earnings (loss) per share:</u>			
Net income (loss) attributable to Frontier common shareholders	\$ (587)	\$ (316)	\$ 133
Less: Dividends paid on unvested restricted stock awards	(3)	(3)	(3)
Total basic and diluted net income (loss) attributable to Frontier common shareholders	<u>\$ (590)</u>	<u>\$ (319)</u>	<u>\$ 130</u>
<u>Basic earnings (loss) per share:</u>			
Total weighted average shares and unvested restricted stock awards outstanding - basic	1,172,131	1,091,798	1,001,812
Less: Weighted average unvested restricted stock awards	(8,032)	(7,192)	(7,394)
Total weighted average shares outstanding - basic	<u>1,164,099</u>	<u>1,084,606</u>	<u>994,418</u>
Basic net income (loss) per share attributable to Frontier common shareholders	<u>\$ (0.51)</u>	<u>\$ (0.29)</u>	<u>\$ 0.13</u>
<u>Diluted earnings (loss) per share:</u>			
Total weighted average shares outstanding - basic	1,164,099	1,084,606	994,418
Effect of dilutive shares	-	-	3,744
Total weighted average shares outstanding - diluted	<u>1,164,099</u>	<u>1,084,606</u>	<u>998,162</u>
Diluted net income (loss) per share attributable to Frontier common shareholders	<u>\$ (0.51)</u>	<u>\$ (0.29)</u>	<u>\$ 0.13</u>

In calculating diluted net loss per common share for the years ended December 31, 2016 and 2015, the effect of all common stock equivalents is excluded from the computation as the effect would be antidilutive.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements.

Stock Options

For the years ended December 31, 2016, 2015 and 2014, options to purchase 40,000, 50,000 and 83,000 shares, respectively, issuable under employee compensation plans were excluded from the computation of diluted earnings (loss) per share (EPS) for those periods because the exercise prices were greater than the average market price of our common stock and, therefore, the effect would be antidilutive.

Stock Units

At December 31, 2016, 2015 and 2014, we had 1,881,460, 1,437,183 and 1,102,995 stock units, respectively, issued under the Director Plans and the 2013 EIP. These securities have not been included in the diluted income per share of common stock calculation because their inclusion would have an antidilutive effect.

Mandatory Convertible Preferred Stock

The impact of the common share equivalents associated with the 19,250,000 shares of Series A Preferred stock described above were not included in the calculation of diluted EPS as of December 31, 2016 and 2015, as their impact was antidilutive.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

**(14) Comprehensive Income (Loss):**

Comprehensive income (loss) consists of net income (loss) and other gains and losses affecting shareholders' investment and pension/postretirement benefit (OPEB) liabilities that, under GAAP, are excluded from net income/(loss).

The components of accumulated other comprehensive loss, net of tax at December 31, 2016, 2015 and 2014, and changes for the years then ended, are as follows:

(\$ in millions)	Pension Costs	OPEB Costs	Deferred taxes on pension and OPEB costs	Total
Balance at January 1, 2014	\$ (412)	\$ (5)	\$ 156	\$ (261)
Other comprehensive income (loss) before reclassifications	(140)	(113)	98	(155)
Amounts reclassified from accumulated other comprehensive income (loss)	20	(1)	(7)	12
Net current-period other comprehensive income (loss)	(120)	(114)	91	(143)
Balance at December 31, 2014	(532)	(118)	247	(404)
Other comprehensive income (loss) before reclassifications	(81)	136	(24)	31
Amounts reclassified from accumulated other comprehensive income (loss)	29	3	(12)	20
Net current-period other comprehensive income (loss)	(52)	139	(36)	51
Balance at December 31, 2015	(584)	20	211	(353)
Other comprehensive income (loss) before reclassifications	(103)	17	32	(54)
Amounts reclassified from accumulated other comprehensive income (loss)	40	(8)	(12)	20
Net current-period other comprehensive income (loss)	(63)	9	20	(34)
Balance at December 31, 2016	\$ (647)	\$ 29	\$ 231	\$ (387)

As a result of the CTF Acquisition, the Frontier Communications Pension Plan (the Plan) was remeasured. This remeasurement resulted in a decrease in the discount rate from 4.50% at December 31, 2015 to 4.00% at the date of the CTF Acquisition. This change in the discount rate resulted in a remeasurement charge to Other comprehensive income (loss) of \$105 million during 2016.

**FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES**  
Notes to Consolidated Financial Statements

The significant items reclassified from each component of accumulated other comprehensive loss for the years ended December 31, 2016, 2015 and 2014 are as follows:

(\$ in millions) Details about Accumulated Other Comprehensive Loss Components	Amount Reclassified from Accumulated Other Comprehensive Loss <sup>(a)</sup>			Affected Line Item in the Statement Where Net Income (Loss) is Presented
	2016	2015	2014	
<b>Amortization of Pension Cost Items <sup>(b)</sup></b>				
Actuarial gains (losses)	\$ (40)	\$ (29)	\$ (20)	
Tax impact	(40)	(29)	(20)	Income (loss) before income taxes
	15	11	7	Income tax (expense) benefit
	\$ (25)	\$ (18)	\$ (13)	Net income (loss)
<b>Amortization of OPEB Cost Items <sup>(b)</sup></b>				
Prior-service costs	\$ 9	\$ 5	\$ 4	
Actuarial gains (losses)	(1)	(8)	(3)	Income (loss) before income taxes
Tax impact	8	(3)	1	Income tax (expense) benefit
	(3)	1	-	Net income (loss)
	\$ 5	\$ (2)	\$ 1	

(a) Amounts in parentheses indicate losses.

(b) These accumulated other comprehensive loss components are included in the computation of net periodic pension and OPEB costs (see Note 17 - Retirement Plans for additional details).

**(15) Segment Information:**

We operate in one reportable segment. Frontier provides both regulated and unregulated voice, data and video services to residential, business and wholesale customers and is typically the incumbent voice services provider in its service areas.

We have utilized the aggregation criteria to combine our seven regional operating segments because all of these regional operations share similar characteristics, in that they provide the same products and services to similar customers using comparable technologies in all of the states in which we operate. The regulatory structure is generally similar.

**(16) Quarterly Financial Data (Unaudited):**

(\$ in millions, except per share amounts)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total Year
<b>2016</b>					
Revenue	\$ 1,355	\$ 2,608	\$ 2,524	\$ 2,409	\$ 8,896
Operating income	58	311	264	255	888
Net loss attributable to Frontier common shareholders	(240)	(80)	(134)	(133)	(587)
Basic net loss per share attributable to Frontier common shareholders	\$ (0.21)	\$ (0.07)	\$ (0.12)	\$ (0.12)	\$ (0.51)
<b>2015</b>					
Revenue	\$ 1,371	\$ 1,368	\$ 1,424	\$ 1,413	\$ 5,576
Operating income	163	193	207	182	745
Net loss attributable to Frontier common shareholders	(51)	(28)	(81)	(156)	(316)
Basic net loss per share attributable to Frontier common shareholders	\$ (0.05)	\$ (0.03)	\$ (0.07)	\$ (0.14)	\$ (0.29)

The quarterly net income (loss) per share amounts are rounded to the nearest cent. Annual net income (loss) per share may vary depending on the effect of such rounding. The change in revenue, operating income, net

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

income (loss) and net income (loss) per share during the second quarter of 2016 and each subsequent quarter of 2016 reflects the additional results of the CTF operations related to the CTF Acquisition, as described further in Note 3.

We recognized \$11 million (\$7 million or \$0.01 per share after tax) and \$80 million (\$52 million or \$0.04 per share after tax) of restructuring costs and other charges during the third and fourth quarters of 2016, respectively.

We recognized \$1 million of restructuring costs and other charges during each of the third and fourth quarters of 2015.

We recognized \$138 million (\$85 million or \$0.07 per share after tax), \$127 million (\$76 million or \$0.07 per share after tax), \$122 million (\$74 million or \$0.06 per share after tax) and \$49 million (\$48 million or \$0.04 per share after tax) of acquisition and integration costs during the first, second, third and fourth quarters of 2016, respectively.

We recognized \$57 million (\$35 million or \$0.04 per share after tax), \$35 million (\$23 million or \$0.02 per share after tax), \$58 million (\$27 million or \$0.02 per share after tax) and \$86 million (\$47 million or \$0.04 per share after tax) of acquisition and integration costs during the first, second, third and fourth quarters of 2015, respectively.

(17) Retirement Plans:

We sponsor a noncontributory defined benefit pension plan covering a significant number of our former and current employees and other postretirement benefit plans that provide medical, dental, life insurance and other benefits for covered retired employees and their beneficiaries and covered dependents. The pension plan and postretirement benefit plans are closed to the majority of our newly hired employees. The benefits are based on years of service and final average pay or career average pay. Contributions are made in amounts sufficient to meet ERISA funding requirements while considering tax deductibility. Plan assets are invested in a diversified portfolio of equity and fixed-income securities and alternative investments.

The accounting results for pension and other postretirement benefit costs and obligations are dependent upon various actuarial assumptions applied in the determination of such amounts. These actuarial assumptions include the following: discount rates, expected long-term rate of return on plan assets, future compensation increases, employee turnover, healthcare cost trend rates, expected retirement age, optional form of benefit and mortality. We review these assumptions for changes annually with our independent actuaries. We consider our discount rate and expected long-term rate of return on plan assets to be our most critical assumptions.

The discount rate is used to value, on a present value basis, our pension and other postretirement benefit obligations as of the balance sheet date. The same rate is also used in the interest cost component of the pension and postretirement benefit cost determination for the following year. The measurement date used in the selection of our discount rate is the balance sheet date. Our discount rate assumption is determined annually with assistance from our independent actuaries based on the pattern of expected future benefit payments and the prevailing rates available on long-term, high quality corporate bonds that approximate the benefit obligation.

As of December 31, 2016, 2015 and 2014, we utilized an estimation technique that is based upon a settlement model (Bond:Link) that permits us to closely match cash flows to the expected payments to participants. This rate can change from year-to-year based on market conditions that affect corporate bond yields.

As a result of the technique described above, Frontier is utilizing a discount rate of 4.10% as of December 31, 2016 for its qualified pension plan, compared to rates of 4.50% and 4.10% in 2015 and 2014, respectively. The discount rate for postretirement plans as of December 31, 2016 was a range of 4.10% to 4.30% compared to a range of 4.50% to 4.70% in 2015 and 4.10% to 4.20% in 2014.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

As a result of the CTF Acquisition, the Frontier Communications Pension Plan (the Plan) was remeasured. This remeasurement resulted in a decrease in the discount rate from 4.50% at December 31, 2015 to 4.00% at the date of the CTF Acquisition. This change in the discount rate resulted in a remeasurement charge to other comprehensive income (loss) of \$105 million during 2016.

The expected long-term rate of return on plan assets is applied in the determination of periodic pension and postretirement benefit cost as a reduction in the computation of the expense. In developing the expected long-term rate of return assumption, we considered published surveys of expected market returns, 10 and 20 year actual returns of various major indices, and our own historical 5 year, 10 year and 20 year investment returns. The expected long-term rate of return on plan assets is based on an asset allocation assumption of 40% in long-duration fixed income securities, and 60% in equity securities and other investments. We review our asset allocation at least annually and make changes when considered appropriate. Our pension asset investment allocation decisions are made by the Retirement Investment & Administration Committee (RIAC), a committee comprised of members of management, pursuant to a delegation of authority by the Retirement Plan Committee of the Board of Directors. The RIAC is responsible for reporting its actions to the Retirement Plan Committee. Asset allocation decisions take into account expected market return assumptions of various asset classes as well as expected pension benefit payment streams. When analyzing anticipated benefit payments, management considers both the absolute amount of the payments as well as the timing of such payments. In 2016, 2015 and 2014, our expected long-term rate of return on plan assets was 7.50%, 7.75%, and 7.75%, respectively. For 2017, we will assume a rate of return of 7.50%. Our pension plan assets are valued at fair value as of the measurement date. The measurement date used to determine pension and other postretirement benefit measures for the pension plan and the postretirement benefit plan is December 31.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

Pension Benefits

The following tables set forth the pension plan's projected benefit obligations, fair values of plan assets and the pension benefit liability recognized on our consolidated balance sheets as of December 31, 2016 and 2015 and the components of total pension benefit cost for the years ended December 31, 2016, 2015 and 2014:

<i>(\$ in millions)</i>	2016	2015
<u>Change in projected benefit obligation (PBO)</u>		
PBO at beginning of year	\$ 2,142	\$ 2,210
Service cost	88	55
Interest cost	122	88
Actuarial (gain)/loss	137	(88)
Benefits paid	(155)	(128)
Connecticut Acquisition transfer	-	5
CTF Acquisition PBO	1,108	-
Special termination benefits	23	-
PBO at end of year	<u>\$ 3,465</u>	<u>\$ 2,142</u>
<u>Change in plan assets</u>		
Fair value of plan assets at beginning of year	\$ 1,572	\$ 1,673
Fair value of plan assets for the CTF operations as of acquisition date	1,120	-
Fair value of plan assets for the Connecticut Operations as of acquisition date	-	5
Actual return on plan assets	201	(40)
Employer contributions	28	62
Benefits paid	(155)	(128)
Fair value of plan assets at end of year	<u>\$ 2,766</u>	<u>\$ 1,572</u>
Funded status	<u>\$ (699)</u>	<u>\$ (570)</u>
<u>Amounts recognized in the consolidated balance sheet</u>		
Pension and other postretirement benefits - current	\$ -	\$ (9)
Pension and other postretirement benefits - noncurrent	<u>\$ (699)</u>	<u>\$ (561)</u>
Accumulated other comprehensive loss	<u>\$ 647</u>	<u>\$ 584</u>

In connection with the completion of the CTF Acquisition, certain employees were transferred to the Frontier Communications Pension Plan (the Plan) effective April 1, 2016. Assets of \$1,108 million related to the CTF Acquisition were transferred from Verizon and the Verizon pension plan trusts during 2016.

<i>(\$ in millions)</i>	2016	2015	2014
<u>Components of total pension benefit cost</u>			
Service cost	\$ 88	\$ 55	\$ 42
Interest cost on projected benefit obligation	122	88	80
Expected return on plan assets	(168)	(129)	(99)
Amortization of unrecognized loss	40	29	20
Net periodic pension benefit cost	<u>82</u>	<u>43</u>	<u>43</u>
Special termination benefits	23	-	-
Total pension benefit cost	<u>\$ 105</u>	<u>\$ 43</u>	<u>\$ 43</u>

The expected amortization of unrecognized loss in 2017 is \$35 million.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

We capitalized \$25 million, \$20 million and \$15 million of pension and OPEB expense into the cost of our capital expenditures during the years ended December 31, 2016, 2015 and 2014, respectively, as the costs relate to our engineering and plant construction activities

The plan's weighted average asset allocations at December 31, 2016 and 2015 by asset category are as follows:

<u>Asset category:</u>	<u>2016</u>	<u>2015</u>
Equity securities	50 %	47 %
Debt securities	38 %	46 %
Alternative investments	11 %	6 %
Cash and other	1 %	1 %
Total	<u>100 %</u>	<u>100 %</u>

The plan's expected benefit payments over the next 10 years are as follows

<u>(\$ in millions)</u>	<u>Amount</u>
2017	\$ 375
2018	308
2019	293
2020	281
2021	271
2022-2026	<u>1,224</u>
Total	<u>\$ 2,752</u>

We made total contributions to our pension plan of \$28 million during 2016 consisting of cash payments of \$13 million and the contribution of real property with a fair value of \$15 million, as described below.

See Note 7 for further discussion of a Frontier contribution of real estate property in 2016 with an aggregate fair value of \$15 million for the purpose of funding a portion of its contribution obligations to the Plan.

We made total cash contributions to our pension plan during 2015 and 2014 of \$62 million and \$83 million, respectively.

The accumulated benefit obligation for the plan was \$3,363 million and \$2,048 million at December 31, 2016 and 2015, respectively.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

Assumptions used in the computation of annual pension costs and valuation of the year-end obligations were as follows:

	2016	2015	2014
Discount rate - used at year end to value obligation	4.10 %	4.50 %	4.10 %
Discount rate - used to compute annual cost	4.50 %	4.10 %	4.90 %
Expected long-term rate of return on plan assets	7.50 %	7.75 %	7.75 %
Rate of increase in compensation levels	2.50 %	2.50 %	2.50 %

Postretirement Benefits Other Than Pensions—"OPEB"

The following tables set forth the OPEB plans' benefit obligations, fair values of plan assets and the postretirement benefit liability recognized on our consolidated balance sheets as of December 31, 2016 and 2015 and the components of total postretirement benefit cost for the years ended December 31, 2016, 2015 and 2014.

<u>(\$ in millions)</u>	2016	2015
<u>Change in benefit obligation</u>		
Benefit obligation at beginning of year	\$ 626	\$ 727
CTF Acquisition PBO	276	-
Service cost	19	19
Interest cost	37	30
Plan participants' contributions	5	5
Actuarial (gain)/loss	(18)	(115)
Benefits paid	(23)	(25)
Connecticut Acquisition transfer	-	5
Plan change	-	(20)
Special termination benefits	3	-
Benefit obligation at end of year	<u>\$ 925</u>	<u>\$ 626</u>
<u>Change in plan assets</u>		
Fair value of plan assets at beginning of year	\$ -	\$ -
Plan participants' contributions	5	5
Employer contribution	18	20
Benefits paid	(23)	(25)
Fair value of plan assets at end of year	<u>\$ -</u>	<u>\$ -</u>
Funded status	<u>\$ (925)</u>	<u>\$ (626)</u>
<u>Amounts recognized in the consolidated balance sheet</u>		
Pension and other postretirement benefits - current	<u>\$ (23)</u>	<u>\$ (24)</u>
Pension and other postretirement benefits - noncurrent	<u>\$ (902)</u>	<u>\$ (602)</u>
Accumulated other comprehensive (gain) loss	<u>\$ (29)</u>	<u>\$ (20)</u>

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

<u>(\$ in millions)</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
<u>Components of total postretirement benefit cost:</u>			
Service cost	\$ 19	\$ 19	\$ 11
Interest cost on projected benefit obligation	37	30	22
Amortization of prior service cost / (credit)	(9)	(5)	(4)
Amortization of unrecognized loss	1	8	3
Net periodic postretirement benefit cost	48	52	32
Special termination benefits	3	-	-
Total postretirement benefit cost	<u>\$ 51</u>	<u>\$ 52</u>	<u>\$ 32</u>

The expected amortization of prior service credit in 2017 is \$9 million and the expected amortization of unrecognized loss in 2017 is \$0.

Assumptions used in the computation of annual OPEB costs and valuation of the year-end OPEB obligations were as follows:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Discount rate - used at year end to value obligation	4.10% - 4.30%	4.50% - 4.70%	4.10% - 4.20%
Discount rate - used to compute annual cost	4.50% - 4.70%	4.10% - 4.20%	4.90% - 5.20%

The OPEB plan's expected benefit payments over the next 10 years are as follows:

<u>(\$ in millions)</u>	<u>Gross Benefit</u>	<u>Medicare Part D Subsidy</u>	<u>Total</u>
2017	\$ 24	-	\$ 24
2018	30	-	30
2019	38	-	38
2020	44	-	44
2021	49	-	49
2022-2026	298	1	299
Total	<u>\$ 483</u>	<u>\$ 1</u>	<u>\$ 484</u>

For purposes of measuring year-end benefit obligations, we used, depending on medical plan coverage for different retiree groups, a 7.00% annual rate of increase in the per-capita cost of covered medical benefits, gradually decreasing to 5.00% in the year 2024 and remaining at that level thereafter. The effect of a 1% increase in the assumed medical cost trend rates for each future year on the aggregate of the service and interest cost components of the total postretirement benefit cost would be \$1 million and the effect on the accumulated postretirement benefit obligation for health benefits would be \$20 million. The effect of a 1% decrease in the assumed medical cost trend rates for each future year on the aggregate of the service and interest cost components of the total postretirement benefit cost would be \$(1) million and the effect on the accumulated postretirement benefit obligation for health benefits would be \$(19) million.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

The amounts in accumulated other comprehensive (gain) loss that have not yet been recognized as components of net periodic benefit cost at December 31, 2016 and 2015 are as follows:

(\$ in millions)	Pension Plan		OPEB	
	2016	2015	2016	2015
Net actuarial loss	\$ 647	\$ 584	\$ 1	\$ 20
Prior service cost/(credit)	-	-	(30)	(40)
Total	\$ 647	\$ 584	\$ (29)	\$ (20)

The amounts recognized as a component of accumulated other comprehensive loss for the years ended December 31, 2016 and 2015 are as follows:

(\$ in millions)	Pension Plan		OPEB	
	2016	2015	2016	2015
Accumulated other comprehensive (gain) loss at beginning of year	\$ 584	\$ 532	\$ (20)	\$ 119
Net actuarial gain (loss) recognized during year	(40)	(29)	(1)	(8)
Prior service (cost) credit recognized during year	-	-	9	5
Net actuarial loss (gain) occurring during year	103	81	(17)	(136)
Net amount recognized in comprehensive income (loss) for the year	63	52	(9)	(139)
Accumulated other comprehensive (gain) loss at end of year	\$ 647	\$ 584	\$ (29)	\$ (20)

#### 401(k) Savings Plans

We sponsor employee retirement savings plans under section 401(k) of the Internal Revenue Code. The plans cover substantially all full-time employees. Under certain plans, we provide matching contributions. Employer contributions were \$48 million, \$28 million and \$21 million for 2016, 2015 and 2014, respectively.

#### (18) Fair Value of Financial Instruments:

Fair value is defined under GAAP as the exit price associated with the sale of an asset or transfer of a liability in an orderly transaction between market participants at the measurement date. Valuation techniques used to measure fair value under GAAP must maximize the use of observable inputs and minimize the use of unobservable inputs. In addition, GAAP establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value.

The three input levels in the hierarchy of fair value measurements are defined by the FASB generally as follows:

Input Level	Description of Input
Level 1	Observable inputs such as quoted prices in active markets for identical assets.
Level 2	Inputs other than quoted prices in active markets that are either directly or indirectly observable.
Level 3	Unobservable inputs in which little or no market data exists

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

The following tables represent Frontier's pension plan assets measured at fair value on a recurring basis as of December 31, 2016 and 2015.

(\$ in millions)	Fair Value Measurements at December 31, 2016			
	Total	Level 1	Level 2	Level 3
Cash and Cash Equivalents	\$ 42	\$ 42	\$ -	\$ -
U.S. Government Obligations	29	-	29	-
Corporate and Other Obligations	400	-	400	-
Common Stock	487	487	-	-
Common/Collective Trusts	1,104	-	1,104	-
Interest in Registered Investment Companies	334	334	-	-
Interest in Limited Partnerships and Limited Liability Companies	118	-	-	118
Total investments at fair value	\$ 2,514	\$ 863	\$ 1,533	\$ 118
Receivable for plan assets of the CTF Operations	258	-	-	-
Interest and Dividend Receivable	6	-	-	-
Due from Broker for Securities Sold	27	-	-	-
Receivable Associated with Insurance Contract	7	-	-	-
Due to Broker for Securities Purchased	(46)	-	-	-
Total Plan Assets, at Fair Value	\$ 2,766	-	-	-

(\$ in millions)	Fair Value Measurements at December 31, 2015			
	Total	Level 1	Level 2	Level 3
Cash and Cash Equivalents	\$ 23	\$ 23	\$ -	\$ -
U.S. Government Obligations	32	-	32	-
Corporate and Other Obligations	315	-	315	-
Common Stock	178	178	-	-
Common/Collective Trusts	894	-	894	-
Interest in Registered Investment Companies	49	49	-	-
Interest in Limited Partnerships and Limited Liability Companies	92	-	-	92
Total investments at fair value	\$ 1,583	\$ 250	\$ 1,241	\$ 92
Interest and Dividend Receivable	4	-	-	-
Due from Broker for Securities Sold	21	-	-	-
Receivable Associated with Insurance Contract	7	-	-	-
Due to Broker for Securities Purchased	(43)	-	-	-
Total Plan Assets, at Fair Value	\$ 1,572	-	-	-

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

There have been no reclassifications of investments between Levels 1, 2 or 3 assets during the years ended December 31, 2016 or 2015.

The tables below set forth a summary of changes in the fair value of the Plan's Level 3 assets for the years ended December 31, 2016 and 2015:

<i>(\$ in millions)</i>	Interest in Limited Partnerships and Limited Liability Companies	
	2016	2015
Balance, beginning of year	\$ 92	\$ 103
Realized gains	7	8
Unrealized losses	13	(11)
Purchases	15	-
Sales and distributions	(9)	(8)
Balance, end of year	<u>\$ 118</u>	<u>\$ 92</u>

F-45

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

The following table provides further information regarding the redemption of the Plan's Level 3 investments as of December 31, 2016:

<i>(\$ in millions)</i>	<u>Fair Value</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>	<u>Liquidation Period</u>
Interest in Limited Partnerships and Limited Liability Companies				
MS IFHF SVP LP Cayman <sup>(a)</sup>	\$ 1	Through liquidation of underlying investments	None	4 years
MS IFHF SVP LP Alpha <sup>(a)</sup>	1	Through liquidation of underlying investments	None	4 years
RII World Timberfund, LLC <sup>(b)</sup>	6	Through liquidation of underlying investments	None	10 years
426 E Casino Road, LLC <sup>(c)</sup>	15	Through liquidation of underlying investments	None	NA
100 Comm Drive, LLC <sup>(c)</sup>	9	Through liquidation of underlying investments	None	NA
100 CTE Drive, LLC <sup>(c)</sup>	13	Through liquidation of underlying investments	None	NA
6430 Oakbrook Parkway, LLC <sup>(c)</sup>	25	Through liquidation of underlying investments	None	NA
8001 West Jefferson, LLC <sup>(c)</sup>	26	Through liquidation of underlying investments	None	NA
1500 MacCorkle Ave SE, LLC <sup>(c)</sup>	14	Through liquidation of underlying investments	None	NA
400 S. Pike Road West, LLC <sup>(c)</sup>	1	Through liquidation of underlying investments	None	NA
601 N US 131, LLC <sup>(c)</sup>	1	Through liquidation of underlying investments	None	NA
9260 E. Stockton Blvd., LLC <sup>(c)</sup>	6	Through liquidation of underlying investments	None	NA
Total Interest in Limited Partnerships and Limited Liability Companies	<u>\$ 118</u>			

(a) The partnerships' investment objective is to seek capital appreciation principally through investing in investment funds managed by third party investment managers who employ a variety of alternative investment strategies. These instruments are subject to certain withdrawal restrictions. The Plan is in the process of liquidating its interest in the partnerships and distributions are expected to be made over the next four years.

(b) The fund's objective is to realize substantial long-term capital appreciation by investing in timberland properties primarily in South America and Australia. This investment is subject to certain withdrawal restrictions.

(c) The entity invests in commercial real estate properties that are leased to Frontier. The leases are triple net, whereby Frontier is responsible for all expenses, including but not limited to, insurance, repairs and maintenance and payment of property taxes.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

The following table represents the Plan's Level 3 financial instruments for its interest in certain limited partnerships and limited liability companies, which all use the direct capitalization valuation technique to measure the fair value of those financial instruments as of December 31, 2016, and the significant unobservable inputs and ranges of values for those inputs:

Instrument	Property	Fair Value	Capitalization Rate
Interest in Limited Partnerships and Limited Companies	426 E. Casino Road, LLC	\$ 15	7.00%
	100 Comm Drive, LLC	\$ 9	7.75%
	100 CTE Drive, LLC	\$ 13	9.00%
	6430 Oakbrook Parkway, LLC	\$ 25	7.75%
	8001 West Jefferson, LLC	\$ 26	8.50%
	1500 MacCorkle Ave SE, LLC	\$ 14	8.25%
	400 S. Pike Road West, LLC	\$ 1	8.50%
	601 N US 131, LLC	\$ 1	9.50%
	9260 E. Stockton Blvd., LLC	\$ 6	7.50%

The following table summarizes the carrying amounts and estimated fair values for long-term debt at December 31, 2016 and 2015. For the other financial instruments including cash, accounts receivable, restricted cash, long-term debt due within one year, accounts payable and other current liabilities, the carrying amounts approximate fair value due to the relatively short maturities of those instruments.

<u>(\$ in millions)</u>	2016		2015	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt	\$ 17,560	\$ 17,539	\$ 15,508	\$ 14,767

The fair value of our long-term debt is estimated based upon quoted market prices at the reporting date for those financial instruments.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements**(19) Commitments and Contingencies:**

Although from time to time we make short-term purchasing commitments to vendors with respect to capital expenditures, we generally do not enter into firm, written contracts for such activities.

In June 2015, Frontier accepted the Federal Communications Commission's (FCC) offer of support to price cap carriers under the Connect America Fund (CAF) Phase II program, which is intended to provide long-term support for broadband in high cost unserved or underserved areas. This program provides \$332 million in annual support, including \$49 million in annual support related to the properties acquired in the CTF Acquisition, through 2020 to make available 10 Mbps downstream/1 Mbps upstream broadband service to approximately 774,000 households across certain of the 29 states where we now operate. To the extent we do not enable the required number of households with 10 Mbps downstream/1 Mbps upstream broadband service by the end of the CAF Phase II term, we will be required to return a portion of the funds previously received.

On April 28, 2016, the FCC completed its inquiry into whether certain terms and conditions contained in specifically identified special access tariff pricing plans offered by four carriers, including Frontier, are just and reasonable. The FCC held that certain of the tariff terms for business data TDM services, specifically DS1s and DS3s, were unreasonable. Specifically, the FCC struck down "excessive" early termination fees and "all-or-nothing" provisions. Frontier has revised its tariffs in accordance with the FCC's Order. The FCC's decision has no retroactive effect, and we anticipate no material impact to Frontier from it.

The FCC deferred the issue of how its ruling will affect customers currently purchasing services from these tariffs to a Notice of Proposed Rulemaking. It is seeking comment on proposed changes to the way the FCC regulates traditional special access services and on a proposal to adopt pricing rules for Ethernet services in markets that are found to be "noncompetitive." The potential impact to Frontier of this proceeding is unknown, though any pending initiative could adversely affect our operations or financial results.

We are party to various legal proceedings (including individual, class and putative class actions) arising in the normal course of our business covering a wide range of matters and types of claims including, but not limited to, general contracts, billing disputes, rights of access, taxes and surcharges, consumer protection, trademark and patent infringement, employment, regulatory, tort, claims of competitors and disputes with other carriers.

In October 2013, the California Attorney General's Office notified certain Verizon companies, including one of the subsidiaries that we acquired in the CTF Acquisition, of potential violations of California state hazardous waste statutes primarily arising from the disposal of electronic components, batteries and aerosol cans at certain California facilities. We are cooperating with this investigation. While penalties relating to the alleged violations could exceed \$100,000, we do not expect that any penalties ultimately incurred will be material.

We accrue an expense for pending litigation when we determine that an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. Legal defense costs are expensed as incurred. None of our existing accruals for pending matters, after considering insurance coverage, is material. We monitor our pending litigation for the purpose of adjusting our accruals and revising our disclosures accordingly, when required. Litigation is, however, subject to uncertainty, and the outcome of any particular matter is not predictable. We will vigorously defend our interests in pending litigation, and as of this date, we believe that the ultimate resolution of all such matters, after considering insurance coverage or other indemnities to which we are entitled, will not have a material adverse effect on our consolidated financial position, results of operations, or our cash flows.

We conduct certain of our operations in leased premises and also lease certain equipment and other assets pursuant to operating leases. The lease arrangements have terms ranging from 1 to 99 years and several contain rent escalation clauses providing for increases in monthly rent at specific intervals. When rent escalation clauses exist, we record annual rental expense based on the total expected rent payments on a straight-line basis over the lease term. Certain leases also have renewal options. Renewal options that are reasonably assured are included in determining the lease term.

FRONTIER COMMUNICATIONS CORPORATION AND SUBSIDIARIES  
Notes to Consolidated Financial Statements

Future minimum rental commitments for all long-term noncancelable operating leases as of December 31, 2016 are as follows:

<u>(\$ in millions)</u>	<u>Operating Leases</u>	
Year ending December 31:		
2017	\$	91
2018		18
2019		18
2020		23
2021		21
Thereafter		76
Total minimum lease payments	<u>\$</u>	<u>247</u>

Total rental expense included in our consolidated statements of operations for the years ended December 31, 2016, 2015 and 2014 was \$137 million, \$119 million and \$100 million, respectively.

We are party to contracts with several unrelated long distance carriers. The contracts provide fees based on traffic they carry for us subject to minimum monthly fees.

At December 31, 2016, the estimated future payments for obligations under our noncancelable long distance contracts and service agreements are as follows:

<u>(\$ in millions)</u>	<u>Amount</u>	
Year ending December 31:		
2017	\$	42
2018		41
2019		7
2020		6
2021		2
Thereafter		10
Total	<u>\$</u>	<u>108</u>

At December 31, 2016, we have outstanding performance letters of credit as follows:

<u>(\$ in millions)</u>	<u>Amount</u>	
CNA Financial Corporation (CNA)	\$	49
AIG Insurance		75
All other		1
Total	<u>\$</u>	<u>125</u>

CNA serves as our agent with respect to general liability claims (auto, workers compensation and other insured perils of Frontier). As our agent, they administer all claims and make payments for claims on our behalf. We reimburse CNA for such services upon presentation of their invoice. To serve as our agent and make payments on our behalf, CNA requires that we establish a letter of credit in their favor. CNA could potentially draw against this letter of credit if we failed to reimburse CNA in accordance with the terms of our agreement. The amount of the letter of credit is reviewed annually and adjusted based on claims history.

None of the above letters of credit restrict our cash balances.



10-K 1 d313765d10k.htm FORM 10-K

Table of Contents


---



---

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

---

**Form 10-K**

---

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

For the fiscal year ended December 31, 2016

Commission File Numbers: 333-72440  
333-82124-02

---

**Mediacom Broadband LLC  
Mediacom Broadband Corporation\***  
(Exact names of Registrants as specified in their charters)

---

**Delaware  
Delaware**  
(State or other jurisdiction of  
incorporation or organization)

06-1615412  
06-1630167  
(I.R.S. Employer  
Identification Numbers)

1 Mediacom Way  
Mediacom Park, New York 10918  
(Address of principal executive offices)

(845) 443-2600  
(Registrants' telephone number)

Securities registered pursuant to Section 12(b) of the Exchange Act:  
None

Securities registered pursuant to Section 12(g) of the Exchange Act:  
None

---

Indicate by check mark if the Registrants are well-known seasoned issuers, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the Registrants are not required to file pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes  No

Indicate by check mark whether the Registrants (1) have filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the Registrants were required to file such reports), and (2) have been subject to such filing requirements for the past 90 days. Yes  No

Note: As voluntary filers, not subject to the filing requirements, the Registrants have filed all reports under Section 13 or 15(d) of the Exchange Act during the preceding 12 months.

Indicate by check mark whether the Registrants have submitted electronically and posted on their 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 Registrants were required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the Registrants' knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. Not Applicable.

Indicate by check mark whether the Registrants are large accelerated filers, accelerated filers, non-accelerated filers or smaller reporting companies. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

- Large accelerated filers
- Accelerated filers
- Non-accelerated filers
- Smaller reporting companies

Indicate by check mark whether the Registrants are shell companies (as defined in Rule 12b-2 of the Exchange Act). Yes  No

State the aggregate market value of the common equity held by non-affiliates of the Registrants: Not Applicable

Indicate the number of shares outstanding of the Registrants' common stock: Not Applicable

\* Mediacom Broadband Corporation meets the conditions set forth in General Instruction I (1) (a) and (b) of Form 10-K and is therefore filing this form with the reduced disclosure format.

Table of Contents

**MEDIACOM BROADBAND LLC  
2016 FORM 10-K ANNUAL REPORT  
TABLE OF CONTENTS**

		<u>Page</u>
<b><u>PART I</u></b>		
Item 1.	<u>Business</u>	4
Item 1A.	<u>Risk Factors</u>	20
Item 1B.	<u>Unresolved Staff Comments</u>	28
Item 2.	<u>Properties</u>	28
Item 3.	<u>Legal Proceedings</u>	28
Item 4.	<u>Mine Safety Disclosures</u>	29
<b><u>PART II</u></b>		
Item 5.	<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	29
Item 6.	<u>Selected Financial Data</u>	30
Item 7.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	32
Item 7A.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	45
Item 8.	<u>Financial Statements and Supplementary Data</u>	46
Item 9.	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	64
Item 9A.	<u>Controls and Procedures</u>	64
Item 9B.	<u>Other Information</u>	65
<b><u>PART III</u></b>		
Item 10.	<u>Directors, Executive Officers and Corporate Governance</u>	66
Item 11.	<u>Executive Compensation</u>	68
Item 12.	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	68
Item 13.	<u>Certain Relationships and Related Transactions, and Director Independence</u>	68
Item 14.	<u>Principal Accounting Fees and Services</u>	68
<b><u>PART IV</u></b>		
Item 15.	<u>Exhibits, Financial Statement Schedules</u>	69
Item 16.	<u>Summary</u>	69

This Annual Report on Form 10-K is for the year ended December 31, 2016. Any statement contained in a prior periodic report shall be deemed to be modified or superseded for purposes of this Annual Report to the extent that a statement herein modifies or supersedes such statement. The Securities and Exchange Commission ("SEC") allows us to "incorporate by reference" information that we file with them, which means that we can disclose important information by referring you directly to those documents. Information incorporated by reference is considered to be part of this Annual Report.

Mediacom Broadband LLC is a Delaware limited liability company and a wholly-owned subsidiary of Mediacom Communications Corporation, a Delaware corporation. Mediacom Broadband Corporation is a Delaware corporation and a wholly-owned subsidiary of Mediacom Broadband LLC. Mediacom Broadband Corporation was formed for the sole purpose of acting as co-issuer with Mediacom Broadband LLC of debt securities and does not conduct operations of its own.

References in this Annual Report to "we," "us," or "our" are to Mediacom Broadband LLC and its direct and indirect subsidiaries (including Mediacom Broadband Corporation), unless the context specifies or requires otherwise. References in this Annual Report to "Mediacom" or "MCC" are to Mediacom Communications Corporation.

## Table of Contents

### **Cautionary Statement Regarding Forward-Looking Statements**

You should carefully review the information contained in this Annual Report and in other reports or documents that we file from time to time with the SEC.

In this Annual Report, we state our beliefs of future events and of our future financial performance. In some cases, you can identify those so-called "forward-looking statements" by words such as "anticipates," "believes," "continue," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "should" or "will," or the negative of those and other comparable words. These forward-looking statements are not guarantees of future performance or results, and are subject to risks and uncertainties that could cause actual results to differ materially from historical results or those we anticipate as a result of various factors, many of which are beyond our control. Factors that may cause such differences to occur include, but are not limited to:

- increased levels of competition from direct broadcast satellite operators, local phone companies, other cable providers, wireless communications companies, providers of over-the-top video, and other services that compete for our customers;
- lower demand for our services from existing and potential residential and business customers due to increased competition, weakened economic conditions or other factors;
- our ability to contain the continued increases in video programming costs, or to raise video rates to offset, in whole or in part, the effects of such costs, including retransmission consent fees;
- an acceleration in bandwidth consumption by high-speed data customers at rates greater than current expectations, which could require unplanned network investments and meaningfully increase our capital expenditures;
- our ability to continue to grow our business services customer base, and associated revenues, which has continued to make increasing contributions to our results of operations;
- our ability to realize the anticipated benefits from the major initiatives under MCC's plan for approximately \$1 billion in total capital expenditures during the three years ending December 31, 2018, as further described in this Annual Report;
- our ability to successfully adopt new technologies and introduce new products and services, or enhance existing ones, to meet customer demands and preferences;
- our ability to secure hardware, software and operational support for the delivery of products and services to consumers;
- disruptions or failures of our network and information systems, including those caused by "cyber-attacks," natural disasters or other events outside our control;
- our reliance on certain intellectual property rights, and not infringing on the intellectual property rights of others;
- our ability to generate sufficient cash flows from operations to meet our debt service obligations;
- our ability to refinance future debt maturities on favorable terms, if at all;
- changes in assumptions underlying our critical accounting policies;
- changes in legislative and regulatory matters that may cause us to incur additional costs and expenses; and
- other risks and uncertainties discussed in this Annual Report for the year ended December 31, 2016 and other reports or documents that we file from time to time with the SEC.

Statements included in this Annual Report are based upon information known to us as of the date that this Annual Report is filed with the SEC, and we assume no obligation to update or alter our forward-looking statements made in this Annual Report, whether as a result of new information, future events or otherwise, except as required by applicable federal securities laws.

**Table of Contents****PART I****ITEM 1. BUSINESS****Mediacom Communications Corporation**

We are a wholly-owned subsidiary of Mediacom Communications Corporation (“Mediacom” or “MCC”). MCC is the fifth largest cable operator in the U.S., serving almost 1.4 million residential and business customer relationships in smaller markets primarily in the Midwest and Southeast. MCC offers a wide array of information, communications and entertainment services to households and businesses, including video, high-speed data (“HSD”), phone, and home security and automation. Through Mediacom Business, MCC provides scalable broadband communications solutions to commercial and public sector customers of all sizes, and sells advertising and production services under the OnMedia brand.

MCC’s cable systems are owned and operated through our operating subsidiaries and those of Mediacom LLC, another wholly-owned subsidiary of MCC. As of December 31, 2016, MCC’s cable systems passed an estimated 2.8 million homes and served approximately 828,000 video customers, 1,156,000 HSD customers and 479,000 phone customers, aggregating 2.5 million primary service units (“PSUs”).

MCC is a privately-owned company. An entity wholly-owned by Rocco B. Commisso and related parties is the sole shareholder of MCC, a C corporation. Mr. Commisso is MCC’s founder, Chairman and Chief Executive Officer. MCC manages us pursuant to management agreements with our operating subsidiaries. See Note 9 in our Notes to Consolidated Financial Statements.

**Mediacom Broadband LLC**

We are a holding company and do not have any operations or hold any assets other than our investments in our operating subsidiaries. As of December 31, 2016, our cable systems passed an estimated 1.5 million homes and served approximately 463,000 video customers, 643,000 HSD customers and 264,000 phone customers, aggregating 1.4 million PSUs. As of the same date, our cable systems served 754,000 residential and business customer relationships.

Our phone number is (845) 443-2600 and our principal executive offices are located at 1 Mediacom Way, Mediacom Park, New York, 10918. Our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and any amendments to such reports filed with or furnished to the SEC under sections 13(a) or 15(d) of the Securities Exchange Act of 1934 are made available free of charge on MCC’s website ([www.mediacomcc.com](http://www.mediacomcc.com)) as soon as reasonably practicable after such reports are electronically filed with or furnished to the SEC. The information posted on MCC’s website is not incorporated into our SEC filings.

**Recent Developments***MCC’s Capital Plan*

In 2016, MCC announced a plan for approximately \$1 billion of total capital expenditures to be made by us and Mediacom LLC during the three years ending December 2018 (“MCC’s Capital Plan”). Among the planned initiatives under MCC’s Capital Plan include:

- “Project Gigabit,” a wide-scale deployment of next-generation DOCSIS 3.1 technology that allows the provisioning of 1 gigabit per second (“Gbps”) HSD service to substantially all of MCC’s homes passed;
- “Project Open Road,” which will connect over 70,000 new commercial locations that contain multiple potential customers in an effort to continue to grow business services revenues at an accelerated rate;
- Residential line extensions resulting in at least 50,000 additional homes passed; and
- Development of community Wi-Fi access points throughout high-traffic commercial and public areas.

During the year ended December 31, 2016, MCC made an aggregate \$335.2 million of capital expenditures, of which \$179.9 million was invested by us. We expect similar levels of capital investments by us and MCC over each of the next two years, with our portion of the initiatives outlined above approximating a level that is commensurate with our capital expenditures as a percentage of MCC’s total capital expenditures. We have already made meaningful progress under MCC’s Capital Plan, including the recent announcement that MCC has become the first major U.S. cable company to have fully installed the necessary equipment to transition to the DOCSIS 3.1 platform. We believe these initiatives will allow us to continue to improve our competitive position for both residential and business services customers in our markets, with additional future revenue and cash flow growth driven by incremental gains in market share than we would have experienced otherwise.



## Table of Contents

### **Description of Our Business**

The following table provides an overview of selected operating data for our cable systems as of December 31:

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Estimated homes passed (1)	1,504,000	1,496,000	1,499,000	1,495,000	1,493,000
<i>Video</i>					
Video customers (2)	463,000	480,000	500,000	528,000	558,000
Video penetration (3)	30.8%	32.1%	33.4%	35.3%	37.4%
<i>High Speed Data</i>					
HSD customers (4)	643,000	605,000	564,000	534,000	505,000
HSD penetration (5)	42.8%	40.4%	37.6%	35.7%	33.8%
<i>Phone</i>					
Phone customers (6)	264,000	239,000	218,000	207,000	190,000
Phone penetration (7)	17.6%	16.0%	14.5%	13.8%	12.7%
<i>Primary Service Units (PSUs)</i>					
PSUs (8)	1,370,000	1,324,000	1,282,000	1,269,000	1,253,000
PSU penetration (9)	91.1%	88.5%	85.5%	84.9%	83.9%
<i>Customer Relationships</i>					
Customer relationships (10)	754,000	732,000	710,000	710,000	708,000

- (1) Estimated homes passed represent the number of single residence homes, apartments and condominium units that we can connect to our distribution system without further extending the transmission lines, based on best available information.
- (2) Represents customers receiving video service. Business services video customers that are billed on a bulk basis are converted into equivalent video customers by dividing their associated revenues by the applicable full-price residential video rate, which is generally consistent with the methodology used in determining payments made to programmers. Video customers include connections to schools, libraries, local government offices and employee households that may not be charged for basic or expanded video service, but may be charged for higher tier video, HSD, phone or other services. Our methodology of calculating the number of video customers may not be identical to those used by other companies offering similar services.
- (3) Represents video customers as a percentage of estimated homes passed.
- (4) Represents customers receiving HSD service. Small- to medium-sized business HSD customers are converted to equivalent HSD customers by dividing their associated revenues by the applicable full-price residential HSD rate. Medium- to large-sized business customers who take our enterprise network services are not counted as HSD customers. Our methodology of calculating HSD customers may not be identical to those used by other companies offering similar services.
- (5) Represents HSD customers as a percentage of estimated homes passed.
- (6) Represents customers receiving phone service. Small- to medium-sized business phone customers are converted to equivalent phone customers by dividing their associated revenues by the applicable full-price residential phone rate. Customers who take our IP-enabled voice trunk service are not counted as phone customers. Our methodology of calculating phone customers may not be identical to those used by other companies offering similar services.
- (7) Represents phone customers as a percentage of estimated homes passed.
- (8) Represents the sum of video, HSD and phone customers.
- (9) Represents PSUs as a percentage of our estimated homes passed.
- (10) Represents the total number of residential and business customers that receive at least one service, without regard to the amount of or which service(s) customers purchase.

### **Services**

We offer video, HSD and phone services individually and in bundled packages to residential and small- to medium-sized business ("SMB") customers over our hybrid fiber and coaxial cable ("HFC") network, and provide fiber-based network and transport services to medium- and large-sized businesses, governments and educational institutions. We also sell advertising to local, regional and national advertisers on television and digital platforms, and offer home security and automation services to residential customers.

## Table of Contents

Our services are typically offered on a subscription basis, with installation fees, monthly rates and related charges associated with the services, equipment and features customers choose. We generally offer discounted packages for new customers, and for those who take multiple services. Customers are typically billed in advance on a monthly basis, and additional charges may apply for installation and other one-time items. Residential customers are generally not subject to minimum-term contracts, while substantially all of our business services customers are under contracts that typically have 3 to 7 year terms.

### **Our Service Areas**

Approximately 75% of our homes passed are in the top 110 television markets in the United States, or designated market areas (“DMAs”), substantially all of which rank between the 65<sup>th</sup> and 110<sup>th</sup> largest.

Our largest markets are:

- Des Moines and Cedar Rapids, Iowa;
- The Quad Cities area in Illinois and Iowa, comprising Bettendorf, Davenport, East Moline, Moline and Rock Island;
- Springfield, Jefferson City and Columbia, Missouri; and
- Columbus, Albany and Valdosta, Georgia.

### **Residential Services**

We market our residential services individually and in bundled packages, with discounts generally available for the subscription to bundled packages or other combinations of services. As of December 31, 2016, approximately 57% of our residential customers took two or more of our services, including about 25% that took all three.

#### *Video*

We offer a wide variety of video services, with multiple packages, tiers and equipment options to appeal to a variety of customer preferences and demographics. Residential video customers are charged a monthly fee that varies depending on the level of video service and equipment taken, with additional revenues generated from one-time installation expenses, video-on-demand (“VOD”) fees and other ancillary purchases.

Our residential video customers receive, at a minimum, a limited basic tier that includes local broadcast stations and public, government and leased access channels, with additional packages and tiers available that include national cable networks and regional sports networks, foreign-language and international programming, digital music channels and other specialty programming. Video customers may also subscribe to premium network programming from HBO, Showtime, Starz and Cinemax that provides commercial-free original programming, movies, live and taped sporting events and concerts, and other special events. We have recently introduced “skinny bundles” as a value proposition to video customers that do not require certain national and regional sports networks, but seek a lower cost option that offers most of the non-sports content in our most popular video packages. Most of our video programming, including many titles in our VOD library, is available in a high-definition (“HD”) format that offers a higher resolution picture, improved audio quality and a wide-screen format.

Our VOD service provides video customers access to over 27,000 titles, including a wide selection of movies, national broadcast and cable network shows, music videos, and locally produced events. Most of our VOD content carries no additional charge when customers take a content package that includes the affiliated content. Special event programs, including live concerts, sporting events, and first-run movies are also available on a pay-per-view basis. Our digital video recorder (“DVR”) service allows customers to record and store content to view at their convenience, along with the ability to pause and rewind live programming.

Our video service generally requires the use of a digital set-top box (“set-top”), which typically provides an interactive, on-screen program guide and access to our VOD library. A rapidly increasing number of our video customers take our next-generation Internet Protocol (“IP”) set-top that offers a cloud-based, graphically-rich TiVo guide with integrated access and search functionality to certain Internet-based, or “over-the-top,” (“OTT”) video services such as Netflix, Hulu, and YouTube, along with a multi-room DVR service and the ability to download certain content to personal devices. In 2017, we plan to introduce a new, lower-cost, IP set-top that offers the TiVo guide and OTT video services, but without the required equipment for DVR service.

## Table of Contents

We also enable video customers to watch certain programming on personal devices connected to the Internet connection, whether in or outside their home, which we refer to as "TV Everywhere." Our video customers currently have access to online content for up to 76 channels, and we plan to further expand our "TV Everywhere" line-up in 2017. Our video customers that take a set-top with the TiVo guide may also remotely view programming listings and schedule and manage DVR recordings remotely through our mobile apps and online portal.

### *HSD*

We offer high-speed Internet access to suit the requirements of our HSD customers, with minimum downstream speeds of 60 megabits per second ("Mbps"), and packages available that provide downstream speeds up to 200 Mbps. Through Project Gigabit, we have installed the necessary equipment to transition substantially all our homes passed to the DOCSIS 3.1 platform, which will allow us to introduce packages offering speeds of up to 1 Gbps across most of our markets in 2017. We will also deploy community Wi-Fi access points throughout high-traffic commercial and public areas in our markets, which we believe will add additional value for our HSD customers.

Our residential HSD customers are charged a monthly fee that varies depending on the speeds and usage allowance associated with their level of HSD service. Our residential HSD service requires a modem, which most of our customers lease from us for a monthly fee. We also offer wireless gateways that combine a modem with a wireless router and phone adapter for an additional monthly fee, which ensures the performance of multiple personal devices used at the same time.

### *Phone*

Our residential phone customers enjoy unlimited nationwide calling and other popular features, including Caller ID, call waiting, call forwarding, three-way calling and, for those who also take our video service, the ability to receive Caller ID information on the customer's television. Residential phone customers are charged a monthly fee, with voicemail services, directory assistance and international calling plans made available for an additional fee. Our residential phone service requires equipment that is either included in the wireless gateway taken by many customers that take both HSD and phone service, or is typically leased by our customers for a monthly fee.

### **Business Services**

Mediacom Business provides SMB customers video, HSD and phone services similar to those offered to our residential customers, along with a multi-line phone service, music services and other features. We also furnish custom fiber solutions, with transmission speeds up to 10 Gbps, for medium- and large-sized businesses and institutions, with IP-enabled trunk-based voice services, and point-to-point, multi-point wide area, and local area network solution. We also supply high-capacity fiber transport and dedicated Internet access to national and regional carriers to support cell tower backhaul, Ethernet and regional transport. Our initiation of "Project Open Road" will extend our network to tens of thousands of new commercial locations that contain multiple businesses, in an effort to sustain or accelerate our rate of growth in business services revenues.

### **Advertising**

We sell advertising and production services to local, regional and national customers under our OnMedia brand. As part of the programming agreements with national cable networks, we generally receive an allocation of scheduled advertising time, typically two minutes per hour, and insert commercials during this allotted time. Our local sales team generally sells the placement of advertising and, in certain markets, we have entered into agreements with other cable operators in the same DMA where we sell advertising on behalf of these other operators, or vice versa, facilitating customers' ability to purchase local advertising in multiple markets. We also sell digital ad placement and other media services as an extension of our advertising business.

### **Marketing and Sales**

We employ a wide range of sales channels to reach current and potential customers, including outbound telemarketing, direct mail, in-bound customer care centers, retail locations, door-to-door field technician sales, and an e-commerce site. Customers are directed to our inbound call centers or website through various forms of advertising, including television advertising on our own cable systems. Mediacom Business has a dedicated sales force and outbound telemarketing, and we have several relationships with third-party agents who sell our services. Xtream is our marketing brand for bundled packages that include video with DVR service and set-tops with the TiVo guide, HSD with a wireless gateway, and phone service. We believe the simplified pricing and value proposition of our Xtream bundles has positively influenced the market's perception of our products and services, and has driven higher levels of sales activity.



## Table of Contents

### **Customer Care**

We continue to make investments that improve the reliability and quality of our services to enhance our customers' experience. Our field operations team focuses on providing a quality experience during installation and service calls, with the goal of resolving any technical issues on the first attempt. We offer 30 minute arrival windows and evening and weekend availability for installation and service calls to provide more convenient scheduling for our customers. Field activity is scheduled and routed seamlessly with remote dispatching and workflow management and GPS systems that facilitate on-time arrival for customer appointments. Our technicians are equipped with diagnostic and monitoring tools that determine the quality of service at the customer's home in real-time.

Our customer care group has multiple contact centers with dedicated customer service, sales, and technical support representatives available at all times, and our virtual contact center allows us to manage resources efficiently and effectively function as a single, unified call center. Our website and mobile applications allow customers to manage their billing account, utilize self-help tools and schedule appointments. Customers who are seeking to speak to an agent for further assistance may use the "call back" feature where our technical staff will call the customer when available, eliminating the need for excessive wait times. We maintain a strong presence on many social networking websites and message boards, including Facebook and Twitter, allowing us the ability to be more proactive in customer service, along with providing customers another point of contact.

### **Technology**

Our services are delivered through a fiber-rich, technologically-advanced, route-diverse network that consists of a national backbone; large-scale, centralized platforms; regional networks and headends; neighborhood nodes; and last-mile connectivity to customer homes or businesses. We utilize an IP ring architecture that minimizes service outages through its redundant design, and our network operations center supports and continuously monitors our network. We believe our network infrastructure provides several advantages over most of our competitors, including significantly more bandwidth capacity, greater reliability and higher quality of service.

Our national backbone is connected to leading carriers, with a presence in several major carrier hotels, and allows us to introduce new services across all our markets and realize greater economic efficiencies and scale. Our national backbone connects centralized platforms that control video content delivery, HSD and phone services, provisioning, customer care and email, and provides access to several aggregation and exchange points in our regional networks to ensure network redundancy and enhanced quality of service.

The last-mile connectivity is delivered through our HFC network, transporting content via laser-fed fiber-optic cable by regional networks and headends to local nodes, and by coaxial cable from these nodes to our customers. We have installed back-up power supplies that are intended to allow our services to continue to be available in the event of a commercial power outage. For certain business customers that have high-capacity requirements, we extend fiber-optic cable from the node site directly to the customer's premise.

HSD customers have consumed rapidly increasing amounts of bandwidth over the last several years, largely driven by increased usage of OTT video, and we expect this trend to continue. To provide additional network capacity to facilitate meaningful bandwidth consumption increases, we have deployed multiple tools to recapture bandwidth and optimize our network to allow for faster HSD speeds and greater levels of capacity. In substantially all of our markets, we have converted video service to an "all-digital" delivery platform, freeing up spectrum that was previously used to deliver analog video signals that require more capacity. We have installed the necessary equipment to transition to the DOCSIS 3.1 platform in substantially all of our markets, which allows us to use our existing network capacity in a more efficient manner. These bandwidth reclamation and optimization efforts have enabled continuing increases in the speeds and usage allowances in our HSD service packages, and we will further increase our maximum speeds to 1 Gbps in many of our markets in 2017.

### **Community Relations**

We are dedicated to fostering strong relations with the communities we serve and believe our local involvement strengthens the awareness and favorable perception of our brand. We support local charities and community causes with scholarships, events and campaigns to raise funds and supplies for persons in need, and in-kind donations that include production services and free airtime on cable networks. As of December 31, 2016, we provided free video service to over 1,700 schools and free HSD service to over 200 schools, and also provided free video service to over 1,600 government buildings, libraries and not-for-profit hospitals, nearly 200 of which also receive free HSD service.

## Table of Contents

### Franchises

As of December 31, 2016, we served 501 communities under non-exclusive franchises granted to us by local or state governmental authorities. Many of the provisions of local franchises are subject to federal regulation under the Communications Act of 1934, as amended (the "Cable Act"). Our franchises typically impose numerous conditions, including requirements around construction of the cable network in certain of the franchise areas; customer service requirements; the broad categories of programming required; the provision of free service to schools and other public institutions; and the provision and funding of public access channels. Many of the provisions of local franchises are subject to a fee based on gross revenues of specified cable services that we typically pass through directly to the customer. The Cable Act prohibits such franchise fees from exceeding 5%.

We believe that we have satisfactory relationships with our franchising communities, and have never had a franchise revoked, or had a community refuse to consent to a franchise transfer to us. The Cable Act provides comprehensive renewal procedures, which require that an incumbent franchisee's renewal application be assessed on its own merits and not as part of a comparative process with competing applications. For more information around our franchises, see "Legislation and Regulation – *State and Local Regulation – Franchise Matters.*"

### Sources of Supply

#### *Programming*

The programming content carried by our cable systems is generally obtained pursuant to fixed-term contracts with suppliers whose compensation is typically based on a fixed monthly fee per video customer, subject to contractual escalations. Most of our contracts are entered into directly with the programmers, but we also secure content through a programming cooperative in certain cases where we receive more favorable pricing or terms than are available to us independently. In general, we attempt to secure longer-term programming contracts, ranging from three to eight years. We also have various retransmission consent agreements that permit us to retransmit the signals of local broadcast television stations. Under FCC rules, local broadcast stations must elect, on a three-year cycle, either "must-carry" rights or "retransmission consent," where we are not allowed to carry the station's signals without its permission. Retransmission consent is generally conditioned upon our payment of cash fees and/or our carriage of one or more of their affiliated stations or programming networks.

Programming expenses have historically been our largest single expense item, and these costs have historically increased substantially more than the inflation rate on a per-unit basis, particularly for sports programming and retransmission consent. Consolidation among media companies and independent broadcast station groups has been significant over the past several years, and may further continue. As a result of such consolidation, many popular cable networks are owned by large media conglomerates, and many local broadcast stations are owned by large independent television broadcast groups that own, control or represent a significant number of local broadcast stations across the country and, in some cases, multiple stations in the same market.

Moreover, many of those powerful owners of programming require us to purchase their content in bundles and dictate how we offer them to our customers. Consequently, we have little or no ability to individually or selectively negotiate for networks or broadcast stations, to forego purchasing networks or stations that generate low customer interest, to offer sports programming services, such as ESPN and regional sports networks, on one or more separate tiers, or to offer networks or stations on an a la carte basis to give our customers more choice and potentially lower their costs. In many instances, such programmers have created additional networks and migrated popular programming, particularly sports programming, to these new networks, which has contributed to the increases in our programming costs. Additionally, we believe certain programmers may also demand higher fees from us in an effort to partially offset declines in their advertising revenue as more advertisers allocate a greater portion of their spending to Internet advertising. All of these practices increase our programming expense, and while such growth in programming expenses can be offset, in whole or in part, by rate increases to our video customers, our video gross margins will continue to decline if they cannot be fully offset.

#### *HSD Service*

We deliver HSD service through route-diverse fiber networks that are owned by us or leased from third parties and through backbone networks that are operated by third parties. We pay fees for leased circuits based on the amount of capacity and for Internet connectivity based on the amount of HSD traffic over the provider's network.

#### *Phone Service*

Our phone service is delivered through a Voice over Internet Protocol ("VoIP") platform over a route-diverse infrastructure. We source certain services from outside parties to support our phone service, the most significant of which are long-distance services from a

number of Tier 1 carriers, E911 database management, and leased circuits from incumbent local exchange carriers (“ILECs”).

## Table of Contents

### *Set-Tops, Programming Guides, Cable Modems and Network Equipment*

We purchase set-tops from a limited number of suppliers, principally Arris Group Inc., and lease these devices to customers on a monthly basis. We provide our customers with set-top program guides from TiVo Inc. and Rovi Corporation. We mainly purchase cable modems from Hitron Technologies and Technicolor SA, and routers, switches and other network equipment from Cisco Systems, Casa Technology Systems and Huawei Technologies Co. Ltd.

### **Competition**

We face competition for residential and business customers from a wide range of communication, entertainment and information services. Our residential video, HSD and phone services have historically faced, and continue to face, intense competition from existing providers in the areas of price, product offerings and service reliability. Rapid technological advances and changes in consumer behavior and demands have led to an increasing number of companies that offer new products and services that compete with ours, including OTT video and wireless Internet and phone services. Our business services generally compete with existing providers who may have a stronger foothold and customer penetration in our markets, and we continue to face a number of challengers for advertising sales.

Many of our current and potential future competitors have strong brand name recognition and significant financial resources, which may allow them to react to technological developments or changes in consumer behavior quicker than us. Recent consolidation has resulted in certain competitors becoming larger and offering additional services. AT&T's acquisition of DirecTV in 2015 enhanced their ability to offer bundled wireline and wireless services, and facilitated their recent launch of "DirecTV Now," an OTT video service that competes with ours. In 2016, AT&T announced a proposed merger with Time Warner Inc. which, if completed, would integrate a variety of video content with its established distribution platforms. Further consolidation may occur in the future, which may further pressure our competitive position.

### *Video*

#### *Direct Broadcast Satellite ("DBS") Providers*

We face our most significant competition for video customers from DBS providers, principally DirecTV, which is owned by AT&T, and DISH Network, whom offer satellite-delivered video packages and collectively have over 33 million video customers throughout the U.S., based on publicly filed information. These DBS providers offer similar video packages to ours, including certain features we may not provide including ad-skipping functionality and exclusive content such as DirecTV's agreement with the National Football League. DBS providers also have certain other advantages over us, including a national brand and marketing platform, and greater operational efficiencies resulting from their ability to avoid certain expenses which we incur, principally franchise fees and property taxes. We believe aggressive promotional pricing and advanced customer equipment offered by these DBS providers have contributed to our historical video customer losses.

#### *Phone Companies*

Certain phone companies have built fiber-based networks that allow them to offer video service, which is then bundled with Internet, phone and, in some cases, wireless, services. As of December 31, 2016, approximately 5% and 4% of our homes passed faced wireline video competition from AT&T U-Verse and CenturyLink Prism, respectively, based on internal estimates. The video services offered by these phone companies are substantially similar to ours. In markets where phone companies do not offer wireline video service, they have typically bundled their Internet and/or phone services with a DBS video service.

#### *Other Overbuilders*

We compete with other operators known as "overbuilders" that operate under non-exclusive franchises granted by local authorities and offer video service to markets representing approximately 24% (excluding the phone companies noted above) of our homes passed. The level of competition provided by these overbuilders varies, depending on the quality of their network and services offered, but they generally market bundled packages similar to ours. Some of these competitors, including municipally-owned entities, may be granted franchises on more favorable terms than ours, or enjoy other advantages, such as exemptions from property taxes or regulatory requirements, and pole rental charges, to which we are subject. We believe there has been limited expansion of such entities in our markets in the past several years.

## Table of Contents

### *OTT Video*

Our video service faces increasing competition from a variety of OTT video providers that offer streaming and downloading of video content over the Internet, often available for a monthly subscription priced meaningfully lower than our video service, or free of charge. These services have become increasingly accessible as technological advances have facilitated the ability of consumers to watch OTT video on their television and a variety of platforms and devices. The quality and amount of content offered by these providers continues to improve, and some OTT video services, including Netflix, Hulu and Amazon Prime Video have also recently introduced high-quality original content that is exclusive to their respective service. OTT video packages have also been recently made available, or will soon become available including DISH's SlingTV, DirecTV Now, YouTube TV and Hulu that replicate the linear video experience and provide additional competition to our video service. Additionally, certain content providers, including HBO, Showtime and CBS, have begun selling their programming direct to consumers over the Internet, bypassing distribution by a traditional video provider and additional content providers have announced intentions to do so in 2017 and beyond.

If OTT video providers continue to add popular content, including services that offer linear video, substitution of our video services may accelerate. Additionally, because OTT video is very popular with younger demographics, there may be an increasing substitution of traditional video if newly formed households were more likely to choose one or several OTT video services as their only video provider. However, we believe most OTT video services are used to supplement traditional video, and we have facilitated their usage by integrating many third-party video services on our next-generation set-top. While increasing use of OTT video services may lead to lower demand for our VOD and, to a lesser extent, video service in general, we expect the associated bandwidth requirements will result in greater HSD customer growth and retention given our competitive position.

### *Other*

We also face competition for our video service from over-the-air broadcast television, of which the extent of such competition for our video service is dependent on the quality and quantity of broadcast signals available through an "off-air" antenna.

## **HSD**

### *Phone Companies*

Our HSD service faces its most significant competition from local phone companies, including CenturyLink, AT&T and Windstream, that generally offer digital subscriber line ("DSL") Internet service, which is limited by technical constraints to maximum speeds considerably slower than ours. These phone companies generally market their DSL service at a lower price than our HSD service, but in certain markets where they have upgraded portions of their network to allow for faster speeds, their higher-speed DSL tiers were typically available at similar or higher prices than ours.

Some phone companies have upgraded portions of their network to a fiber-to-the-node ("FTTN") system that allows for Internet speeds comparable to our 60 Mbps service or fiber-to-the-home ("FTTH") systems, which are capable of providing Internet speeds as fast as our highest speeds. AT&T and CenturyLink have upgraded their networks to FTTN delivery systems in several of our markets, and AT&T has committed to deploying FTTH service to 12.5 million nation-wide locations within four years of their 2016 acquisition of DirecTV. We do not compete with FTTH services in a meaningful number of our markets. We generally believe our markets have been a lower priority for these phone companies, given the higher costs associated with building out such fiber networks in lower density markets such as ours, as compared to larger metropolitan markets. However, we may face greater competition for HSD customers if these companies were to continue, or accelerate, the deployment of fiber in markets which we compete.

### *Wireless Providers*

We also face competition from wireless providers such as AT&T, Verizon Wireless, T-Mobile and Sprint that offer third and fourth generation, or "3G" and "4G," wireless Internet service. While certain households or individuals with minimal bandwidth requirements may fully substitute their wireline Internet service for a wireless one, we do not believe that wireless Internet service offers a full replacement to our HSD service given higher data usage costs, slower speeds and lower reliability. However, the level of competition provided by wireless Internet services may increase in the future with the deployment of fifth generation, or "5G" technology and the recent introduction of packages with unlimited bandwidth consumption.

### *Other*

Our HSD service also faces limited competition from other providers, including many of the overbuilders noted above, and certain municipalities and commercial entities that have built fiber networks and offer Internet service that competes with ours. In a limited



## **Table of Contents**

number of markets outside our service area, Google has launched a FTTH service, and has announced plans to expand to additional markets. Some local governments in our footprint are considering or actively pursuing the subsidized build out of additional fiber and/or Wi-Fi networks. Our HSD service also faces competition from certain commercial venues, such as retail shopping areas, restaurants and airports that offer Wi-Fi Internet service, sometimes free of charge. If any of these providers were to significantly expand services in our markets, we would face additional competitive pressures.

### ***Phone***

Our phone service faces its most significant competition from the phone companies noted above that offer wireline phone service that is substantially similar to ours and, increasingly, from the wireless providers noted above. As households continue to utilize cell phones as their only phone service, the number of customers taking a wireline phone service has meaningfully declined, a trend we believe will continue.

Our phone service also competes with providers of IP-based phone services such as Vonage, Skype and magicJack, and from other forms of communication such as text and video messaging.

### ***Business Services***

Our business services primarily compete for SMB customers with local phone companies, many of which have had a historical advantage given long-term relationships with such customers, a nation-wide footprint that allows them to more effectively serve multiple locations, and existing networks built in certain commercial areas that we do not currently serve. However, in recent years, we have aggressively marketed our business services and expanded our network into additional commercial areas, which have led to significant customer and revenue increases associated with business services, which we expect to continue.

Our cell tower backhaul and enterprise-level services also face competition from these local phone companies as well as other carriers, including metro and regional fiber-based carriers.

### ***Advertising***

We compete for the sale of advertising against a wide variety of media outlets, including local broadcast stations, national broadcast networks, national and regional programming networks, local radio broadcast stations, local and regional newspapers, magazines and Internet sites. Competition has increased and will likely continue to increase as digital and other new formats for advertising seek to attract the same advertisers.

### ***Other Competition***

We also face competition for all of our services with all other sources of leisure, news, information and entertainment, including movies, sporting or other live events, radio broadcasts, home video services, console games, print media and the Internet. There can be no assurance that these or other existing, proposed, or as yet undeveloped technologies will not become dominant in the future and render our products and services less profitable or even obsolete.

### **Employees**

As of December 31, 2016, we had 2,445 employees. None of our employees are organized under, or covered by, a collective bargaining agreement. We consider our relations with our employees to be satisfactory.

## Table of Contents

### **Legislation and Regulation**

#### *General*

Federal, state and local laws regulate the development and operation of cable systems and, to varying degrees, the services we offer. Significant legal requirements imposed on us because of our status as a cable operator, or by virtue of the services we offer, are described below.

Many of our operations are regulated to a varying degree under different provisions of federal law, principally Title I (information services), Title II (telecommunications services) and Title VI (cable services) of the Communications Act of 1934, as amended (“Communications Act”).

#### *Recent Significant FCC Activity*

##### *HSD Regulatory Reclassification and Network Neutrality*

In 2015, the FCC adopted its Open Internet Order changing the historical classification of HSD Services, commonly referred to as broadband Internet access services (“BIAS”), from lightly regulated Title I information services to telecommunications services subject to regulation under Title II of the Communications Act. Although the FCC acted to forebear enforcement of many of Title II’s provisions, the FCC may rescind any or all such forbearance at will. With the Republicans in charge of both houses of Congress and the White House, reports have circulated that legislation may be introduced to undo in whole or in part the effect of the 2015 Order. We cannot predict if such changes will be adopted or what the impact of those changes may be.

The Open Internet Order established three “bright line rules” that restrict blocking of content, throttling of speed and paid prioritization of traffic (giving certain traffic priority in return for consideration). More generally, a provider of BIAS also cannot unreasonably interfere with or unreasonably disadvantage: (i) consumers’ ability to select, access or use lawful content, applications, services or devices; or (ii) edge providers’ ability to make lawful content, applications, services or devices available to consumers. To determine what conduct is “reasonable” or “unreasonable,” the FCC will resolve complaints on a case-by-case basis. Until complaints are filed and resolved, the scope of permitted conduct is not known and this creates regulatory uncertainty.

The Open Internet Order mandates additional consumer disclosures regarding promotional rates, fees, surcharges and data caps or allowances, and packet loss measures. Network management practices must continue to be disclosed with the added requirement of disclosure if a network practice is likely to significantly affect an end user’s use of the service. The Open Internet Order distinguishes so-called “legitimate network management” practices from other business practices. Our interconnections with other networks in order to exchange broadband traffic are now subject to FCC regulation. These arrangements will be regulated on a case-by-case basis if and as complaints are filed. Until complaints against ISPs are filed and resolved, it is difficult to determine the standards that distinguish permitted from proscribed conduct and, therefore, the potential impact upon our existing interconnection arrangements or future needs.

On October 27, 2016, the FCC adopted new privacy and data security requirements for BIAS providers pursuant to its Title II authority. These include specific disclosures and the timing of such disclosures, enhanced choice by subscribers over the use of sensitive data and data breach notification requirements. On March 1, 2017, the FCC stayed the effective date of the new rules to allow time to work with the Federal Trade Commission to create a comprehensive and consistent framework with respect to online privacy. We cannot predict if or when new rules will be issued or what effect they will have, if any, on our business.

We provide HSD services to business customers. On April 28, 2016, the FCC adopted a Tariff Investigation Order and Further Notice of Proposed Rulemaking that sought, among other things, to impose price caps on the provision of business data services. In late January 2017, a proposed order was removed from the FCC’s list on items on circulation, meaning that it could no longer be voted upon. It is unclear whether the proposed order will be reinstated, the new FCC Chairman would propose an alternative order or no order would be issued at all.

##### *Preemption of State Restriction of Municipal-Based Broadband Systems*

In a limited number of our markets, our products and services face competition from municipally owned electric utilities that have constructed telecommunications systems. Certain of the states in which we operate have adopted laws that impose conditions upon the conduct of a telecommunications business by local municipalities. For example, some states may require voter approval and prohibit cross-subsidization of the telecommunications business by electric, gas and water utility customers. In 2015, the FCC adopted a Memorandum Opinion and Order preempting certain state laws imposing restrictions or conditions upon the ability of municipal

utilities in North Carolina and Tennessee to offer or expand broadband service. However, on August 10, 2016, the United States Court of Appeals for the Sixth Circuit struck down the FCC's ban and the FCC did not to appeal.

## Table of Contents

### *Federal Telecommunications Act Rewrite*

Members of Congress have discussed undertaking a rewrite of the telecommunications laws that is necessary to develop laws that can be applied on a technology- and platform-neutral basis. Currently, each technology, regardless of whether it offers a similar service, e.g., multichannel video programming, broadband access or phone service, is regulated in a silo subject to a different regulatory regime. Such treatment often disadvantages one technology compared to others. We cannot predict whether such a rewrite and/or network neutrality legislation to establish a statutory framework to replace the Open Internet Order will occur. Any changes in regulation that would result from a rewrite could affect all of our products and services, the outcome of which, if any, cannot be predicted.

### *Privacy and Data Security*

How we collect, use, disclose and retain personally identifiable information and other sensitive information about our customers and what we do in the event of a data security breach is governed by federal and state laws. In addition, many states in which we operate have also enacted customer privacy statutes, including obligations to notify customers when certain customer information is accessed or believed to have been accessed without authorization. These state provisions are in some cases more restrictive than those in federal law.

The Cable Act imposes a number of restrictions on the manner in which cable operators can collect, disclose and retain data about individual system customers and requires cable operators to take actions to prevent unauthorized access to such information. The statute also requires that the system operator periodically provide all customers with written information about its policies, including the types of information collected; the use of such information; the nature, frequency and purpose of any disclosures; the period of retention; the times and places where a customer may have access to such information; the limitations placed on the cable operator by the Cable Act; and a customer's enforcement rights. In the event that a cable operator is found to have violated the customer privacy provisions of the Cable Act, it could be required to pay damages, attorneys' fees and other costs. Certain of these Cable Act requirements have been modified by more recent federal laws. Other federal laws currently impact the circumstances and the manner in which we disclose certain customer information and future federal legislation may further impact our obligations.

As more fully discussed in the *Recent Significant FCC Activity – HSD Regulatory Reclassification and Network Neutrality* section above, our HSD Service has become subject to new requirements, some of which have and others which are scheduled to take effect, regarding the collection, use and disclosure of certain customer, usage and network information.

In addition to any privacy laws that may apply to our provision of VoIP services, we must comply with additional privacy provisions contained in the FCC's CPNI regulations related to certain telephone customer records. In addition to employee training programs and other operating and disciplinary procedures, the CPNI rules require establishment of customer authentication and password protections, limit the means that we may use for such authentication, and provide customer approval prior to certain types of uses or disclosures of CPNI.

### *Pole Attachment Regulation*

The Cable Act requires certain public utilities, including all local telephone companies and electric utilities, except those owned by municipalities and co-operatives, to provide cable operators and telecommunications carriers with nondiscriminatory access to poles, ducts, conduits and rights-of-way at just and reasonable rates. This right of access is beneficial to us. Federal law also requires the FCC to regulate the rates, terms and conditions imposed by such public utilities for cable systems' use of utility pole and conduit space unless state authorities have demonstrated to the FCC that they adequately regulate pole attachment rates, as is the case in certain states in which we operate. In the absence of state regulation, the FCC will regulate pole attachment rates, terms and conditions only in response to a formal complaint. The FCC established a rate formula which governs the maximum rate certain utilities may charge for attachments to their poles and conduit by companies providing telecommunications services, including cable operators.

In 2011, the FCC adopted an Order modifying the pole attachment rules to promote broadband deployment. Previously, poles subject to the FCC attachment rules used a formula that resulted in lower rates for cable attachments and higher rates for telecommunication services attachments. The FCC had previously ruled that the provision of Internet services would not, in and of itself, trigger use of this new formula and the U.S. Supreme Court affirmed this decision.

Pursuant to the FCC's 2011 Order, the telecommunications attachment rate formula would yield results that would approximate the attachment rates for cable television operators. On November 17, 2015, the FCC adopted an Order on Reconsideration that revised the FCC's pole attachment rate formula to lessen the disparity between the cable and telecommunications rates that arose under certain

factual scenarios. As a result, in almost all circumstances the cable and telecommunications rates now approximate each other. Thus, even though it remains unclear whether the reclassification of broadband service as a telecommunications service pursuant to the Open

## Table of Contents

Internet Order discussed more fully in *Recent Significant FCC Activity – HSD Regulatory Reclassification and Network Neutrality* above, will impact our ability to continue to seek attachment rates computed as a cable operator as opposed to as a telecommunications provider, the practical effect of that distinction has been virtually eliminated. However, to the extent the FCC's action lowers the pole attachment costs of our competitors, that could adversely impact us.

### *Universal Service Fund*

In recent years, the FCC has adopted a series of reforms to the Universal Service Fund ("USF") support mechanism to help to make broadband available to areas that do not have or would not have broadband service. In addition, the FCC has expanded the types of services that must contribute to the USF. Since 2006, VoIP providers must contribute to the USF, and the FCC has a pending rulemaking that, if adopted, could impose fees on currently non-assessable services such as broadband Internet access.

Any increased costs resulting from having to contribute to USF, however, would increase our cost of service to consumers and that could adversely affect our business. We cannot predict how these various changes either may add costs or burdens to our existing VoIP and broadband services or how they may potentially benefit those who provide competing services.

### *Cable System Operations and Video Services*

#### *Federal Regulation*

Title VI of the Communications Act, referred to as the Cable Act, establishes the principal federal regulatory framework for our operation of cable systems and for the provision of our video services. The Cable Act allocates primary responsibility for enforcing the federal policies among the FCC and state and local governmental authorities.

#### *Content Regulations*

##### *Must Carry and Retransmission Consent*

The FCC's regulations require local commercial television broadcast stations to elect once every three years whether to require a cable system to carry the primary signal of their stations, subject to certain exceptions, commonly called must-carry, or to negotiate the terms by which the cable system may carry the station on its cable systems, commonly called retransmission consent. The most recent elections took effect through December 31, 2017. Through January 1, 2020, Congress bars broadcasters from entering into exclusive retransmission consent agreements. Congress also requires all parties to negotiate retransmission consent agreements in good faith.

The Satellite Television Extension and Localism Act Reauthorization Act ("STELAR") prohibits stations not under common ownership from engaging in joint negotiations with multichannel video programming distributors ("MVPDs") and restricting broadcasters from generally limiting carriage of stations that are significantly viewed or otherwise entitled to carriage, and eliminating the restriction on removing or repositioning stations during certain periods of time when network ratings are assessed, known as "sweeps." Pursuant to STELAR, in 2015 the FCC issued a Notice of Proposed Rulemaking ("NPRM") to review the "totality of the circumstances" test applied, in part, to determine whether parties have attempted to negotiate retransmission consent in good faith and whether certain other actions should evidence bad faith. We cannot predict whether the FCC will modify its rules or the impact of any such modifications. If the FCC fails to modify its rules, such action could be seen as an endorsement of current broadcaster negotiating tactics that often introduce challenges to the negotiation of retransmission consent agreements.

In 2014, the FCC issued an NPRM revisiting the definition of an MVPD, whether it should be technology-neutral to allow inclusion of certain Internet-delivered video services, the impact of such change on various industry players and consumers, and how to ensure any change promotes competition and broadband adoption. We cannot predict when, or if, the FCC will implement any new rules or change existing rules or the impact that any new rules or legislation may have on our business. Any new rules or legislation that would strengthen the relative negotiating position of broadcasters or the competitive position of Internet-delivered video service providers could have an adverse effect on our business.

We carry both must-carry broadcast stations and broadcast stations that have granted retransmission consent. A significant number of local broadcast stations carried by our cable systems have elected to negotiate for retransmission consent, and we have entered into retransmission consent agreements with substantially all of them. Retransmission consent agreements representing approximately 37% of our video customers receiving local broadcast stations will expire and require renegotiation prior to January 1, 2018.

## Table of Contents

### *Syndicated Exclusivity/Network Non-duplication/Sports Blackout*

Pursuant to FCC regulations, under certain circumstances, broadcasters can bar us from carrying certain network and syndicated programming. In 2014, the FCC issued a Further NPRM to expand the record on whether it should eliminate the ability of broadcasters to impose such restrictions on us.

### *Other Content Regulations*

On February 18, 2016, the FCC issued an order reapportioning the responsibilities regarding closed captioning quality, between video programming distributors ("VPDs") and video programming owners and producers. Initially, the burden had ultimately been borne by VPDs. Moreover, the FCC also adopted a burden-shifting model for investigation of complaints that can, in certain instances, shift the investigatory obligations to the owners or producers.

Pursuant to the Twenty-First Century Communications and Video Accessibility Act of 2010, the FCC has adopted rules that, among other things, impose certain accessibility requirements on navigation devices and digital apparatus that utilize encryption or other forms of conditional access to display video programming. Such devices must make on-screen text menus and guides for the display or selection of MVPD programming audibly accessible and make video programming accessible to individuals who are blind or visually impaired. These rules also require MVPDs to not rely solely on voice controls to activate closed captioning, establish customer notification requirements on manufacturers to publicize the availability of audible on-screen program guides, established information and documentation that must be made available to persons with disabilities and specified customer service training requirement topics for MVPDs.

### *Use of Our Cable Systems by the Government and Unrelated Third Parties*

The Cable Act allows local franchising authorities and unrelated third parties to obtain access to a portion of our cable systems' channel capacity for their own use through channels set aside for PEG programming and requires most cable operators to designate a significant portion of its activated channel capacity for commercial leased access by third parties to provide programming that may compete with services offered by the cable operator.

### *Cable Equipment*

The Cable Act and FCC regulations gave consumers the right to purchase set-top converters from third parties as long as the equipment does not harm the network, does not interfere with services purchased by other customers and is not used to receive unauthorized services. In 2016, the FCC adopted an NPRM and Memorandum Opinion and Order that removed the ban on the integration of security and non-security function in set-tops and proposed new rules aimed at increasing the availability of navigation devices or apps that have the functional equivalency of set-tops from providers unaffiliated with an MVPD. To accomplish this, the FCC proposed rules requiring MVPDs to split their signal into three core information streams: (i) *Service discovery*: information about what programming is available to the consumer, such as the channel listing and video-on-demand lineup, and what is on those channels; (ii) *Entitlements*: information about what a device is allowed to do with content, such as recording; and (iii) *Content delivery*: the video programming itself. The FCC declined to establish standards, instead recommending that they be established by an unnamed independent open standards body. It remains unclear whether these rules, if adopted, would interfere with contractual security requirements of programming networks, impair subscriber privacy, impair or duplicate an MVPD's ability to capture and use viewing information or otherwise adversely impact the subscriber experience. In late January 2017, a proposed order was removed from the FCC's list of items on circulation, meaning that it could no longer be voted upon. It is unclear whether the proposed order will be reinstated, the new FCC Chairman would propose an alternative order or no order would be issued at all. Should these or similar rules ultimately be enacted, we cannot predict what reengineering of our systems would be required, if any, or the cost of implementing and providing such split streams of information. We also cannot predict whether a subscriber's use of such alternative device or app would impair our accessibility to or the value of viewing information.

### *Multiple Dwelling Unit Building Wiring*

The FCC has adopted cable inside wiring rules to provide a more specific procedure for the disposition of residential home wiring and internal building wiring that belongs to an incumbent cable operator that is forced by the building owner to terminate its cable services in a building with multiple dwelling units. The FCC has issued rules voiding existing, and prohibiting future, exclusive service contracts for services to multiple dwelling unit or other residential developments, however, the FCC has affirmed the permissibility of bulk rate agreements and exclusive marketing agreements. Our inability to secure such express rights in the future may adversely affect our business to customers residing in multiple dwelling unit buildings and certain other residential developments.



## Table of Contents

### *Copyright*

Our cable systems typically include in their channel line-ups local and distant television and radio broadcast signals, which are protected by the copyright laws. We generally do not obtain a license to use this programming directly from the owners of the copyrights associated with this programming, but instead comply with an alternative federal compulsory copyright licensing process. In exchange for filing certain reports and contributing a percentage of our revenues to a federal copyright royalty pool, we obtain blanket permission to retransmit the copyrighted material carried on these broadcast signals. The nature and amount of future copyright payments for broadcast signal carriage cannot be predicted at this time.

DBS providers, to become more competitive with cable operators, operate under a similar statutory compulsory license that unlike that of cable operators, has a fixed term. In 2014, Congress extended the satellite compulsory license through 2019. As part of that legislation, Congress required the United States Government Accountability Office (“GAO”) to conduct another study regarding carriage and copyright issues relating to broadcast programming and the impact of the current regulatory regime on consumers. Pursuant to an earlier mandate, in 2011, GAO issued a report to Congress that found that the impact of a phase-out of the compulsory copyright licenses would have an uncertain impact on the market and regulatory environment. In part, the scheme (i.e., direct licensing, collective licensing or sublicensing) that would replace the compulsory licenses would impact the outcome. Additionally, in 2008 and 2011 the Copyright Office issued reports to Congress recommending phasing out the distant signal compulsory license. We cannot predict whether Congress will eliminate the cable compulsory license, or what scheme would replace it, if any; however, any loss of the current compulsory license could increase our costs.

### *State and Local Regulation*

#### *Franchise Matters*

Our cable systems use local streets and rights-of-way. Consequently, we must comply with state and local regulation, which is typically imposed through the franchising process. We have non-exclusive franchises granted by municipal, state or other local government entities for virtually every community in which we operate that authorize us to construct, operate and maintain our cable systems. Our franchises generally are granted for fixed terms and in many cases are terminable if we fail to comply with material provisions. The terms and conditions of our franchises vary materially from jurisdiction to jurisdiction. Each franchise granted by a municipal or local governmental entity generally contains provisions governing:

- franchise fees;
- franchise term;
- system construction and maintenance obligations;
- system channel capacity;
- design and technical performance;
- customer service standards;
- sale or transfer of the franchise; and
- territory of the franchise.

Although franchising matters have traditionally been regulated at the local level through a franchise agreement and/or a local ordinance, many states now allow or require cable service providers to bypass the local process and obtain franchise agreements or equivalent authorizations directly from state government. Many of the states in which we operate, including Illinois, Iowa, Missouri and Wisconsin make state-issued franchises available, which typically contain less restrictive provisions than those issued by municipal or other local government entities. State-issued franchises in many states generally allow local telephone companies or others to deliver services in competition with our cable service without obtaining equivalent local franchises. In states where available, we are generally able to obtain state-issued franchises upon expiration of our existing franchises. Our business may be adversely affected to the extent that our competitors are able to operate under franchises that are more favorable than our existing local franchises. While most franchising matters are dealt with at the state and/or local level, the Cable Act provides oversight and guidelines to govern our relationship with local franchising authorities whether they are at the state, county or municipal level.

## Table of Contents

### *HSD Service*

#### *Federal Regulation and Network Neutrality*

For a complete discussion of the federal regulatory status and network neutrality requirements, see *Recent Significant FCC Activity – HSD Regulatory Reclassification and Network Neutrality*.

#### *Digital Millennium Copyright Act*

We regularly receive notices of claimed infringements by our HSD service users. The owners of copyrights have been active in seeking to prevent use of the Internet to violate their rights. In many cases, their claims of infringement are based on the acts of customers of an Internet service provider — for example, a customer's use of an Internet service or the resources it provides to post, download or disseminate copyrighted music, movies, software or other content without the consent of the copyright owner or to seek to profit from the use of the goodwill associated with another person's trademark. In some cases, copyright and trademark owners have sought to recover damages from the Internet service provider, as well as or instead of the customer. The law relating to the potential liability of Internet service providers in these circumstances is unsettled. In 1996, Congress adopted the Digital Millennium Copyright Act, which is intended to grant ISPs protection against certain claims of copyright infringement resulting from the actions of customers, provided that the ISP complies with certain requirements.

#### *International Law*

Our HSD service enables individuals to access the Internet and to exchange information, generate content, conduct business and engage in various online activities on an international basis. The law relating to the liability of providers of these online services for activities of their users is currently unsettled both within the United States and abroad. Potentially, third parties could seek to hold us liable for the actions and omissions of our HSD customers, such as defamation, negligence, copyright or trademark infringement, fraud or other theories based on the nature and content of information that our customers use our service to post, download or distribute. We also could be subject to similar claims based on the content of other websites to which we provide links or third-party products, services or content that we may offer through our Internet service. Due to the global nature of the Web, it is possible that the governments of other states and foreign countries might attempt to regulate its transmissions or prosecute us for violations of their laws.

#### *State and Local Regulation and Competition*

Our HSD services provided over our cable systems have not generally subject to regulation by state or local jurisdictions. We cannot predict whether or not our HSD services will become subject to increased state regulation as a result of the Open Internet Order as more fully discussed in the *Recent Significant FCC Activity — HSD Regulatory Reclassification and Network Neutrality* section, above, or if they are, the impact that such regulation would have on our business.

### *Voice-over-Internet Protocol Phone Service*

#### *Federal Law*

The 1996 amendments to the Cable Act created a more favorable regulatory environment for cable operators to enter the phone business. Most major cable operators now offer voice-over-Internet protocol ("VoIP") phone service as a competitive alternative to traditional circuit-switched telephone service. Various states, including states where we operate, considered or attempted differing regulatory treatment, ranging from minimal or no regulation to heavily-regulated common carrier status. As part of the proceeding to determine any appropriate regulatory obligations for VoIP phone service, the FCC decided that alternative voice technologies, like certain types of VoIP phone service, should be regulated only at the federal level, rather than by individual states. Many implementation details remain unresolved, and there are substantial regulatory changes being considered that could either benefit or harm VoIP phone service as a business operation.

#### *Federal Regulatory Obligations*

The FCC has applied some traditional landline telephone provider regulations to VoIP services. In addition to certain USF obligations as discussed in *Recent Significant FCC Activity — HSD Regulatory Reclassification and Network Neutrality* section, above, the FCC also has extended other regulations and reporting requirements to VoIP providers, including E-911, CPNI, local number portability, disability access, Form 477 (subscriber information) reporting obligations, international service revenue reporting and outage

reporting. In 2010, the FCC issued an NOI and an NPRM that would transition high-cost program funds from analog phone service to the provision of broadband services.

**Table of Contents***State and Local Regulation*

Although our entities that provide VoIP phone service services are certificated as competitive local exchange carriers in most of the states in which they operate, they generally provide few, if any, services in that capacity. Rather, we provide VoIP services that are not generally subject to regulation by state or local jurisdictions. The FCC has preempted some state commission regulation of VoIP services, but has stated that its preemption does not extend to state consumer protection requirements. Some states continue to attempt to impose obligations on VoIP service providers, including state universal service fund payment obligations.

## Table of Contents

### ITEM1A. RISK FACTORS

#### Risks Related to our Operations

*We face intense competition that could adversely affect our business, financial condition and results of operations.*

We face significant competition for our products and services from a growing number of competitors that offer a wide range of communication, entertainment and information services. Many of our competitors have, compared to us, greater financial resources, more favorable brand recognition, fewer regulatory burdens and long-standing relationships with regulatory authorities and customers. Technological advances and changes in consumer behavior and demands have led to an increasing number of companies that offer new products and services that compete with ours, including “over-the-top” (“OTT”) video, and wireless Internet and phone services.

We face significant competition for video service from:

- DBS providers, principally DirecTV and DISH, that compete for video customers with satellite-delivered video packages throughout our footprint;
- Phone companies, principally AT&T and CenturyLink, that offer a wireline video service substantially similar to ours in markets representing approximately 9% of our homes passed;
- Other overbuilders offering a similar video service to ours in markets representing about 24% of our homes passed; and
- OTT video providers that are offering increasingly comprehensive video content, including high-quality exclusive content and linear video programming packages.

Our HSD service faces its most meaningful competition from:

- Phone companies, including CenturyLink, AT&T and Windstream, that primarily offer DSL Internet service that is typically limited to speeds considerably slower than ours. These phone companies have also upgraded limited portions of their networks to a FTTN or FTTH delivery system that allows for speeds comparable to our HSD service;
- Wireless providers, including AT&T, Verizon Wireless, T-Mobile and Sprint, that offer “3G” and “4G” wireless Internet service that may fully suffice for certain consumers with lower bandwidth requirements, and may offer greater levels of competition in the future with the deployment of “5G” technology and packages with unlimited bandwidth consumption; and
- Other providers of Internet access, including other overbuilders, municipalities and commercial entities that have built, or are considering building, fiber and/or Wi-Fi networks that may compete with our HSD service;

Other services we provide also face significant competition:

- Our phone service primarily competes with the phone companies noted above that offer substantially similar services to ours throughout our footprint, with the wireless providers that serve to deliver a form of “wireline substitution”, and with providers of IP-based phone services and other forms of communication including text and video messaging;
- We generally compete for business services customers with phone companies and, for our cell tower backhaul and enterprise level services, with other competitors, including metro and regional fiber-based carriers;
- We compete for advertising sales with a wide variety of media outlets, which will likely remain increasingly competitive as digital and other new formats of advertising seek to attract the same advertisers.

Although we have generally eliminated or reduced tactical discounts for customers that do not take bundled services, in order to attract new customers and maintain our existing customer base, we continue to make certain promotional offers that include short-term discounted service or equipment rates, which may result in lower revenues and greater marketing expenses. Customers who take these discounted bundled services may not remain customers following the end of the promotional period, which could adversely affect our business, financial condition and results of operations.

For additional information regarding our competitors, see “Business Description – Competition.”

*Continued increases in video programming expenses may drive the pricing of our video services to levels that customers deem unaffordable, which could have an adverse effect on our business, financial condition and results of operations.*

Video programming expenses have historically been, and we expect will continue to be, our largest single expense item and, in recent years, have reflected substantial per-unit percentage increases. The rate of increase in such expenses has been well in excess of the inflation rate and increase in U.S. wages, primarily caused by higher per unit rates for national and regional sports and other popular cable networks and rapidly rising retransmission consent fees imposed by local broadcast stations.

## Table of Contents

We believe these expenses will continue to grow at a significant rate because of the demands of large media conglomerates or other owners of most of the popular cable networks and major market local broadcast stations, and large independent television broadcast groups, who own, control or otherwise represent a significant number of local broadcast stations across the country and, in some cases, own or control multiple stations in the same market. Consolidation among these independent broadcast station groups has been significant over the past several years, and given recent proposed and completed transactions in the broadcast marketplace, the pace of consolidation has accelerated. As a result, the independent broadcast groups have become much larger based on the number of stations that they own in our markets. This will strengthen their position by allowing them to negotiate on behalf of a larger amount of local stations at one time.

Moreover, many of those powerful owners of programming require us to purchase their content in bundles and dictate how we offer them to our video customers, and impose economic penalties if we fail to comply. Consequently, we have little or no ability to individually or selectively negotiate for networks or local broadcast stations, to forego purchasing networks or local broadcast stations that generate low subscriber interest, to offer sports programming services, such as ESPN and regional sports networks, on one or more separate tiers, or to offer networks or stations on an a la carte basis to give our customers more choice and potentially lower their costs. In many instances, programmers have created additional networks and migrated popular programming, particularly sports programming, to these new networks that contributed to the increases in our programming costs. Additionally, we believe certain programmers may also demand higher fees from us in an effort to partially offset declines in their advertising revenue as more advertisers allocate a greater portion of their spending to Internet advertising. These practices, along with costs associated with offering the same programming on additional outlets including online and VOD platforms, increase our programming expense. Because of the leverage these large programming companies have over us, we also are obligated to carry additional programming that we would otherwise not offer, which increases our programming expense and lowers our capacity to introduce other new products and services.

If we are unable to successfully negotiate new agreements with these programmers before our current agreements expire, the programmers could require us to cease carrying their signals, possibly for an indefinite period, which may result in a loss of video customers and advertising revenue. On certain occasions in the past, negotiations have led to disputes with programmers that have resulted in temporary periods where we were not carrying a particular broadcast network or programming service or services, which increases the risk of customer dissatisfaction and the loss of customers. Because of the leverage these large programming companies have over us, we also may be obligated to carry additional programming that we would otherwise not offer, which may increase our programming expenses and lower our capacity to introduce other new products or services. We may also selectively choose not to renew our agreements with certain content providers if we believe it is uneconomical to do so, which could result in a loss of video customers and advertising revenues. In addition, if our HSD customers are unable to access desirable content online because content providers block or limit access by our customers if we do not carry their video programming, we may have difficulty retaining certain HSD customers.

While we attempt to offset such growth in programming expenses by customer rate increases, including the direct pass-through of increases in retransmission consent and regional sports network fees, our video gross margins will likely continue to decline given the outsized increases to our programming costs we expect in the future. If increases in our programming costs were to drive the pricing of our video services to levels that are deemed unaffordable, our customers may no longer purchase our video services and instead rely on over-the-air viewing or use an OTT video service, which could have an adverse effect on our business, financial condition and results of operations.

### *Weak economic conditions may adversely impact our business, financial condition and results of operations.*

Most of our revenues are sourced from consumers whose spending behavior is impacted by prevailing economic conditions. Weak job and business creation, occupied housing levels, personal income growth and consumer confidence can adversely impact demand for our services, and may cause increased cancellations by our customers or lead to unfavorable changes in the mix of products taken. The expanded availability of free or lower cost services that may compete with ours, including OTT video and wireless Internet available in certain commercial or public locations, may further pressure our customer retention. Weak economic conditions also may decrease advertising demand and negatively impact our advertising revenues.

Because our video service is an established and highly penetrated business, our ability to gain new video customers depends, in part, on growth in occupied housing in our service areas, which is influenced by both local and national economic conditions. If the number of occupied homes in our service areas were to decline or not grow at all, our ability to attract and retain new video customers may be negatively impacted, and could adversely impact our business, financial condition and results of operations.

## Table of Contents

*An acceleration in bandwidth consumption by HSD customers greater than current expectations could require unplanned network investments and meaningfully increase our capital expenditures.*

The level of bandwidth consumption by our HSD customers has grown at sizeable rates for the past several years as usage of many Internet-based services, particularly OTT video, has rapidly increased. If bandwidth consumption were to accelerate greater than current expectations, we may need to make unplanned network investments and meaningfully increase our capital expenditures to expand the bandwidth capacity of our systems and ensure the quality of service provided to our HSD customers. Our ability to develop, implement and refine business models that respond to changing consumer bandwidth usage and demands efficiently could be restricted by regulatory and legislative efforts to impose so-called “net neutrality” requirements on Internet providers. See “Business — Legislation and Regulation — General — Recent Significant FCC Activity.”

*We face risks as we attempt to continue to grow our business services customer base and associated revenues.*

Business services customers, and associated revenues, have made increasing contributions to our results of operations in the last several years, and we may encounter challenges as we attempt to further expand the delivery of HSD and phone to small- and medium-sized businesses, and data networking and fiber connectivity to medium- and large-sized businesses and wireless carriers’ cellular towers. We expect to continue to commit significant investments on technology, equipment and personnel focused on our business services, including the 2016 introduction of “Project Open Road” where we plan to extend our network to numerous locations that contain multiple potential business customers. If we are unable to sufficiently build the necessary infrastructure and internal support functions to scale and expand our customer base, the potential growth of business services would be limited. In many cases, business service customers have service level agreements that require us to provide higher standards of service and reliability. If we are unable to meet these service level requirements, or more broadly, the expectations of SMB and enterprise customers, or we fail to properly scale and support these activities, our results of operations may be adversely affected.

*We may not realize the expected benefits of the major initiatives under MCC’s Capital Plan*

We believe the major initiatives under MCC’s Capital Plan will improve our competitive position and provide additional opportunities to grow our customer base and associated revenues than we would have experienced otherwise. If we were to face greater levels of competition that impaired our ability to gain incremental market share or anticipated revenues, or higher than expected capital expenditures as we deploy such initiatives, we may not fully realize the expected benefits under MCC’s Capital Plan.

*If we are unable to keep pace with rapid technological developments and respond effectively to changes in consumer behavior and demand, our business, financial condition and results of operations may be adversely affected.*

We operate in a rapidly changing environment and our success depends, in part, on our ability to maintain or improve our competitive position by acquiring, developing, adopting and exploiting new and existing technologies to add introduce new products and services, or enhance existing ones. Continued development of newer technologies and services and rapidly evolving consumer preferences will likely continue to drive expansion of the products and services offered by our existing competitors and increase the number of competitors that we face. Next-generation technology has allowed for linear OTT video services that may suffice as a full replacement for our video service, and may allow wireless Internet providers to offer a service based on “5G” technology that may adequately serve as a full replacement for our HSD service. If our competitors were to introduce new or products and services that we do not currently offer, or enhanced versions of existing products and services that consumers find more compelling than ours, we may be required to deploy greater levels of marketing expenditures and capital investments to maintain our competitive position. We may also recognize lower revenues if such new products and services require us to offer certain of our existing services at a lower or no cost to our customers. Such changes could cause our business, financial condition and results of operation may be adversely affected.

To keep pace with future developments, we must choose third-party suppliers whose technologies or equipment are more effective, cost-efficient and attractive to customers than those offered by our competitors. We rely on third-party providers to make available to us new, cost-effective set-tops and programming guides that allow us to offer our video customers an enhanced user experience. If our vendors were unable to provide set-tops and programming guides that our customers prefer in a timely manner, compared to those offered by our competitors, we may experience greater video customer losses, and our business, financial condition and results of operation may be adversely affected.

*We depend on network and information systems and other technologies to operate our businesses. A disruption or failure in such networks, systems or technologies resulting from “cyber-attacks,” natural disasters or other events outside our control have a material adverse effect on our business, financial condition and results of operations.*

Because of the importance of network and information systems and other technologies to our business, disruptions or failures caused by “cyber-attacks” such as computer hacking, computer viruses, denial of service attacks, worms or other disruptive software could have a devastating impact on our business. Both unsuccessful and successful “cyber-attacks” on companies have continued to increase in frequency, scope and potential harm in recent years. Because the techniques used in such attacks have become more sophisticated and change frequently, we may be unable to anticipate these techniques or implement adequate preventative measures. Such “cyber-attacks” may result in misappropriation, misuse, leakage, falsification and accidental release or loss of information maintained in our information technology system and networks, including customer, personnel and vendor data. We could also be subject to employee error or malfeasance, or other disruptions.

## Table of Contents

As a result of the increasing awareness concerning the importance of safeguarding personal information and the potential misuse of such information, businesses such as ours that handle a large amount of personal customer data are subject to legislation that has been adopted or is being considered regarding the protection, privacy and security of personal information and information-related risks. We may also provide certain customer and employee information to third parties in connection with our business. While we obtain assurance such data will be protected by these third-parties, they are potentially vulnerable to the same threats noted above. If such risks were to materialize, we may be subject to significant costs and expenses, or damage to our reputation and credibility, which could adversely affect our business, financial condition, and results of operations.

Our network and information systems are also vulnerable to damage resulting from power outages, natural disasters, terrorist attacks and other material events that are outside our control. Any such event may degrade or disrupt our service, lead to excessive volume at our call centers, and damage our plant, equipment, data and reputation. While we generally implement redundant systems to allow our network to continue to function in an outage, these measures may be ineffective in certain events. We are unable to predict the impact of such events, and any resulting customer or revenue losses, or increases in costs and expenses or capital expenditures, could have a material adverse effect on our business, financial condition, and results of operations.

We are unable to predict the impact of such events, and any resulting customer or revenue losses, or increases in costs and expenses or capital expenditures, could have a material adverse effect on our business, financial condition, and results of operations.

*We may be unable to secure necessary hardware, software, telecommunications components and their operational support, and the related product development, which may impair our ability to provision and service our customers and to compete effectively.*

Third-party firms supply most of the components used in delivering our products and services, including set-tops and VOD equipment; interactive programming guides; cable modems; routers and other switching equipment; provisioning and other software; network connections for our phone services; fiber-optic cable and construction services for expansion and upgrades of our network; and our customer billing platform. Some of these companies may have negotiating leverage over us because they are the sole supplier of certain products and services, or because there may be a long lead time and/or significant expense required to transition to another provider. We also rely on these third-party firms to develop next-generation technology so that we may stay competitive with the latest products and services, and such reliance may result in less product innovation or higher costs than we would experience with multiple suppliers. In many cases, these hardware, software and operational support vendors and service providers have, either through contract or as a result of intellectual property rights, a position of some exclusivity, and our operations depend on a successful relationship with these companies.

Any delays or disruptions in the relationship as a result of contractual disagreements, operational or financial failures on the part of the suppliers, or other adverse events affecting these suppliers could negatively affect our ability to effectively provision and service our customers. We may face significant lapses in service and costs to upgrade our networks to allow them to operate with alternate equipment if such events were to occur, which would negatively affect our business, financial condition and results of operations.

*Our business depends on certain intellectual property rights and on not infringing on the intellectual property rights of others.*

We rely on our copyrights, trademarks and trade secrets, as well as licenses and other agreements with our vendors and other parties, to use our technologies, conduct our operations and sell our products and services. Third-party firms have in the past, and may in the future, assert claims or initiate litigation related to patent, copyright, trademark, and other intellectual property rights to technologies and related standards that are relevant to us. These assertions have increased over time as a result of our growth and the general increase in the pace of patent claims assertions, particularly in the United States. Recently, the number of intellectual property infringement claims has been increasing in the communications and entertainment fields, and from time to time, we have been party to litigation alleging that certain of our services or technologies infringe upon the intellectual property rights of others. Because of the large number of patents in the networking field, the secrecy of some pending patents and the rapid rate of issuance of new patents, it is not economically practical or, in some cases, possible to determine in advance whether a product or any of its components infringes or will infringe on the patent rights of others. Asserted claims and/or initiated litigation can include claims against us or our manufacturers, suppliers, or customers, alleging infringement of their proprietary rights with respect to our existing or future products and/or services or components of those products and/or services. Regardless of the merit of these claims, they can be time-consuming to defend; result in costly litigation and diversion of technical and management personnel; and require us to develop a non-infringing technology or enter into license agreements. There can be no assurance that licenses will be available on acceptable terms and conditions, if at all, or that any indemnification by our suppliers will be adequate to cover our costs if a claim were brought directly against us or our customers. Furthermore, because of the potential for high monetary awards that are not predictable, it is not unusual to find even arguably unmeritorious claims settled for significant amounts.



## Table of Contents

If any infringement or other intellectual property claim made against us by any third-party is successful, if we are required to indemnify a customer with respect to a claim against the customer, or if we fail to develop non-infringing technology or license the proprietary rights on commercially reasonable terms and conditions, our business, results of operations, and financial condition could be adversely affected.

### *The loss of key personnel could have a material adverse effect on our business.*

Our success is substantially dependent upon the retention of, and the continued performance by, MCC's key personnel, including Rocco B. Comisso, MCC's Chairman and Chief Executive Officer. If any of MCC's key personnel cease to participate in our business and operations, it could have an adverse effect on our business, financial condition and results of operations.

## **Risks Related to our Financial Condition**

### *We have a significant amount of debt, and the associated interest and principal payments could limit our operational flexibility and have an adverse effect on our business, financial condition, liquidity, and results of operations.*

As of December 31, 2016, our total debt was \$1.628 billion. Given our substantial debt, we are highly leveraged and will continue to be so. Our debt obligations require us to use a large portion of our cash flows from operations to pay interest and principal payments on such debt, resulting in less cash available to finance our operations, capital expenditures and other activities.

Our significant amount of debt and associated debt service requirements could have adverse consequences, such as:

- limiting our ability to obtain future financing to refinance our existing indebtedness on terms acceptable to us or at all;
- exposing us to greater interest expense as a result of having to refinance existing debt on less favorable terms than we currently experience, or due to higher market interest rates on 32% of our debt that is exposed to variable rates;
- limiting our ability to react to changes in our business, which may place us at a competitive disadvantage compared to competitors with less debt and stronger liquidity positions;
- restricting us from making necessary capital expenditures or from pursuing strategic acquisitions, or causing us to make divestitures of strategic or non-strategic assets; and
- increasing our vulnerability to adverse economic, industry and competitive conditions.

If we are unable to obtain financing on acceptable terms, or at all, to refinance our debt as it comes due, we would need to take other actions, including selling assets or seeking strategic investments from third parties, potentially on unfavorable terms, and deferring capital expenditures or other discretionary uses of cash. Such potential asset sales or third-party investments could adversely affect our results of operations, liquidity and financial condition, and any significant reduction in capital expenditures could affect our ability to compete effectively. If such measures were to become necessary, there can be no assurance that we would be able to sell assets or raise strategic investment capital sufficient enough to meet our scheduled debt maturities as they come due.

### *The financial markets are subject to volatility and disruptions, which may adversely affect our access to, or the cost of, new capital or our ability to refinance our scheduled debt maturities and other obligations as they come due.*

Volatility and disruptions in the capital and credit markets as a result of uncertainty, changing or increased regulation of financial institutions, reduced alternatives or failures of significant financial institutions could adversely affect our access to the liquidity needed for our businesses. Such disruptions could require us to take measures to conserve cash until the markets stabilize or until alternative credit arrangements or other funding for our business needs can be arranged.

Our access to funds under our revolving credit commitments is dependent on the ability of the financial institutions that are parties to those facilities to meet their funding commitments. Those financial institutions may not be able to meet their funding commitments if they experience shortages of capital and liquidity or if they experience excessive volumes of borrowing requests within a short period of time. Moreover, the obligations of the financial institutions under our revolving credit commitments are several and not joint and, as a result, a funding default by one or more institutions does not need to be made up by the others.

### *We are a holding company, and if our operating subsidiaries are unable to make funds available to us, we may not be able to fund our indebtedness and other obligations.*

We are a holding company, and do not have any operations or hold any assets other than our investments in, and our advances to, our operating subsidiaries. Our operating subsidiaries conduct all of our consolidated operations and own substantially all of our consolidated assets. Our operating subsidiaries are separate and distinct legal entities and have no obligation, contingent or otherwise, to make funds available to us.

## Table of Contents

The only source of cash that we have to fund our senior notes (including, without limitation, the payment of interest on, and the repayment of, principal) is the cash that our operating subsidiaries generate from operations or borrow under their bank credit facility (the "credit facility"). The ability of our operating subsidiaries to make funds available to us will depend upon their results and applicable laws and contractual restrictions, including the covenants set forth in the credit agreement governing the credit facility (the "credit agreement"). If our operating subsidiaries were unable to make funds available to us, then we may not be able to make payments of principal or interest due under our senior notes. If such an event occurred, we may be required to adopt one or more alternatives, such as refinancing our senior notes or the outstanding debt of our operating subsidiaries at or before maturity, or raising additional capital through debt or equity issuance, or both. If we were not able to successfully accomplish those tasks, then we may have to take other actions, including selling assets or seeking strategic investments from third parties, potentially on unfavorable terms, and deferring capital expenditures or other discretionary uses of cash.

There can be no assurance that any of the foregoing actions would be successful. Any inability to meet our debt service obligations or refinance our indebtedness would materially adversely affect our business, financial condition and results of operations.

*A default under our credit agreement or indentures could result in an acceleration of our indebtedness and other material adverse effects.*

As of December 31, 2016, the principal financial covenants of the credit agreement required our operating subsidiaries to maintain a total leverage ratio (as defined in the credit agreement) of no more than 5.0 to 1.0 and an interest coverage ratio (as defined in the credit agreement) of no less than 2.0 to 1.0. The credit agreement also contains various other covenants that, among other things, impose certain limitations on mergers and acquisitions, consolidations and sales of certain assets, liens, restricted payments and certain transactions with affiliates. See Note 6 in our Notes to Consolidated Financial Statements.

As of December 31, 2016, the principal financial covenant of the indentures governing our senior notes (the "indentures") was a limitation on the incurrence of additional indebtedness based upon a maximum debt to operating cash flow ratio (as defined in the indenture) of 8.5 to 1.0. The indentures also contain various other covenants, though they are generally less restrictive than those found in our credit facility. See Note 6 in our Notes to Consolidated Financial Statements.

The breach of any of the covenants under the credit agreement or indentures could cause a default, which may result in the associated indebtedness becoming immediately due and payable. If this were to occur, we would be unable to adequately finance our operations. The membership interests of our operating subsidiaries are pledged as collateral under our credit facility. A default under our credit agreement could result in a foreclosure by the lenders on the membership interests pledged under that facility. Because we are dependent upon our operating subsidiaries for all of our cash flows, a foreclosure would have a material adverse effect on our business, financial condition, liquidity, and results of operations.

In the event of a liquidation or reorganization of any of our subsidiaries, the creditors of any of such subsidiaries, including trade creditors, would be entitled to a claim on the assets of such subsidiaries prior to any claims of the stockholders of any such subsidiaries, and those creditors are likely to be paid in full before any distribution is made to such stockholders. To the extent that we, or any of our direct or indirect subsidiaries, are a creditor of another of our subsidiaries, the claims of such creditor could be subordinated to any security interest in the assets of such subsidiary and/or any indebtedness of such subsidiary senior to that held by such creditor.

*A lowering or cessation of the ratings assigned to our debt securities by ratings agencies may increase our future borrowing costs and reduce our access to capital.*

Our future access to the debt markets and the terms and conditions we receive are influenced by our debt ratings. MCC's corporate credit ratings are Ba3 with a positive outlook by Moody's, and BB with a stable outlook by Standard and Poor's ("S&P"). Our senior unsecured ratings are B2 with a positive outlook by Moody's, and B+ with a stable outlook by S&P. There can be no assurance that Moody's or S&P will maintain their ratings on MCC and us. A negative change to these credit ratings could result in higher interest rates on future debt issuance than we currently experience, or adversely impact our ability to raise additional funds.

## Table of Contents

### ***Impairment of our goodwill and other intangible assets could cause significant losses.***

As of December 31, 2016, we had approximately \$1.4 billion of unamortized intangible assets, including franchise rights of \$1.2 billion and goodwill of \$0.2 billion on our consolidated balance sheets. These intangible assets represented approximately 60% of our total assets.

Accounting Standards Codification (“ASC”) No. 350 — *Intangibles — Goodwill and Other* (“ASC 350”) requires that goodwill and other intangible assets deemed to have indefinite useful lives, such as cable franchise rights, cease to be amortized. ASC 350 also requires that goodwill and certain intangible assets be tested at least annually for impairment. If we find that the carrying value of goodwill or cable franchise rights exceeds its fair value, we will reduce the carrying value of the goodwill or intangible asset to the fair value, and will recognize an impairment loss in our results of operations. See “Management’s Discussion and Analysis — Critical Accounting Policies — *Valuation and Impairment Testing of Indefinite-lived Intangibles*” and Note 2 in our Notes to Consolidated Financial Statements.

### **Risks Related to Legislative and Regulatory Matters**

#### ***Changes in government regulation could adversely impact our business.***

The cable industry is subject to extensive legislation and regulation at the federal and local levels and, in some instances, at the state level. Additionally, our HSD and phone services are also subject to regulation, and additional regulation is under consideration. Aspects of such regulation are currently the subject of judicial and administrative proceedings, legislative and administrative proposals, and lobbying efforts by us and our competitors. Legislation is reportedly under consideration that could entirely rewrite our principal regulatory statute, and the FCC and/or Congress may attempt to change the classification of or change the way that our video and/or HSD services are regulated and/or change the framework under which broadcast signals are carried, remove the copyright compulsory license and change the rights and obligations of our competitors. We expect that court actions and regulatory proceedings will continue to refine our rights and obligations under applicable federal, state and local laws. The results of current or future judicial and administrative proceedings and legislative activities cannot be predicted. Modifications to existing requirements or imposition of new requirements or limitations could have an adverse impact on our business including those described below. See “Business — Legislation and Regulation.”

#### ***Recent FCC action and possible court proceedings and legislation could adversely affect our HSD service.***

Reclassification of the regulatory status of HSD service to a telecommunications service under Title II of the Communications Act may significantly impact how we provide and charge for our HSD service and operate our network by imposing significant regulations on us and introducing regulatory uncertainty due to lack of clarity of new regulations. The FCC could choose to impose this regulation in a way that adversely affects our business by imposing new regulatory burdens and limiting our business and customer relationships. The regulatory scheme introduced in the FCC’s Open Internet Order relies heavily on forbearance of many types of Title II regulations, however, the FCC could at any time in the future choose to forgo forbearance and impose significant new regulations of our HSD service. As only one example, the FCC has decided to forebear from applying its extensive authority to regulate prices under Title II, and if it decided to end that forbearance, our results of operations could suffer. Even if the FCC continues to forebear from applying certain provisions of Title II, our business, financial condition and results of operations could be adversely impacted by the provisions that it does intend to apply. In addition, the uncertainty created by the fact that the impact of the new rules cannot yet be determined and the fact that the FCC could end forbearance in the future may impede our ability to obtain financing for our business or increase the cost of that financing. See “Business — Legislation and Regulation — *General — Recent Significant FCC Activity — HSD Regulatory Reclassification and Network Neutrality*,” “Business — Legislation and Regulation — *General — Privacy and Data Security*,” “Business — Legislation and Regulation — *General — Pole Attachment Regulation*,” “Business — Legislation and Regulation — *General — Universal Service Fund*” and “Business — Legislation and Regulation — *HSD Service — State and Local Regulation and Competition*.”

#### ***Government financing of broadband providers in our service areas could adversely impact our business.***

Possible changes to how USF monies are distributed may provide funding and subsidies to those who either compete with us or seek to compete with us and therefore put us at a competitive disadvantage. Moreover, if the FCC chooses to impose USF fees on broadband services, bundled services or VoIP services that could increase the cost of our services and harm our ability to compete. See “Business — Legislation and Regulation — *General — Universal Service Fund*” and “Business — Legislation and Regulation — *Voice-over-Internet-Protocol Phone Service — Federal Regulatory Obligations*.”

## Table of Contents

### ***Changes in the definition of an MVPD may make programming available to Internet providers of video services.***

If the FCC changes the definition of an MVPD to include those distributors of multiple channels of video programming over the Internet that do not own physical distribution facilities, competitors and potential competitors may have access to certain traditional cable programming under the FCC's program access rules. If Internet-based providers have greater access to programming of value to our customers and can offer service at a lower price because they are not facilities-based, that could hurt our business, financial condition and results of operations. See "Business – Legislation and Regulation – *Cable System Operations and Video Services – Access to Certain Programming.*"

### ***Opening our services to third-party navigation devices or apps, requiring downloadable security and limiting how much we charge for leased navigation devices may adversely impact our provision of services, raise our costs and decrease our revenues.***

If the FCC changes its regulations to require that we reengineer our systems to permit subscribers to use third-party devices and/or apps in place of our leased set-tops, that could impair the subscriber experience potentially causing a loss of subscribers, raise our costs, decrease our revenues from leased set-tops, cause early retirement of set-tops, increase liability arising from security vulnerabilities created by either the mandatory structure to allow third-party navigation devices or by the devices or apps themselves and could devalue viewing information by either limiting our access to it or by allowing third-parties to capture and use such data for their own gain. If rules are adopted requiring the usage of downloadable security configurations from a third-party trust authority, the risk of security breaches to our system may increase and the protection of the content that we provide as part of our cable service may be compromised, which in turn could increase our exposure to legal actions by affected third parties, such as the content owners. Any rules that would limit how much we charge for leased navigation devices could adversely impact our revenue stream or our ability to price such devices competitively. See "Business — Legislation and Regulation — *Cable System Operations and Video Services — Cable Equipment.*"

### ***Denials of franchise renewals or continued absence of franchise parity can adversely impact our business.***

Where state-issued franchises are not available, local franchising authorities may demand concessions, or other commitments, as a condition to renewal, and these concessions or other commitments could be costly. Although the Cable Act affords certain protections, there is no assurance that we will not be compelled to meet such demands in order to obtain renewals.

Our cable systems are operated under non-exclusive franchises. We believe that, as of December 31, 2016, various entities are currently offering video service, through wireline distribution networks, to about 33% of our estimated homes passed. Because of the FCC's actions to speed issuance of local competitive franchises and because many states in which we operate cable systems have adopted, and other states may adopt, legislation to allow others, including local telephone companies, to deliver services in competition with our cable service without obtaining equivalent local franchises, we may face not only increasing competition but we may be at a competitive disadvantage due to lack of regulatory parity. Any of these factors could adversely affect our business. See "Business — Legislation and Regulation — *Cable System Operations and Video Services — State and Local Regulation — Franchise Matters.*"

### ***Our phone service may become subject to additional regulation.***

The regulatory treatment of phone services that we and other providers offer remains uncertain. The FCC, Congress, the courts and the states continue to look at issues surrounding the provision of VoIP, including whether this service is properly classified as either a telecommunications service or an information service. Any changes to existing law as it applies to VoIP or any determination that results in greater or different regulatory obligations than competing services would result in increased costs, lower revenues or an impeded ability to effectively compete or otherwise adversely affect our ability to successfully conduct our phone business. See "Business — Legislation and Regulation — *Voice-over-Internet-Protocol Phone Service — Federal Law.*"

### ***Changes in pole attachment regulations or actions by pole owners could significantly increase our pole attachment costs.***

Our cable facilities are often attached to, or use, public utility poles, ducts or conduits. Although changes in 2011 to the FCC's long-standing pole attachment rate formulas and attachment requirements may be beneficial to us, the effective and significant lowering of the rate attachment costs to our telecommunications competitors through the FCC's 2015 Open Internet Order coupled with increasing their ease of attachment may significantly benefit those that provide services that compete with ours. Our business, financial condition and results of operations could suffer a material adverse impact from changes that make it both easier and less costly for those who compete with us to attach to poles. See "Business — Legislation and Regulation — *General — Pole Attachment Regulation.*"

## Table of Contents

### *Changes in compulsory copyright regulations could significantly increase our license fees.*

If Congress either eliminates the current cable compulsory license or enacts the proposed revisions to the Copyright Act, the elimination could impose increased costs and transactional burdens or the revisions could impose oversight and conditions that could adversely affect our business. Additionally, the Copyright Office's implementation of any such legislative changes could impose requirements on us or permit overly intrusive access to financial and operational records. Any future decision by Congress to eliminate the cable compulsory license, which would require us to obtain copyright licensing of all broadcast material at the source, would impose significant administrative burdens and additional costs that could adversely affect our business. See "Business — Legislation and Regulation — *Cable System Operations and Video Services — Federal Regulation — Copyright.*"

### **Risks Related to MCC's Chairman and Chief Executive Officer's Controlling Position**

*MCC's Chairman and Chief Executive Officer has the ability to control all major corporate decisions, and a sale of his ownership interest could result in a change of control that would have unpredictable effects.*

An entity wholly-owned by Rocco B. Commisso and related parties is the sole shareholder of MCC. Mr. Commisso is MCC's founder, Chairman and Chief Executive Officer. Our debt arrangements provide that a default may result upon certain change of control events, including if Mr. Commisso were to sell a significant stake in us or MCC to a third party. Our debt agreements provide, however, that a change of control will not be deemed to have occurred so long as MCC continues to be our manager and/or Mr. Commisso continues to be MCC's, or our, Chairman or Chief Executive Officer.

A change in control could result in a default under our debt arrangements, which require us to offer to repurchase our senior notes at 101% of their principal amount, trigger a variety of federal, state and local regulatory consent requirements and potentially limit MCC's further utilization of net operating losses for income tax purposes. Any of the foregoing results could adversely affect our results of operations and financial condition.

### **ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

### **ITEM 2. PROPERTIES**

Our principal physical assets consist of fiber-optic networks, including signal receiving, encoding and decoding devices, headend facilities and distribution systems and equipment at, or near, customers' homes. The signal receiving apparatus typically includes a tower, antenna, ancillary electronic equipment and earth stations for reception of satellite signals. Headend facilities are located near the receiving devices. Our distribution system consists primarily of coaxial and fiber-optic cables and related electronic equipment. Customer premise equipment consists of set-top devices, cable modems and related equipment. Our distribution systems and related equipment generally are attached to utility poles under pole rental agreements with local public utilities, although in some areas the distribution cable is buried in underground ducts or trenches. The physical components of the cable systems require maintenance and periodic upgrading to improve performance and capacity. In addition, we maintain a network operations center with equipment necessary to monitor and manage the status of our network.

We own and lease the real property housing our regional call centers, business offices and warehouses throughout our operating regions. Our headend facilities, signal reception sites and microwave facilities are located on owned and leased parcels of land, and we generally own the towers on which certain of our equipment is located. We own most of our service vehicles. We believe that our properties, both owned and leased, are in good condition and are suitable and adequate for our operations.

### **ITEM 3. LEGAL PROCEEDINGS**

We are involved in various legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our consolidated financial position, results of operations, cash flows or business.

**Table of Contents**

**ITEM 4. *MINE SAFETY DISCLOSURES***

Not applicable.

**PART II**

**ITEM 5. *MARKET FOR REGISTRANTS' COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES***

There is no public trading market for our equity, all of which is held by MCC.

Table of Contents**ITEM 6. SELECTED FINANCIAL DATA**

In the table below, we provide selected historical consolidated statement of operations data, cash flow data and other data for the years ended December 31, 2012 through 2016 and balance sheet data and operating data as of December 31, 2012 through 2016, which are derived from our consolidated financial statements (except other data and operating data). Dollars are in thousands, except operating data. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

	Year Ended December 31,				
	2016	2015	2014	2013	2012
<b>Statements of Operations Data:</b>					
Revenues	\$ 1,033,239	\$ 982,362	\$ 948,447	\$ 918,614	\$ 897,420
Costs and expenses:					
Service costs	419,406	401,751	381,014	365,436	356,915
Selling, general and administrative expenses	193,669	182,144	180,084	185,188	180,736
Management fee expense	20,800	19,000	17,650	16,600	14,335
Depreciation and amortization	147,114	144,220	153,478	156,397	151,240
Operating income	252,250	235,247	216,221	194,993	194,194
Interest expense, net	(78,725)	(94,668)	(100,436)	(96,203)	(112,561)
Gain on derivatives, net	1,203	9,173	23,226	22,782	6,217
Loss on early extinguishment of debt	(1,156)	(4,382)	(300)	(832)	(11,114)
Other expense, net	(1,686)	(1,377)	(1,262)	(1,793)	(1,483)
Net income	<u>\$ 171,886</u>	<u>\$ 143,993</u>	<u>\$ 137,449</u>	<u>\$ 118,947</u>	<u>\$ 75,253</u>
<b>Balance Sheets Data (end of period):</b>					
Total assets	\$2,292,154	\$2,257,033	\$2,259,413	\$2,273,845	\$2,284,584
Total debt	\$1,613,650	\$1,809,518	\$1,957,000	\$1,908,000	\$1,959,000
Total member's equity (deficit)	\$ 317,492	\$ 95,461	\$ (30,683)	\$ 12,955	\$ (59,323)
<b>Cash Flows Data:</b>					
Net cash flows provided by (used in):					
Operating activities	\$ 336,034	\$ 297,236	\$ 280,292	\$ 248,092	\$ 231,038
Investing activities	\$ (183,289)	\$ (148,289)	\$ (137,571)	\$ (146,018)	\$ (155,784)
Financing activities	\$ (148,979)	\$ (147,957)	\$ (144,506)	\$ (102,633)	\$ (75,188)
<b>Other Data:</b>					
OIBDA (1)	\$ 399,364	\$ 379,467	\$ 369,699	\$ 351,390	\$ 345,434
OIBDA margin (2)	38.7%	38.6%	39.0%	38.3%	38.5%
Ratio of earnings to fixed charges and preferred dividends					
	2.44	2.02	1.93	1.82	1.41
<b>Operating Data (end of period):</b>					
Estimated homes passed (3)	1,504,000	1,496,000	1,499,000	1,495,000	1,493,000
Video customers (4)	463,000	480,000	500,000	528,000	558,000
HSD customers (5)	643,000	605,000	564,000	534,000	505,000
Phone customers (6)	264,000	239,000	218,000	207,000	190,000
Primary service units (7)	1,370,000	1,324,000	1,282,000	1,269,000	1,253,000
Customer relationships (8)	754,000	732,000	710,000	710,000	708,000

**Table of Contents**

- (1) "OIBDA" is not a financial measure calculated in accordance with generally accepted accounting principles ("GAAP") in the United States. We define OIBDA as operating income before depreciation and amortization. OIBDA has inherent limitations as discussed below.

OIBDA is one of the primary measures used by management to evaluate our performance and to forecast future results. We believe OIBDA is useful for investors because it enables them to assess our performance in a manner similar to the methods used by management, and provides a measure that can be used to analyze value and compare the companies in the cable industry. A limitation of OIBDA, however, is that it excludes depreciation and amortization, which represents the periodic costs of certain capitalized tangible and intangible assets used in generating revenues in our business. Management uses a separate process to budget, measure and evaluate capital expenditures. In addition, OIBDA may not be comparable to similarly titled measures used by other companies, which may have different depreciation and amortization policies.

OIBDA should not be regarded as an alternative to operating income or net income as an indicator of operating performance, or to the statement of cash flows as a measure of liquidity, nor should it be considered in isolation or as a substitute for financial measures prepared in accordance with GAAP. We believe that operating income is the most directly comparable GAAP financial measure to OIBDA.

The following represents a reconciliation of OIBDA to operating income, which is the most directly comparable GAAP measure (dollars in thousands):

	Year Ended December 31,				
	2016	2015	2014	2013	2012
OIBDA	\$ 399,364	\$ 379,467	\$ 369,699	\$ 351,390	\$ 345,434
Depreciation and amortization	<u>(147,114)</u>	<u>(144,220)</u>	<u>(153,478)</u>	<u>(156,397)</u>	<u>(151,240)</u>
Operating income	<u>\$ 252,250</u>	<u>\$ 235,247</u>	<u>\$ 216,221</u>	<u>\$ 194,993</u>	<u>\$ 194,194</u>

- (2) Represents OIBDA as a percentage of revenues. See Note 1 above.
- (3) Represents the number of single residence homes, apartments and condominium units that we can connect to our distribution system without further extending the transmission lines, based on best available information.
- (4) Represents customers receiving video service. Business services video customers that are billed on a bulk basis are converted into equivalent video customers by dividing their associated revenues by the applicable full-price residential video rate, which is generally consistent with the methodology used in determining payments made to programmers. Video customers include connections to schools, libraries, local government offices and employee households that may not be charged for basic or expanded video service, but may be charged for higher tier video, HSD, phone or other services. Our methodology of calculating the number of video customers may not be identical to those used by other companies offering similar services.
- (5) Represents customers receiving HSD service. Small- to medium-sized business HSD customers are converted to equivalent HSD customers by dividing their associated revenues by the applicable full-price residential HSD rate. Medium- to large-sized business customers who take our enterprise network services are not counted as HSD customers. Our methodology of calculating HSD customers may not be identical to those used by other companies offering similar services.
- (6) Represents customers receiving phone service. Small- to medium-sized business phone customers are converted to equivalent phone customers by dividing their associated revenues by the applicable full-price residential phone rate. Customers who take our IP-enabled voice trunk service are not counted as phone customers. Our methodology of calculating phone customers may not be identical to those used by other companies offering similar services.
- (7) Represents the sum of video, HSD and phone customers.
- (8) Represents the total number of residential and business customers that receive at least one service, without regard to which service(s) customers purchase.

Table of Contents**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Reference is made to the "Risk Factors" in Item 1A for a discussion of important factors that could cause actual results to differ from expectations and any of our forward-looking statements contained herein. The following discussion should be read in conjunction with our audited consolidated financial statements as of, and for the years ended, December 31, 2016, 2015 and 2014.

**Overview**

We are a wholly-owned subsidiary of Mediacom Communications Corporation ("MCC"), the nation's fifth largest cable company based on the number of customers who purchase one or more video services, or video customers. As of December 31, 2016, we served approximately 463,000 video customers, 643,000 high-speed data ("HSD") customers and 264,000 phone customers, aggregating 1.37 million primary service units ("PSUs"). As of the same date, we served 754,000 residential and business customer relationships.

We offer video, HSD and phone services individually and in bundled packages to residential and small- to medium-sized business ("SMB") customers over our hybrid fiber and coaxial cable ("HFC") network, and provide fiber-based network and transport services to medium- and large-sized businesses, governments and educational institutions. We also sell advertising to local, regional and national advertisers on television and digital platforms, and offer home security and automation services to residential customers. Our services are typically offered on a subscription basis, with installation fees, monthly rates and related charges associated with the services, equipment and features customers choose. We offer discounted packages for new customers and those who take multiple services, and our Xstream marketing brand offers bundled packages that include video with digital video recorder ("DVR") service and set-tops with the TiVo guide, HSD with a wireless gateway, and phone service. We believe the simplified pricing and value proposition of our Xstream bundles has positively influenced the market's perception of our products and services, and has driven higher levels of sales activity.

Over the past several years, revenues from residential services have increased mainly due to residential HSD customer growth. We expect to continue to grow revenues from residential services through HSD customer growth and increased revenue per customer relationship as more customers take faster HSD tiers and advanced video services, including our next-generation set-top and DVR service. Our business services revenues have grown at a meaningfully faster rate than our residential revenues as we have rapidly expanded our SMB and, to a lesser extent, enterprise customer base. In an effort to sustain or accelerate our rate of growth in business services revenues, we have recently commenced "Project Open Road," where we plan to extend our network to a meaningful number of new commercial locations that contain multiple businesses that represent potential customers.

Our residential video service principally competes with direct broadcast satellite ("DBS") providers that offer video programming substantially similar to ours. Over the past several years, we have experienced meaningful video customer losses, as DBS competitors have deployed aggressive marketing campaigns, including deeply discounted promotional packages, more advanced customer premise equipment and exclusive sports programming. We have placed a greater emphasis on higher quality residential customer relationships, as we have generally eliminated or reduced tactical discounts for customers not likely to purchase two or more services or to stay with us for an extended period, which may further contribute to video customer declines. To appeal to such higher-quality residential consumers, we have deployed a next-generation Internet Protocol ("IP") set-top that offers a cloud-based, graphically-rich TiVo guide with access and integrated search functionality to certain third-party Internet-based video applications ("video apps"), such as Netflix, Hulu, and YouTube, along with a multi-room DVR service and the ability to download certain content to personal devices. In 2017, we also plan to introduce a new, lower-cost, IP set-top that offers the TiVo guide and video apps, but without the required equipment for DVR service. We believe our video strategy has enabled us to reduce the rate of video customer losses and regain market share of new video connects. If we are unsuccessful with this strategy and cannot offset video customer losses through higher average unit pricing and greater penetration of our advanced video services, we may experience future declines in annual video revenues.

Our residential HSD service competes primarily with digital subscriber line ("DSL") services offered by local phone companies, and we have continued to grow our HSD customer base over the last several years. We believe our HSD service is generally superior to DSL offerings in our service areas as our minimum downstream speed of 60 megabits per second ("Mbps") is faster than the highest speed offered by substantially all our DSL competition. As consumers' bandwidth requirements have dramatically risen in recent years, we have dedicated increasing levels of capital expenditures to allow for faster speeds and greater levels of consumption. Through "Project Gigabit," we have installed the necessary equipment to transition substantially all our homes passed to the DOCSIS 3.1 platform, which will allow us to introduce packages offering speeds of up to 1 gigabit per second ("Gbps") across most of our markets in 2017. We expect to continue to grow HSD revenues as we further take market share and our HSD customers choose higher speed tiers.

Our residential phone service mainly competes with substantially comparable phone services offered by local phone companies and cellular phone services offered by national wireless providers. We believe we will continue to grow residential phone customers, but may experience modest declines in phone revenues due to unit pricing pressure.

## Table of Contents

Our business services primarily compete for SMB customers with local phone companies, many of which have had a historical advantage given long-term relationships with such customers, a nation-wide footprint that allows them to more effectively serve multiple locations, and existing networks built in certain commercial areas that we do not currently serve. Our cell tower backhaul and enterprise-level services also face competition from these local phone companies as well as other carriers, including metro and regional fiber-based carriers. In recent years, we have aggressively marketed our business services and expanded our network into additional commercial areas, which has allowed us to gain meaningful market share and led to strong growth rates of business services revenues in the past several years, which we believe will continue.

We compete for advertising revenues principally against local broadcast stations, national cable and broadcast networks, radio, newspapers, magazines, outdoor display and Internet companies. Competition will likely elevate as new formats for advertising are introduced into our markets.

Historically, video programming has been our single largest expense, and we have experienced substantial increases in programming costs per video customer, particularly for sports and local broadcast programming, well in excess of the inflation rate or the change in the consumer price index. We believe these expenses will continue to grow at a high single- to low double-digit rate because of the demands of large media conglomerates or other owners of most of the popular cable networks and major market local broadcast stations, and of large independent television broadcast groups, who own or control a significant number of local broadcast stations across the country and, in some cases, own, control or otherwise represent multiple stations in the same market. Moreover, many of those powerful owners of programming require us to purchase their networks and stations in bundles and effectively dictate how we offer them to our customers, given the contractual economic penalties if we fail to comply. Consequently, we have little or no ability to individually or selectively negotiate for networks or stations, to forego purchasing networks or stations that generate low customer interest, to offer sports programming services, such as ESPN and regional sports networks, on one or more separate tiers, or to offer networks or stations on an a la carte basis to give our customers more choice and potentially lower their costs. In many instances, such programmers have created additional networks and migrated popular programming, particularly sports programming, to these new networks, which has contributed to the increases in our programming costs. Additionally, we believe certain programmers may also demand higher fees from us in an effort to partially offset declines in their advertising revenue as more advertisers allocate a greater portion of their spending to Internet advertising. While such growth in programming expenses can be offset, in whole or in part, by rate increases, we expect our video gross margins will continue to decline if increases in programming costs outpace any growth in video revenues.

## **Recent Developments**

### *MCC's Capital Plan*

In 2016, MCC announced a plan for approximately \$1 billion of total capital expenditures to be made by us and Mediacom LLC during the three years ending December 2018 ("MCC's Capital Plan"). Among the planned initiatives under MCC's Capital Plan include:

- "Project Gigabit," a wide-scale deployment of next-generation DOCSIS 3.1 technology that allows the provisioning of 1 Gbps HSD service to substantially all of MCC's homes passed;
- "Project Open Road," which will connect over 70,000 new commercial locations that contain multiple potential customers in an effort to continue to grow business services revenues at an accelerated rate;
- Residential line extensions resulting in at least 50,000 additional homes passed; and
- Development of community Wi-Fi access points throughout high-traffic commercial and public areas.

During the year ended December 31, 2016, MCC made an aggregate \$335.2 million of capital expenditures, of which \$179.9 million was invested by us. We expect similar levels of capital investments by us and MCC over each of the next two years, with our portion of the initiatives outlined above approximating a level that is commensurate with our capital expenditures as a percentage of MCC's total capital expenditures. We have already made meaningful progress under MCC's Capital Plan, including the recent announcement that MCC has become the first major U.S. cable company to have fully installed the necessary equipment to transition to the DOCSIS 3.1 platform. We believe these initiatives will allow us to continue to improve our competitive position for both residential and business services customers in our markets, with additional future revenue and cash flow growth driven by incremental gains in market share than we would have experienced otherwise.

## Table of Contents

### Revenues

#### *Video*

Video revenues primarily represent monthly subscription fees charged to residential customers, which vary according to the level of service, the type and amount of equipment taken, and revenue from the sale of VOD content and pay-per-view events. Video revenues also include installation, reconnection and wire maintenance fees, franchise and late payment fees, and other ancillary revenues.

#### *HSD*

HSD revenues primarily represent monthly subscription fees charged to residential customers, which vary according to the level of service and type of equipment taken.

#### *Phone*

Phone revenues primarily represent monthly subscription and equipment fees charged to residential customers for our phone service.

#### *Business Services*

Business services revenues primarily represent monthly fees charged to SMBs for video, HSD and phone services, which vary according to the level of service taken, and fees charged to large businesses, including revenues from cell tower backhaul and enterprise class services.

#### *Advertising*

Advertising revenues primarily represent revenues received from selling advertising time we receive under programming license agreements to local, regional and national advertisers for the placement of commercials on channels offered on our video services.

### Costs and Expenses

#### *Service Costs*

Service costs consist of the costs related to providing and maintaining services to our customers. Significant service costs comprise: video programming; HSD service, including bandwidth connectivity; phone service, including leased circuits and long distance; our enterprise networks business, including leased access; technical personnel who maintain the cable network, perform customer installation activities and provide customer support; network operations center; utilities, including pole rental; and field operations, including outside contractors, vehicle fuel and maintenance and leased fiber for regional connectivity.

Video programming costs, which are generally paid on a per-video customer basis, have historically represented our single largest expense. In recent years, we have experienced substantial increases in the per-unit cost of programming, which we believe will continue to grow due to the increasing contractual rates and retransmission consent fees demanded by large programmers and independent broadcasters. Our HSD costs fluctuate depending on customers' bandwidth consumption and customer growth. Phone service costs are mainly determined by network configuration, customers' long distance usage and net termination payments to other carriers. Our other service costs generally rise as a result of customer growth and inflationary cost increases for personnel, outside vendors and other expenses. Personnel and related support costs may increase as the percentage of expenses that we capitalize declines due to lower levels of new service installations. We anticipate that service costs, with the exception of programming expenses, will remain fairly consistent as a percentage of our revenues.

#### *Selling, General and Administrative Expenses*

Significant selling, general and administrative expenses comprise: call center, customer service, marketing, business services, support and administrative personnel; franchise fees and other taxes; bad debt; billing; marketing; advertising; and general office administration. These expenses generally rise due to customer growth and inflationary cost increases for personnel, outside vendors and other expenses. We anticipate that selling, general and administrative expenses will remain fairly consistent as a percentage of our revenues.

## Table of Contents

Service costs and selling, general and administrative expenses exclude depreciation and amortization, which we present separately.

### *Management Fee Expense*

Management fee expense reflects compensation paid to MCC for the performance of services it provides our operating subsidiaries in accordance with management agreements between MCC and our operating subsidiaries.

### *Capital Expenditures*

Capital expenditures are categorized in accordance with the National Cable and Telecommunications Association ("NCTA") disclosure guidelines, which are intended to provide more consistency in the reporting of capital expenditures among peer companies in the cable industry. These disclosure guidelines are not required under GAAP, nor do they impact our accounting for capital expenditures under GAAP. Our capital expenditures comprise:

- Customer premise equipment, which include equipment and labor costs incurred in the purchase and installation of equipment that resides at a residential or commercial customer's premise;
- Enterprise networks, which include costs associated with furnishing custom fiber solutions for medium- to large-sized business customers, including for cell tower backhaul;
- Scalable infrastructure, which include costs incurred in the purchase and installation of equipment at our facilities associated with network-wide distribution of services;
- Line extensions, which include costs associated with the extension of our network into new service areas;
- Upgrade / rebuild, which include costs to modify or replace existing components of our network; and
- Support capital, which include vehicles and all other capital purchases required to support our customers and general business operations.

### **Use of Non-GAAP Financial Measures**

"OIBDA" is not a financial measure calculated in accordance with generally accepted accounting principles ("GAAP") in the United States. We define OIBDA as operating income before depreciation and amortization. OIBDA has inherent limitations as discussed below.

OIBDA is one of the primary measures used by management to evaluate our performance and to forecast future results. We believe OIBDA is useful for investors because it enables them to assess our performance in a manner similar to the methods used by management, and provides a measure that can be used to analyze our value and evaluate our performance compared to other companies in the cable industry. A limitation of OIBDA, however, is that it excludes depreciation and amortization, which represents the periodic costs of certain capitalized tangible and intangible assets used in generating revenues in our business. Management uses a separate process to budget, measure and evaluate capital expenditures. In addition, OIBDA may not be comparable to similarly titled measures used by other companies, which may have different depreciation and amortization policies.

OIBDA should not be regarded as an alternative to operating income or net income as an indicator of operating performance, or to the statement of cash flows as a measure of liquidity, nor should it be considered in isolation or as a substitute for financial measures prepared in accordance with GAAP. We believe that operating income is the most directly comparable GAAP financial measure to OIBDA.

Table of Contents*Year Ended December 31, 2016 Compared to Year Ended December 31, 2015 Compared to Year Ended December 31, 2014*

The table below sets forth our consolidated statements of operations and OIBDA for the years ended December 31, 2016, 2015 and 2014 (dollars in thousands and percentage changes that are not meaningful are marked NM):

	Year Ended December 31,			% Change	% Change
	2016	2015	2014	2015 to 2016	2014 to 2015
Revenues	\$ 1,033,239	\$ 982,362	\$ 948,447	5.2%	3.6%
Costs and expenses:					
Service costs (exclusive of depreciation and amortization)	419,406	401,751	381,014	4.4%	5.4%
Selling, general and administrative expenses	193,669	182,144	180,084	6.3%	1.1%
Management fee expense	20,800	19,000	17,650	9.5%	7.6%
Depreciation and amortization	147,114	144,220	153,478	2.0%	(6.0%)
Operating income	252,250	235,247	216,221	7.2%	8.8%
Interest expense, net	(78,725)	(94,668)	(100,436)	(16.8%)	(5.7%)
Gain on derivatives, net	1,203	9,173	23,226	NM	NM
Loss on early extinguishment of debt	(1,156)	(4,382)	(300)	NM	NM
Other expense, net	(1,686)	(1,377)	(1,262)	22.4%	9.1%
Net income	\$ 171,886	\$ 143,993	\$ 137,449	19.4%	4.8%
OIBDA	\$ 399,364	\$ 379,467	\$ 369,699	5.2%	2.6%

The table below represents a reconciliation of OIBDA to operating income, which we believe is the most directly comparable GAAP measure (dollars in thousands):

	Year Ended December 31,			% Change	% Change
	2016	2015	2014	2015 to 2016	2014 to 2015
OIBDA	\$ 399,364	\$ 379,467	\$ 369,699	5.2%	2.6%
Depreciation and amortization	(147,114)	(144,220)	(153,478)	2.0%	(6.0%)
Operating income	\$ 252,250	\$ 235,247	\$ 216,221	7.2%	8.8%

Table of Contents*Revenues*

The tables below set forth revenue and selected customer and average monthly revenue statistics as of, and for the years ended, December 31, 2016, 2015 and 2014 (dollars in thousands, except per unit data):

	Year Ended December 31,			% Change 2015 to 2016	% Change 2014 to 2015
	2016	2015	2014		
Video	\$ 450,658	\$451,446	\$449,038	(0.2%)	0.5%
HSD	331,778	295,049	265,685	12.4%	11.1%
Phone	57,999	60,087	63,111	(3.5%)	(4.8%)
Business services	141,054	128,684	115,348	9.6%	11.6%
Advertising	51,750	47,096	55,265	9.9%	(14.8%)
Total	<u>\$1,033,239</u>	<u>\$982,362</u>	<u>\$948,447</u>	<u>5.2%</u>	<u>3.6%</u>

	Year Ended December 31,			% Change 2015 to 2016	% Change 2014 to 2015
	2016	2015	2014		
Video customers	463,000	480,000	500,000	(3.5%)	(4.0%)
HSD customers	643,000	605,000	564,000	6.3%	7.3%
Phone customers	264,000	239,000	218,000	10.5%	9.6%
Primary service units (PSUs)	<u>1,370,000</u>	<u>1,324,000</u>	<u>1,282,000</u>	<u>3.5%</u>	<u>3.3%</u>
Customer relationships	754,000	732,000	710,000	3.0%	3.1%
Average total monthly revenue per customer relationship (1)	\$ 115.89	\$ 113.54	\$ 111.32	2.1%	2.0%

(1) Represents average total monthly revenues for the year divided by average customer relationships for the year.

Revenues increased 5.2% for year ended December 31, 2016, due to greater HSD and, to a much lesser extent, business services and advertising revenues, slightly offset by declines in phone and, to a lesser extent, video revenues.

Revenues increased 3.6% for the year ended December 31, 2015, due to greater HSD and, to a lesser extent, business services and video revenues, offset in part by declines in advertising and, to a lesser extent, phone revenues.

*Video*

Video revenues declined 0.2% for the year ended December 31, 2016, mainly due to a lower residential video customer base compared to the prior year, mostly offset by rate adjustments associated with the pass-through of higher programming costs for retransmission consent fees and, to a much lesser extent, for regional sports networks and more customers taking our advanced video services.

Video revenues increased 0.5% for the year ended December 31, 2015, largely due to rate adjustments associated with the pass-through of higher programming costs for retransmission consent fees and, to a lesser extent, for regional sports networks, mostly offset by a lower residential video customer base compared to the prior year.

We lost 17,000, 20,000 and 28,000 video customers during the years ended December 31, 2016, 2015 and 2014, respectively. As of December 31, 2016, we served 463,000 video customers, or 30.8% of our estimated homes passed, and 42.0% of our residential video customers took our DVR service, which represents a large component of revenues from advanced video services.

*HSD*

HSD revenues grew 12.4% and 11.1% for the years ended December 31, 2016 and 2015, respectively, primarily due to more customers paying higher rates for faster speed tiers and a greater residential HSD customer base compared to the prior years.

We gained 38,000, 41,000 and 30,000 HSD customers during the years ended December 31, 2016, 2015 and 2014, respectively. As of December 31, 2016, we served 643,000 HSD customers, or 42.8% of our estimated homes passed, and 49.3% of our residential HSD customers took our wireless home gateway service.

## Table of Contents

### *Phone*

Phone revenues decreased 3.5% and 4.8% for the years ended December 31, 2016 and 2015, respectively, principally due to higher levels of discounted pricing, offset in part by a greater residential phone customer base compared to the prior years.

We gained 25,000, 21,000 and 11,000 phone customers during the years ended December 31, 2016, 2015 and 2014, respectively. As of December 31, 2016, we served 264,000 phone customers, or 17.6% of our estimated homes passed.

### *Business Services*

Business services revenues rose 9.6% and 11.6% for the years ended December 31, 2016 and 2015, respectively, mainly due to a greater SMB customer base compared to the prior years.

### *Advertising*

Advertising revenues grew 9.9% for the year ended December 31, 2016, predominantly due to higher levels of political advertising compared to the prior year. Advertising revenues fell 14.8% for the year ended December 31, 2015, substantially due to lower levels of political advertising compared to the prior year.

### *Costs and Expenses*

#### *Service Costs*

Service costs increased 4.4% and 5.4% for the years ended December 31, 2016 and 2015, respectively, primarily due to greater video programming charges and, to a lesser extent, for the year ended December 31, 2016, employee costs. Programming costs grew 4.4% and 7.8% for the years ended December 31, 2016 and 2015, respectively, principally due to higher fees associated with the renewal of programming contracts and contractual increases under agreements with certain local broadcast stations and cable networks, offset in part by a lower video customer base compared to the prior years. Employee costs were 6.0% higher for the year ended December 31, 2016, largely due to increased technical, maintenance and other operating employee staff and compensation levels.

Service costs as a percentage of revenues were 40.6%, 40.9% and 40.2% for the years ended December 31, 2016, 2015 and 2014, respectively.

#### *Selling, General and Administrative Expenses*

Selling, general and administrative expenses increased 6.3% for the year ended December 31, 2016, largely as a result of greater marketing, employee and, to a lesser extent, bad debt and advertising expenses. Marketing expenses rose 11.3%, principally due to expenses related to marketing of our Xstream bundled services and, to a lesser extent, the marketing of our business services and a greater use of third-party sales services. Employee expenses increased 3.6%, mainly due to greater customer service and other administrative employee staff and compensation levels. Bad debt grew 14.0%, substantially due to the aging of business customer accounts. Advertising expenses rose 16.5%, predominantly due to new promotional activity for our advertising sales group.

Selling, general and administrative expenses increased 1.1% for the year ended December 31, 2015, largely as a result of greater marketing costs, offset in part by lower bad debt and administrative expenses. Marketing costs grew 11.7%, principally due to expenses related to the marketing of our Xstream bundled services, the marketing of our business services and greater use of third-party sales services. Bad debt declined 8.0%, substantially due to a lower number of written off accounts. Administrative expenses fell 20.8%, mainly as a result of lower customer service software expenses and a decline in legal and other professional fees.

Selling, general and administrative expenses as a percentage of revenues were 18.7%, 18.5% and 19.0% for the years ended December 31, 2016, 2015 and 2014, respectively.

#### *Management Fee Expense*

Management fee expense grew 9.5% and 7.6% for the years ended December 31, 2016 and 2015, respectively, reflecting higher fees charged by MCC. Management fee expense as a percentage of revenues were 2.0%, 1.9% and 1.9% for the years ended December 31, 2016, 2015 and 2014, respectively.

## Table of Contents

### *Depreciation and Amortization*

Depreciation and amortization was 2.0% higher for the year ended December 31, 2016, as greater depreciation of investments in customer premise equipment, HSD bandwidth expansion and business support were offset in part by long-lived network assets having been fully depreciated in the prior year.

Depreciation and amortization was 6.0% lower for the year ended December 31, 2015, mainly due to long-lived networks assets having been fully depreciated in the prior year, offset in part by greater depreciation of investments in customer premise equipment, HSD bandwidth expansion and business support.

### *Operating Income*

Operating income rose 7.2% and 8.8% for the years ended December 31, 2016 and 2015, respectively, as the increase in revenues was offset in part by higher service costs and selling, general and administrative expenses.

### *Interest Expense, Net*

Interest expense, net, fell 16.8% and 5.7% for the years ended December 31, 2016 and 2015, respectively, due to lower average borrowing costs as a result of recent favorable financing transactions and, for the year ended December 31, 2016, lower average outstanding indebtedness.

### *Gain on Derivatives, Net*

As a result of changes to the mark-to-market valuation of our interest rate exchange agreements, we recorded net gains on derivatives of \$1.2 million, \$9.2 million and \$23.2 million for the years ended December 31, 2016, 2015 and 2014, respectively. See Notes 4 and 6 in our Notes to Consolidated Financial Statements.

### *Loss on Early Extinguishment of Debt*

Loss on early extinguishment of debt totaled \$1.2 million, \$4.4 million and \$0.3 million for the years ended December 31, 2016, 2015 and 2014, respectively, which represented the write-off of unamortized financing costs as a result of the repayment of certain previously existing term loans under our bank credit facility.

### *Other Expense, Net*

Other expense, net, was \$1.7 million for the year ended December 31, 2016, representing \$1.5 million of revolving credit commitment fees and \$0.2 million of other net fees, \$1.4 million for the year ended December 31, 2015, representing \$1.2 million of revolving credit commitment fees and \$0.2 million of other net fees, and \$1.3 million for the year ended December 31, 2014, representing \$1.4 million of revolving credit commitment fees, partly offset by \$0.1 million of other net income.

### *Net Income*

As a result of the factors described above, we recognized net income of \$171.9 million, \$144.0 million and \$137.4 million for the years ended December 31, 2016, 2015 and 2014, respectively.

### *OIBDA*

OIBDA grew 5.2% and 2.6% for the years ended December 31, 2016 and 2015, respectively, primarily due to the increase in revenues, offset in part by higher service costs and selling, general and administrative expenses.

### **Liquidity and Capital Resources**

Our net cash flows provided by operating activities are primarily used to fund investments to enhance the capacity and reliability of our network and further expand our products and services, and make scheduled and voluntary repayments of our indebtedness and periodic distributions to MCC. As of December 31, 2016, our near-term liquidity requirements included term loan principal repayments of \$16.6 million over the next twelve months. As of the same date, our sources of liquidity included \$14.2 million of cash and

\$246.2 million of unused and available commitments under our \$368.5 million revolving credit facility, after giving effect to \$112.6 million of outstanding loans and \$9.7 million of letters of credit issued to various parties as collateral.

## Table of Contents

We believe that we will be able to continue to meet our current and long-term liquidity and capital requirements, including fixed charges, through existing cash, internally generated cash flows from operating activities, cash available to us under our revolver credit commitments and our ability to obtain future financing. If we are unable to obtain sufficient future financing on acceptable terms, or at all, we may need to take other actions to conserve or raise capital that we would not take otherwise. However, we have accessed the debt markets for significant amounts of capital in the past, and expect to continue to be able to access these markets in the future as necessary.

### *Net Cash Flows Provided by Operating Activities*

Net cash flows provided by operating activities were \$336.0 million for the year ended December 31, 2016, primarily due to OIBDA of \$399.4 million and the \$11.5 million net change in our operating assets and liabilities, offset in part by interest expense of \$78.7 million. The net change in our operating assets and liabilities was primarily due to increases in accounts payable, accrued expenses, and other current liabilities of \$5.9 million and in accounts payable to affiliates of \$4.1 million, a decrease in accounts receivable, net, of \$2.0 million and an increase in deferred revenue of \$2.0 million, offset in part by an increase in prepaid expenses and other assets of \$2.4 million.

Net cash flows provided by operating activities were \$297.2 million for the year ended December 31, 2015, primarily due to OIBDA of \$379.5 million and the \$6.9 million net change in our operating assets and liabilities, offset in part by interest expense of \$94.7 million. The net change in our operating assets and liabilities was primarily due to increases in accounts payable, accrued expenses, and other current liabilities of \$10.2 million, in accounts payable to affiliates of \$9.2 million and in deferred revenue of \$1.7 million, offset in part by increases in accounts receivable, net, of \$10.6 million and in prepaid expenses and other assets of \$4.3 million.

### *Net Cash Flows Used in Investing Activities*

Capital expenditures continue to be our primary use of capital resources and generally comprise substantially all of our net cash flows used in investing activities.

Net cash flows used in investing activities were \$183.3 million for the year ended December 31, 2016, substantially comprising \$179.7 million of capital expenditures and a net change in accrued property, plant, and equipment of \$3.8 million.

Net cash flows used in investing activities were \$148.3 million for the year ended December 31, 2015, substantially comprising \$151.2 million of capital expenditures and \$1.6 million associated with the acquisition of other intangible assets, slightly offset by a net change in accrued property, plant and equipment of \$4.9 million.

### *Capital Expenditures*

The table below sets forth our capital expenditures (dollars in thousands):

	Year Ended December 31,			\$ Change 2015 to 2016	\$ Change 2014 to 2015
	2016	2015	2014		
Customer premise equipment	\$ 75,033	\$ 80,885	\$ 62,746	\$ (5,852)	\$ 18,139
Enterprise networks	10,367	9,209	11,621	1,158	(2,412)
Scalable infrastructure	41,688	21,277	28,621	20,411	(7,344)
Line extensions	15,141	6,351	6,155	8,790	196
Upgrade / rebuild	23,610	20,306	16,074	3,304	4,232
Support capital	13,857	13,176	12,058	681	1,118
Total capital expenditures	<u>\$179,696</u>	<u>\$151,204</u>	<u>\$137,275</u>	<u>\$ 28,492</u>	<u>\$ 13,929</u>

Capital expenditures for the year ended December 31, 2016, increased \$28.5 million, largely reflecting greater investments in scalable infrastructure, mainly next-generation HSD network equipment for Project Gigabit, and, to a lesser extent, the expansion of our network, largely for Project Open Road, offset in part by lower spending on customer premise equipment, primarily for our next-generation set-top.

Capital expenditures for the year ended December 31, 2015, increased \$13.9 million, largely reflecting greater investments in customer premise equipment, mainly our next-generation set-top and, to a lesser extent, the expansion of our fiber network, offset by lower

spending on scalable infrastructure, largely for local HSD bandwidth management and, to a lesser extent, enterprise networks, primarily for fiber connectivity to cell towers.

## Table of Contents

### *Net Cash Flows Used in Financing Activities*

Net cash flows used in financing activities were \$149.0 million for the year ended December 31, 2016, comprising \$201.8 million of net repayments under the credit facility, \$18.0 million of dividend payments on preferred members' interest and \$7.0 million of capital distributions to our parent, MCC, offset in part by \$75.0 million of capital contributions from our parent, MCC, and \$2.8 million of other financing activities.

Net cash flows used in financing activities were \$148.0 million for the year ended December 31, 2015, substantially comprising \$127.3 million of net repayments under the credit facility, \$18.0 million of dividend payments on preferred members' interest and \$2.3 million of financing costs.

### **Capital Structure**

As of December 31, 2016, our total indebtedness was \$1.628 billion, of which approximately 68% was at fixed interest rates or had interest rate exchange agreements that fixed the variable portion of debt. During the year ended December 31, 2016, we paid cash interest of \$76.7 million, net of capitalized interest.

### *2016 Financing Activity*

On May 19, 2016, we repaid the entire \$245.6 million balance of Term Loan I under our bank credit facility, funded by borrowings of \$170.6 million under our revolving credit commitments and \$75.0 million of capital contributions from our parent, MCC.

### *Bank Credit Facility*

As of December 31, 2016, we maintained a \$1.384 billion credit facility, comprising \$1,015.4 million of term loans with maturities ranging from January 2021 to June 2021, and \$368.5 million of revolving credit commitments, which are scheduled to expire in October 2019. As of the same date, we had \$246.2 million of unused lines under our revolving credit commitments, all of which were available to be borrowed and used for general corporate purposes, after taking into account \$112.6 million of outstanding loans and \$9.7 million of letters of credit issued thereunder to various parties as collateral.

The credit facility is collateralized by our ownership interests in our operating subsidiaries, and is guaranteed by us on a limited recourse basis to the extent of such ownership interests. The credit agreement governing the credit facility (the "credit agreement") requires us to maintain a total leverage ratio (as defined in the credit agreement) of no more than 5.0 to 1.0 and an interest coverage ratio (as defined in the credit agreement) of no less than 2.0 to 1.0. For all periods through December 31, 2016, our operating subsidiaries were in compliance with all covenants under the credit agreement including, as of the same date, a total leverage ratio of 2.5 to 1.0 and an interest coverage ratio of 4.4 to 1.0. We do not believe that our operating subsidiaries will have any difficulty complying with any of the covenants under the credit agreement in the near future.

### *Interest Rate Swaps*

We have entered into several interest rate exchange agreements (which we refer to as "interest rate swaps") with various banks to fix the variable rate on a portion of our borrowings under the credit facility to reduce the potential volatility in our interest expense that may result from changes in market interest rates. As December 31, 2016, we had interest rate swaps that fixed the variable portion of \$600 million of borrowings at a rate of 1.5%, all of which are scheduled to expire during December 2018.

As of December 31, 2016, the weighted average rate on outstanding borrowings under the credit facility, including the effects of our interest rate swaps, was 3.5%.

### *Senior Notes*

As of December 31, 2016, we had \$500.0 million of outstanding senior notes, comprising \$200.0 million of 5 1/2% senior notes due April 2021 and \$300.0 million of 6 3/8% senior notes due April 2023.

Our senior notes are unsecured obligations, and the indentures governing our senior notes (the "indentures") limit the incurrence of additional indebtedness based upon a maximum debt to operating cash flow ratio (as defined in the indentures) of 8.5 to 1.0. For all

## Table of Contents

periods through December 31, 2016, we were in compliance with covenants under the indentures including, as of the same date, a debt to operating cash flow ratio of 3.8 to 1.0. We do not believe that we will have any difficulty complying with any of the covenants under the indentures in the near future.

### *Debt Ratings*

MCC's corporate credit ratings are Ba3 by Moody's, with a positive outlook, and BB by Standard and Poor's ("S&P"), with a stable outlook, and our unsecured ratings are B2 by Moody's, with a positive outlook, and B+ by S&P, with a stable outlook.

There can be no assurance that Moody's or S&P will maintain their ratings on MCC and us. A negative change to these credit ratings could result in higher interest rates on future debt issuance than we currently experience, or adversely impact our ability to raise additional funds. There are no covenants, events of default, borrowing conditions or other terms in the credit agreement or indentures that are based on changes in our credit rating assigned by any rating agency.

### **Contractual Obligations and Commercial Commitments**

The following table summarizes our contractual obligations and commercial commitments, and the effects they are expected to have on our liquidity and cash flow, for the five years subsequent to December 31, 2016 and thereafter (dollars in thousands)\*:

	Scheduled <u>Debt Maturities</u>	Operating <u>Leases</u>	Interest Expense <u>(1)</u>	Purchase <u>Obligations (2)</u>	<u>Total</u>
January 1, 2017 to December 31, 2017	\$ 16,575	\$ 2,055	\$ 69,822	\$ 27,621	\$ 116,073
January 1, 2018 to December 31, 2019	145,725	2,504	134,336	—	282,565
January 1, 2020 to December 31, 2021	1,165,700	1,473	90,854	—	1,258,027
Thereafter	300,000	1,618	23,906	—	325,524
Total cash obligations	<u>\$ 1,628,000</u>	<u>\$ 7,650</u>	<u>\$ 318,918</u>	<u>\$ 27,621</u>	<u>\$ 1,982,189</u>

\* Refer to Note 6 and Note 11 in our Notes to Consolidated Financial Statements for a discussion of our long-term debt and of our operating leases and other commitments and contingencies, respectively.

- (1) Interest payments on floating rate debt and interest rate swaps are estimated using amounts outstanding as of December 31, 2016 and the average interest rates applicable under such debt obligations. Interest expense amounts are net of amounts capitalized.
- (2) We have contracts with programmers who provide video programming services to our customers. Our contracts typically provide that we have an obligation to purchase video programming for our customers as long as we deliver cable services to such customers. We have no obligation to purchase these services if we are not providing cable services, except when we do not have the right to cancel the underlying contract or for contracts with a guaranteed minimum commitment. There are no programming service amounts included in our purchase obligations. We also maintain other service agreements with various vendors that contain future contractual commitments.

### **Critical Accounting Policies**

The preparation of our financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. Periodically, we evaluate our estimates, including those related to doubtful accounts, long-lived assets, capitalized costs and accruals. We base our estimates on historical experience and on various other assumptions that we believe are reasonable. Actual results may differ from these estimates under different assumptions or conditions. We believe that the application of the critical accounting policies discussed below requires significant judgments and estimates on the part of management. For a summary of our accounting policies, see Note 2 in our Notes to Consolidated Financial Statements.

### *Property, Plant and Equipment*

We capitalize the costs of new construction and replacement of our cable transmission and distribution facilities and new service installation in accordance with Accounting Standards Codification ("ASC") No. 922 — *Entertainment — Cable Television*. Costs associated with subsequent installations of additional services not previously installed at a customer's dwelling are capitalized to the extent such costs are incremental and directly attributable to the installation of such additional services. Capitalized costs include all direct labor and materials as well as certain indirect costs. Capitalized costs are recorded as additions to property, plant and equipment

and depreciated over the average life of the related assets. We use standard costing models, developed from actual historical costs and relevant operational data, to determine our capitalized amounts. These models include labor rates, overhead rates and standard time

## Table of Contents

inputs to perform various installation and construction activities. The development of these standards involves significant judgment by management, especially in the development of standards for our newer, advanced products and services in which historical data is limited. Changes to the estimates or assumptions used in establishing these standards could be material. We perform periodic evaluations of the estimates used to determine the amount of costs that are capitalized. Any changes to these estimates, which may be significant, are applied in the period in which the evaluations were completed.

### *Valuation and Impairment Testing of Indefinite-lived Intangibles*

As of December 31, 2016, we had approximately \$1.4 billion of unamortized intangible assets, including franchise rights of \$1.2 billion and goodwill of \$0.2 billion on our consolidated balance sheets. Franchise rights are our largest asset and, together with goodwill, represent approximately 60% of our total assets as of the same date.

Our cable systems operate under non-exclusive cable franchises, or franchise rights, granted by state and local governmental authorities for varying lengths of time. We acquired these cable franchises through acquisitions of cable systems and were accounted for using the purchase method of accounting. As of December 31, 2016, we held 501 franchises in areas located throughout the United States. The value of a franchise is derived from the economic benefits we receive from the right to solicit new customers and to market new products and services, such as digital video, HSD and phone, in a specific market territory. We concluded that our franchise rights have an indefinite useful life since, among other things, there are no legal, regulatory, contractual, competitive, economic or other factors limiting the period over which these franchise rights contribute to our revenues and cash flows. Goodwill is the excess of the acquisition cost of an acquired entity over the fair value of the identifiable net assets acquired. In accordance with ASC No. 350 — *Intangibles — Goodwill and Other* (“ASC 350”), we do not amortize franchise rights and goodwill. Instead, such assets are tested annually for impairment or more frequently if impairment indicators arise.

We follow the provisions of ASC 350 to test our goodwill and franchise rights for impairment. We assess the fair values of our reporting unit using the Excess Earnings Method of the Income Approach as our discounted cash flow (“DCF”) methodology, under which the fair value of cable franchise rights are determined in a direct manner. We employ the Multi-Period Excess Earnings Method to calculate the fair values of our cable franchise rights, using unobservable inputs (Level 3). This assessment involves significant judgment, including certain assumptions and estimates that determine future cash flow expectations and other future benefits, which are consistent with the expectations of buyers and sellers of cable systems in determining fair value. These assumptions and estimates include discount rates, estimated growth rates, terminal growth rates, revenues per customer, market penetration as a percentage of homes passed and operating margin. We also consider market transactions, market valuations, research analyst estimates and other valuations using multiples of operating income before depreciation and amortization to confirm the reasonableness of fair values determined by the DCF methodology. We also employ the Greenfield model to corroborate the fair values of our cable franchise rights determined under the In-use Excess Earnings DCF methodology. Significant impairment in value resulting in impairment charges may result if the estimates and assumptions used in the fair value determination change in the future. Such impairments, if recognized, could potentially be material.

Based on the guidance outlined in ASC 350, we have determined that the unit of accounting, or reporting unit, for testing goodwill and franchise rights is Mediacom Broadband. Comprising cable system clusters across several states, Mediacom Broadband is at the financial reporting level that is managed and reviewed by the corporate office (i.e., chief operating decision maker) including our determination as to how we allocate capital resources and utilize the assets. The reporting unit level also reflects the level at which the purchase method of accounting for our acquisitions was originally recorded.

In accordance with ASC 350, we are required to determine goodwill impairment using a two-step process. The first step compares the fair value of a reporting unit with our carrying amount, including goodwill. If the fair value of the reporting unit exceeds our carrying amount, goodwill of the reporting unit is considered not impaired and the second step is unnecessary. If the carrying amount of a reporting unit exceeds our fair value, the second step is performed to measure the amount of impairment loss, if any. The second step compares the implied fair value of the reporting unit's goodwill, calculated using the residual method, with the carrying amount of that goodwill. If the carrying amount of the goodwill exceeds the implied fair value, the excess is recognized as an impairment loss.

The impairment test for our franchise rights and other intangible assets not subject to amortization consists of a comparison of the fair value of the intangible asset with its carrying value. If the carrying value of the intangible asset exceeds its fair value, the excess is recognized as an impairment loss.

Since our adoption of ASC 350 in 2002, we have not recorded any impairments as a result of our impairment testing. We completed our most recent impairment test as of October 1, 2016, which reflected no impairment of our franchise rights, goodwill or other intangible assets.



**Table of Contents**

For illustrative purposes, if there were a hypothetical decline of 15% in the fair values determined for cable franchise rights, goodwill and other finite-lived intangible assets at our reporting unit, no impairment loss would result as of our impairment testing date of October 1, 2016.

We could record impairments in the future if there are changes in the long-term fundamentals of our business, in general market conditions or in the regulatory landscape that could prevent us from recovering the carrying value of our long-lived intangible assets. The economic conditions affecting the U.S. economy, and how that may impact the fundamentals of our business, may have a negative impact on the fair values of the assets in our reporting unit.

In accordance with Accounting Standards Update No. 2010-28 — *When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts (a consensus of the FASB Emerging Issues Task Force)*, as of October 1, 2016 and 2015, we have evaluated whether there are any adverse qualitative factors surrounding our Mediacom Broadband reporting unit indicating that a goodwill impairment may exist. We do not believe that it is “more likely than not” that a goodwill impairment exists. As such, we have not performed Step 2 of the goodwill impairment test. As of both December 31, 2016 and 2015, the Mediacom Broadband reporting unit had a positive carrying amount.

**Recent Accounting Pronouncements**

See Note 2 in our Notes to the Consolidated Financial Statements.

**Inflation and Changing Prices**

Our costs and expenses are subject to inflation and price fluctuations. Such changes in costs and expenses can generally be passed through to customers. Programming costs have historically increased at rates in excess of inflation and are expected to continue to do so. We believe that under the FCC’s existing cable rate regulations we may increase rates for cable services to more than cover any increases in programming. However, competitive conditions and other factors in the marketplace may limit our ability to increase our rates.

Table of Contents**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

In the normal course of business, we use interest rate exchange agreements (which we refer to as "interest rate swaps") with counterparty banks to fix the variable rate on a portion of our borrowings under our credit facility. As of December 31, 2016, we had current interest rate swaps with various banks pursuant to which the interest rate on \$600 million of variable rate debt was fixed at a rate of 1.5%, all of which were scheduled to expire during December 2018. The fixed rates of our interest rate swaps are offset against the applicable variable rate to determine the related interest expense.

Under the terms of our interest rate swaps, we are exposed to credit risk in the event of nonperformance by our counterparties; however, we do not anticipate such nonperformance. As of December 31, 2016, based on their mark-to-market valuation, we would have paid approximately \$0.7 million, if we terminated these interest rate swaps. Our interest rate swaps and debt arrangements do not contain credit rating triggers that could affect our liquidity.

The table below provides the scheduled maturity and estimated fair value of our debt as of December 31, 2016 (dollars in thousands):

	<u>Senior Notes</u>	<u>Bank Credit Facility</u>	<u>Total</u>
Scheduled Maturity:			
January 1, 2017 to December 31, 2017	—	16,575	16,575
January 1, 2018 to December 31, 2018	—	16,575	16,575
January 1, 2019 to December 31, 2019	—	129,150	129,150
January 1, 2020 to December 31, 2020	—	16,575	16,575
January 1, 2021 to December 31, 2021	200,000	949,125	1,149,125
Thereafter	<u>300,000</u>	<u>—</u>	<u>300,000</u>
Total	<u>\$ 500,000</u>	<u>\$ 1,128,000</u>	<u>\$ 1,628,000</u>
Fair Value	<u>\$ 522,000</u>	<u>\$ 1,135,633</u>	<u>\$ 1,657,633</u>
Weighted Average Interest Rate	<u>6.0%</u>	<u>3.5%</u>	<u>4.3%</u>

Table of ContentsITEM 8. *FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA*

## MEDIACOM BROADBAND LLC AND SUBSIDIARIES

## INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

## Contents

	<u>Page</u>
<u>Report of Independent Registered Public Accounting Firm</u>	47
<u>Consolidated Balance Sheets as of December 31, 2016 and 2015</u>	48
<u>Consolidated Statements of Operations for the Years Ended December 31, 2016, 2015 and 2014</u>	49
<u>Consolidated Statements of Changes in Member's Equity for the Years Ended December 31, 2016, 2015 and 2014</u>	50
<u>Consolidated Statements of Cash Flows for the Years Ended December 31, 2016, 2015 and 2014</u>	51
<u>Notes to Consolidated Financial Statements</u>	52
<u>Financial Statement Schedule: Schedule II — Valuation and Qualifying Accounts</u>	71

**Table of Contents****Report of Independent Registered Public Accounting Firm**

To the Member of Mediacom Broadband LLC:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of Mediacom Broadband LLC and its subsidiaries at December 31, 2016 and December 31, 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the accompanying index presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States) and in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP  
March 3, 2017

Table of Contents

**MEDIACOM BROADBAND LLC AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(Dollars in thousands)

	<u>December 31,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash	\$ 14,208	\$ 10,442
Accounts receivable, net of allowance for doubtful accounts of \$3,857 and \$3,627	67,724	69,743
Prepaid expenses and other current assets	14,562	11,347
Total current assets	<u>96,494</u>	<u>91,532</u>
Property, plant and equipment, net of accumulated depreciation of \$1,619,301 and \$1,589,422	816,389	783,653
Franchise rights	1,176,908	1,176,908
Goodwill	195,945	195,945
Other assets, net of accumulated amortization of \$4,101 and \$3,054	6,418	8,995
Total assets	<u>\$ 2,292,154</u>	<u>\$ 2,257,033</u>
<b>LIABILITIES, PREFERRED MEMBERS' INTEREST AND MEMBER'S EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable, accrued expenses and other current liabilities	\$ 154,818	\$ 151,929
Accounts payable - affiliates	14,852	10,690
Deferred revenue	39,856	37,904
Current portion of long-term debt	16,575	19,075
Total current liabilities	<u>226,101</u>	<u>219,598</u>
Long-term debt, net (less current portion)	1,597,075	1,790,443
Other non-current liabilities	1,486	1,531
Total liabilities	<u>1,824,662</u>	<u>2,011,572</u>
Commitments and contingencies (Note 11)		
PREFERRED MEMBERS' INTEREST (Note 7)	150,000	150,000
<b>MEMBER'S EQUITY</b>		
Capital distributions	(37,348)	(105,493)
Retained earnings	354,840	200,954
Total member's equity	<u>317,492</u>	<u>95,461</u>
Total liabilities, preferred members' interest and member's equity	<u>\$ 2,292,154</u>	<u>\$ 2,257,033</u>

The accompanying notes are an integral part of these statements.

Table of Contents

**MEDIACOM BROADBAND LLC AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Dollars in thousands)

	<u>Year Ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Revenues	\$1,033,239	\$982,362	\$ 948,447
Costs and expenses:			
Service costs (exclusive of depreciation and amortization)	419,406	401,751	381,014
Selling, general and administrative expenses	193,669	182,144	180,084
Management fee expense	20,800	19,000	17,650
Depreciation and amortization	<u>147,114</u>	<u>144,220</u>	<u>153,478</u>
Operating income	252,250	235,247	216,221
Interest expense, net	(78,725)	(94,668)	(100,436)
Gain on derivatives, net	1,203	9,173	23,226
Loss on early extinguishment of debt (Note 6)	(1,156)	(4,382)	(300)
Other expense, net	<u>(1,686)</u>	<u>(1,377)</u>	<u>(1,262)</u>
Net income	\$ 171,886	\$143,993	\$ 137,449
Dividend to preferred members (Note 7)	<u>(18,000)</u>	<u>(18,000)</u>	<u>(18,000)</u>
Net income applicable to member	<u>\$ 153,886</u>	<u>\$125,993</u>	<u>\$ 119,449</u>

The accompanying notes are an integral part of these statements.

Table of Contents

**MEDIACOM BROADBAND LLC AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN MEMBER'S EQUITY**  
(Dollars in thousands)

	Capital Contributions (Distributions)	(Accumulated Deficit) Retained Earnings	Total
<b>Balance, December 31, 2013</b>	<u>\$ 57,443</u>	<u>\$ (44,488)</u>	<u>\$ 12,955</u>
Net income	—	137,449	137,449
Dividend payments to related party on preferred members' interest	—	(18,000)	(18,000)
Capital distributions to parent	(163,300)	—	(163,300)
Other	213	—	213
<b>Balance, December 31, 2014</b>	<u>\$ (105,644)</u>	<u>\$ 74,961</u>	<u>\$ (30,683)</u>
Net income	—	143,993	143,993
Dividend payments to related party on preferred members' interest	—	(18,000)	(18,000)
Other	151	—	151
<b>Balance, December 31, 2015</b>	<u>\$ (105,493)</u>	<u>\$ 200,954</u>	<u>\$ 95,461</u>
Net income	—	171,886	171,886
Dividend payments to related party on preferred members' interest	—	(18,000)	(18,000)
Capital contributions from parent	75,000	—	75,000
Capital distributions to parent	(7,000)	—	(7,000)
Other	145	—	145
<b>Balance, December 31, 2016</b>	<u>\$ (37,348)</u>	<u>\$ 354,840</u>	<u>\$ 317,492</u>

The accompanying notes are an integral part of these statements.

Table of Contents

**MEDIACOM BROADBAND LLC AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Dollars in thousands)

	Year Ended December 31,		
	2016	2015	2014
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income	\$ 171,886	\$ 143,993	\$ 137,449
Adjustments to reconcile net income to net cash flows provided by operating activities:			
Depreciation and amortization	147,114	144,220	153,478
Gain on derivatives, net	(1,203)	(9,173)	(23,226)
Loss on early extinguishment of debt (Note 6)	1,156	4,382	300
Amortization of deferred financing costs	5,617	6,909	6,132
Changes in assets and liabilities:			
Accounts receivable, net	2,019	(10,579)	(2,788)
Accounts receivable - affiliates	—	—	4,444
Prepaid expenses and other assets	(2,414)	(4,347)	880
Accounts payable, accrued expenses and other current liabilities	5,892	10,207	1,605
Accounts payable - affiliates	4,060	9,177	1,513
Deferred revenue	1,952	1,659	646
Other non-current liabilities	(45)	788	(141)
Net cash flows provided by operating activities	<u>\$ 336,034</u>	<u>\$ 297,236</u>	<u>\$ 280,292</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Capital expenditures	\$(179,696)	\$(151,204)	\$ (137,275)
Change in accrued property, plant and equipment	(3,841)	4,890	(315)
Proceeds from sale of assets	248	272	—
Acquisition of other intangible assets	—	(1,559)	—
Other, net	—	(688)	19
Net cash flows used in investing activities	<u>\$(183,289)</u>	<u>\$(148,289)</u>	<u>\$ (137,571)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
New borrowings of bank debt	\$ 378,575	\$ 430,125	\$ 853,750
Repayment of bank debt	(580,325)	(557,375)	(1,004,750)
Issuance of senior notes	—	—	200,000
Dividend payments on preferred members' interest (Note 7)	(18,000)	(18,000)	(18,000)
Capital contributions from parent (Notes 6 and 8)	75,000	—	—
Capital distributions to parent (Note 8)	(7,000)	—	(163,300)
Financing costs	—	(2,299)	(12,480)
Other financing activities	2,771	(408)	274
Net cash flows used in financing activities	<u>\$(148,979)</u>	<u>\$(147,957)</u>	<u>\$ (144,506)</u>
Net increase (decrease) in cash	3,766	990	(1,785)
CASH, beginning of year	10,442	9,452	11,237
CASH, end of year	<u>\$ 14,208</u>	<u>\$ 10,442</u>	<u>\$ 9,452</u>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>			
Cash paid during the period for interest, net of amounts capitalized	<u>\$ 76,738</u>	<u>\$ 82,753</u>	<u>\$ 92,739</u>

The accompanying notes are an integral part of these statements.

Table of Contents**MEDIACOM BROADBAND LLC AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****1. ORGANIZATION**

Mediacom Broadband LLC ("Mediacom Broadband" and collectively with its subsidiaries, "we," "our" or "us") is a Delaware limited liability company wholly-owned by Mediacom Communications Corporation ("MCC"). MCC is involved in the acquisition and operation of cable systems serving smaller cities and towns in the United States, and its cable systems are owned and operated through our operating subsidiaries and those of Mediacom LLC, a New York limited liability company wholly-owned by MCC. As limited liability companies, we and Mediacom LLC are not subject to income taxes and, as such, are included in the consolidated federal and state income tax returns of MCC, a C corporation.

Our principal operating subsidiaries conduct all of our consolidated operations and own substantially all of our consolidated assets. Our operating subsidiaries are separate and distinct legal entities and have no obligation, contingent or otherwise, to make funds available to us.

We rely on our parent, MCC, for various services such as corporate and administrative support. Our financial position, results of operations and cash flows could differ from those that would have resulted had we operated autonomously or as an entity independent of MCC. See Notes 8 and 9.

Mediacom Broadband Corporation, a Delaware corporation wholly-owned by us, co-issued, jointly and severally with us, public debt securities. Mediacom Broadband Corporation has no operations, revenues or cash flows and has no assets, liabilities or stockholders' equity on its balance sheet, other than a one-hundred dollar receivable from an affiliate and the same dollar amount of common stock. Therefore, separate financial statements have not been presented for this entity.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES***Basis of Preparation of Consolidated Financial Statements*

The consolidated financial statements include the accounts of us and our subsidiaries. All significant intercompany transactions and balances have been eliminated. Comprehensive income is equal to net income for all periods presented. The preparation of the consolidated financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The accounting estimates that require management's most difficult and subjective judgments include: assessment and valuation of intangibles, accounts receivable allowance, useful lives of property, plant and equipment and capitalized labor. Actual results could differ from those and other estimates.

*Reclassifications*

Certain reclassifications have been made to prior year amounts to conform to the current year presentation.

*Revenue Recognition*

Video, high speed data ("HSD"), phone and business services revenues are recognized when the services are provided to our customers. We generally bill customers in advance for the services and equipment they have chosen to use and record such amounts as deferred revenue until the services are provided and the equipment is used. Credit risk is managed by disconnecting services to customers who are deemed to be delinquent. Installation revenues are recognized as customer connections are completed because installation revenues are less than direct installation costs. Advertising sales are recognized in the period that the advertisements are exhibited. Deposits and up-front fees collected from customers are recognized as deferred revenue until the earnings process is complete. Under the terms of our franchise agreements, we are required to pay local franchising authorities up to 5% of our gross revenues derived from providing video service. We normally pass these fees through to our customers. Because franchise fees are our obligation, we present them on a gross basis with a corresponding expense. Franchise fees reported on a gross basis amounted to approximately \$22.7 million, \$22.1 million, and \$21.7 million for the years ended December 31, 2016, 2015 and 2014, respectively. Franchise fees are reported in video revenue and included in selling, general and administrative expenses.

## Table of Contents

### *Allowance for Doubtful Accounts*

The allowance for doubtful accounts represents our best estimate of probable losses in the accounts receivable balance. The allowance is based on the number of days outstanding, customer balances, recoveries, historical experience and other currently available information.

### *Concentration of Credit Risk*

Our accounts receivable are comprised of amounts due from customers in varying regions throughout the United States. Concentration of credit risk with respect to these receivables is limited due to the large number of customers comprising our customer base and their geographic dispersion. We invest our cash with high quality financial institutions.

### *Property, Plant and Equipment*

Property, plant and equipment are recorded at cost. Additions to property, plant and equipment generally include material, labor and indirect costs. Depreciation is calculated on a straight-line basis over the following useful lives:

Buildings	40 years
Leasehold improvements	Lesser of: life of respective lease or life of asset
Cable systems, equipment and customer devices	5-20 years
Vehicles	4-5 years
Furniture, fixtures, and office equipment	5 years

We capitalize improvements that extend asset lives and expense repairs and maintenance as incurred. At the time of retirements, write-offs, sales or other dispositions of property, the original cost and related accumulated depreciation are removed from the respective accounts and any resulting gains or losses are included in depreciation and amortization expense in the consolidated statement of operations.

We capitalize the costs associated with the construction of cable transmission and distribution facilities, new customer installations and indirect costs associated with our phone service. Costs include direct labor and material, as well as certain indirect costs including capitalized interest. We perform periodic evaluations of the estimates used to determine the amount and extent that such costs are capitalized. Any changes to these estimates, which may be significant, are applied in the period in which the evaluations were completed. The costs of disconnecting service at a customer's dwelling or reconnecting to a previously installed dwelling are charged as expense in the period incurred. Costs associated with subsequent installations of additional services not previously installed at a customer's dwelling are capitalized to the extent such costs are incremental and directly attributable to the installation of such additional services. See Note 3.

### *Capitalized Software Costs*

We account for internal-use software development and related costs in accordance with Accounting Standards Codification ("ASC") 350-40-*Intangibles-Goodwill and Other: Internal-Use Software*. Software development and other related costs consist of external and internal costs incurred in the application development stage to purchase and implement associated software. Costs incurred in the development of application and infrastructure of the software is capitalized and will be amortized over our respective estimated useful life of 5 years. During the years ended December 31, 2016 and 2015, we wrote off approximately \$3.3 million (\$2.8 million of which were fully amortized) and \$5.3 million (\$4.5 million of which was fully amortized), respectively, of software development costs. Capitalized software had a net book value of \$0.2 million and \$0.7 million as of December 31, 2016 and 2015, respectively.

### *Marketing and Promotional Costs*

Marketing and promotional costs are expensed as incurred and were \$35.7 million, \$31.9 million and \$24.3 million for the years ended December 31, 2016, 2015 and 2014, respectively.

### *Intangible Assets*

Our cable systems operate under non-exclusive cable franchises, or franchise rights, granted by state and local governmental authorities for varying lengths of time. We acquired these cable franchises through acquisitions of cable systems and were accounted

for using the purchase method of accounting. As of December 31, 2016, we held 501 franchises in areas located throughout the United States. The value of a franchise is derived from the economic benefits we receive from the right to solicit new customers and to market

## Table of Contents

our products and services, including video, HSD and phone, in a specific market territory. We concluded that our franchise rights have an indefinite useful life since, among other things, there are no legal, regulatory, contractual, competitive, economic or other factors limiting the period over which these franchise rights contribute to our revenues and cash flows. Goodwill is the excess of the acquisition cost of an acquired entity over the fair value of the identifiable net assets acquired. In accordance with ASC 350 — *Intangibles – Goodwill and Other* (“ASC 350”), we do not amortize franchise rights and goodwill. Instead, such assets are tested annually for impairment or more frequently if impairment indicators arise.

We follow the provisions of ASC 350 to test our goodwill and franchise rights for impairment. We assess the fair values of our reporting unit using the Excess Earnings Method of the Income Approach as our discounted cash flow (“DCF”) methodology, under which the fair value of cable franchise rights are determined in a direct manner. We employ the Multi-Period Excess Earnings Method to calculate the fair values of our cable franchise rights, using unobservable inputs (Level 3). This assessment involves significant judgment, including certain assumptions and estimates that determine future cash flow expectations and other future benefits, which are consistent with the expectations of buyers and sellers of cable systems in determining fair value. These assumptions and estimates include discount rates, estimated growth rates, terminal growth rates, comparable company data, revenues per customer, market penetration as a percentage of homes passed and operating margin. We also consider market transactions, market valuations, research analyst estimates and other valuations using multiples of operating income before depreciation and amortization to confirm the reasonableness of fair values determined by the DCF methodology. We also employ the Greenfield model to corroborate the fair values of our cable franchise rights determined under the In-use Excess Earnings DCF methodology. Significant impairment in value resulting in impairment charges may result if the estimates and assumptions used in the fair value determination change in the future. Such impairments, if recognized, could potentially be material.

Based on the guidance outlined in ASC 350, we have determined that the unit of accounting or reporting unit, for testing goodwill and franchise rights is Mediacom Broadband. Comprising cable system clusters across several states, Mediacom Broadband is at the financial reporting level that is managed and reviewed by the corporate office (i.e., chief operating decision maker) including our determination as to how we allocate capital resources and utilize the assets. The reporting unit level also reflects the level at which the purchase method of accounting for our acquisitions was originally recorded.

In accordance with ASC 350, we are required to determine goodwill impairment using a two-step process. The first step compares the fair value of a reporting unit with our carrying amount, including goodwill. If the fair value of the reporting unit exceeds our carrying amount, goodwill of the reporting unit is considered not impaired and the second step is unnecessary. If the carrying amount of a reporting unit exceeds our fair value, the second step is performed to measure the amount of impairment loss, if any. The second step compares the implied fair value of the reporting unit’s goodwill, calculated using the residual method, with the carrying amount of that goodwill. If the carrying amount of the goodwill exceeds the implied fair value, the excess is recognized as an impairment loss.

The impairment test for our franchise rights and other intangible assets not subject to amortization consists of a comparison of the fair value of the intangible asset with its carrying value. If the carrying value of the intangible asset exceeds its fair value, the excess is recognized as an impairment loss.

Since our adoption of ASC 350 in 2002, we have not recorded any impairments as a result of our impairment testing. We completed our most recent impairment test as of October 1, 2016, which reflected no impairment of our franchise rights, goodwill or other intangible assets.

We could record impairments in the future if there are changes in the long-term fundamentals of our business, in general market conditions or in the regulatory landscape that could prevent us from recovering the carrying value of our long-lived intangible assets. The economic conditions affecting the U.S. economy, and how that may impact the fundamentals of our business, may have a negative impact on the fair values of the assets in our reporting unit.

In accordance with Accounting Standards Update No. 2010-28 — *When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts (a consensus of the FASB Emerging Issues Task Force)*, as of October 1, 2016 and 2015, we have evaluated whether there are any adverse qualitative factors surrounding our Mediacom Broadband reporting unit indicating that a goodwill impairment may exist. We do not believe that it is “more likely than not” that a goodwill impairment exists. As such, we have not performed Step 2 of the goodwill impairment test. As of both December 31, 2016 and 2015, the Mediacom Broadband reporting unit had a positive carrying amount.

## Table of Contents

The following table details changes in the carrying value of goodwill for the years ended December 31, 2016 and 2015 (dollars in thousands):

Balance - December 31, 2014	\$195,945
Acquisitions	—
Dispositions	—
Balance - December 31, 2015	<u>\$195,945</u>
Acquisitions	—
Dispositions	—
Balance - December 31, 2016	<u><u>\$195,945</u></u>

### *Segment Reporting*

ASC 280 — *Segment Reporting* (“ASC 280”) requires the disclosure of factors used to identify an enterprise’s reportable segments. Our operations are organized and managed on the basis of cable system clusters within our service area. Each cable system cluster derives revenues from the delivery of similar products and services to a customer base that is also similar. Each cable system cluster deploys similar technology to deliver our products and services, operates within a similar regulatory environment and has similar economic characteristics. We evaluated the criteria for aggregation under ASC 280 and believe that we meet each of the respective criteria set forth and accordingly, have identified broadband services as our one reportable segment.

### *Accounting for Derivative Instruments*

We account for derivative instruments in accordance with ASC 815 — *Derivatives and Hedging*. These pronouncements require that all derivative instruments be recognized on the balance sheet at fair value. We enter into interest rate exchange agreements to fix the interest rate on a portion of our variable interest rate debt to reduce the potential volatility in our interest expense that would otherwise result from changes in market interest rates. Our derivative instruments are recorded at fair value and are included in other current assets, other assets and other liabilities of our consolidated balance sheet. Our accounting policies for these instruments are based on whether they meet our criteria for designation as hedging transactions, which include the instrument’s effectiveness, risk reduction and, in most cases, a one-to-one matching of the derivative instrument to our underlying transaction. Gains and losses from changes in fair values of derivatives that are not designated as hedges for accounting purposes are recognized in the consolidated statement of operations. We have no derivative financial instruments designated as hedges. Therefore, changes in fair value for the respective periods were recognized in the consolidated statement of operations.

### *Accounting for Asset Retirement*

We adopted ASC 410 — *Asset Retirement Obligations* (“ASC 410”), on January 1, 2003. ASC 410 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. We reviewed our asset retirement obligations to determine the fair value of such liabilities and if a reasonable estimate of fair value could be made. This entailed the review of leases covering tangible long-lived assets as well as our rights-of-way under franchise agreements. Certain of our franchise agreements and leases contain provisions that require restoration or removal of equipment if the franchises or leases are not renewed. Based on historical experience, we expect to renew our franchise or lease agreements. In the unlikely event that any franchise or lease agreement is not expected to be renewed, we would record an estimated liability. However, in determining the fair value of our asset retirement obligation under our franchise agreements, consideration will be given to the Cable Communications Policy Act of 1984, which generally entitles the cable operator to the “fair market value” for the cable system covered by a franchise, if renewal is denied and the franchising authority acquires ownership of the cable system or effects a transfer of the cable system to another person. Changes in these assumptions based on future information could result in adjustments to estimated liabilities.

Upon adoption of ASC 410, we determined that in certain instances, we are obligated by contractual terms or regulatory requirements to remove facilities or perform other remediation activities upon the retirement of our assets. We initially recorded a \$1.8 million asset in property, plant and equipment and a corresponding liability of \$1.8 million. As of both December 31, 2016 and 2015, the corresponding asset, net of accumulated amortization, was \$0.

## Table of Contents

### *Accounting for Long-Lived Assets*

In accordance with ASC 360 — *Property, Plant and Equipment*, we periodically evaluate the recoverability and estimated lives of our long-lived assets, including property and equipment and intangible assets subject to amortization, whenever events or changes in circumstances indicate that the carrying amount may not be recoverable or the useful life has changed. The measurement for such impairment loss is based on the fair value of the asset, typically based upon the future cash flows discounted at a rate commensurate with the risk involved. Unless presented separately, the loss is included as a component of either depreciation expense or amortization expense, as appropriate.

### *Programming Costs*

We have various fixed-term carriage contracts to obtain programming for our cable systems from content suppliers whose compensation is generally based on a fixed monthly fee per video customer. These programming contracts are subject to negotiated renewal. Programming costs are recognized when we distribute the related programming. These programming costs are usually payable each month based on calculations performed by us and are subject to adjustments based on the results of periodic audits by the content suppliers. Historically, such audit adjustments have been immaterial to our total programming costs. Financial incentives, when received, are deferred within non-current liabilities in our consolidated balance sheets and recognized as a reduction of programming costs (which are a component of service costs in the consolidated statement of operations) over the carriage term of the programming contract.

### *Recent Accounting Pronouncements*

In May 2014, the FASB issued ASU No. 2014-09 (“ASU 2014-09”) – *Revenue from Contracts with Customers*. The guidance states that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity should also disclose sufficient information to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. This guidance supersedes most industry-specific guidance, including Statement of Financial Accounting Standards No. 51 – *Financial Reporting by Cable Television Companies*. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Based on a preliminary assessment of certain revenue transactions performed to date, we expect that the new guidance will impact the timing of the recognition of installation revenue and commission expenses. Under the new guidance, these amounts will be recognized as revenue and expenses, respectively, over a period of time instead of immediately, as is being done under current practice. Installation revenues and commission expenses recorded in 2016 are each less than 2% of total revenues recorded in the same period. We are currently in the process of evaluating which method of transition will be utilized at adoption. We continue to assess all of the potential impacts that the adoption of ASU 2014-09 will have on our consolidated financial statements, including the development of new accounting policies, procedures and internal controls associated with the adoption of the standard.

In August 2014, the FASB issued new guidance that requires management to assess the Company’s ability to continue as a going concern and to provide related disclosures in certain circumstances. This guidance is effective for interim and fiscal years ending after December 15, 2016, with early adoption permitted. This guidance did not have a material impact on our financial position, operations or cash flows.

In April 2015 (as amended in August 2015), the FASB issued ASU No. 2015-03 (and ASU 2015-15) – *Interest—Imputation of Interest (Subtopic 835-30) Simplifying the Presentation of Debt Issuance Costs* (“ASU 2015-03”). The purpose of this guidance is to simplify the presentation of debt issuance costs and requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. For public business entities, the amendments in this update are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. An entity should apply the new guidance on a retrospective basis, wherein the balance sheet of each individual period presented should be adjusted to reflect the period-specific effects of applying the new guidance. We adopted ASU 2015-03 and ASU 2015-15 as of January 1, 2016 and implemented retrospectively as of December 31, 2015. We reclassified \$14.4 million of deferred financing costs from other assets, net to long-term debt, net (less current portion) as of December 31, 2016 in accordance with such guidance. We reclassified \$20.2 million of deferred financing costs from other assets, net to long-term debt, net (less current portion) as of December 31, 2015 in accordance with such guidance. See Note 6.

In April 2015, the FASB issued ASU 2015-05 – *Intangibles—Goodwill and Other—Internal-Use Software* (Subtopic 350-40) (“ASU 2015-05”). The objective of ASU 2015-05 is to address the concerns of stakeholders that the lack of guidance about a customer’s

accounting for fees in a cloud computing arrangement leads to unnecessary cost and complexity when evaluating the accounting for those fees, as well as some diversity in practice. The amendments in ASU 2015-05 will help entities evaluate the accounting for fees

## Table of Contents

paid by a customer in a cloud computing arrangement by providing guidance as to whether an arrangement includes the sale or license of software. Examples of cloud computing arrangements include software as a service, platform as a service, infrastructure as a service, and other similar hosting arrangements. This guidance is effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2015. We adopted this new guidance as of January 1, 2016 and determined that there was not a material impact to our operations.

In February 2016, the FASB issued ASU 2016-02 - *Leases* (Topic 842) ("ASU 2016-02"). The objective of ASU 2016-02 is to address the concerns to increase the transparency around lease obligations. To address these concerns, previously unrecorded off-balance sheet obligations will now be brought more prominently to light by presenting lease liabilities on the face of the balance sheet. Accompanied by enhanced qualitative and quantitative disclosures in the notes to the financial statements, financial statement users will be able to more accurately compare information from one company to another. This guidance is effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2018. We have not completed our evaluation of this new guidance.

In August 2016, the FASB issued ASU 2016-15 - *Statement of Cash Flows* - Clarification of Certain Cash Receipts and Cash Payments. ("ASU 2016-15"). Stakeholders indicated that there is diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows under Topic 230, *Statement of Cash Flows*, and other topics. ASU 2016-15 addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. The amendments in ASU 2016-15 are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. We do not expect ASU 2016-15 will have a material impact on financial position, operations or cash flows upon adoption.

### 3. PROPERTY, PLANT AND EQUIPMENT

As of December 31, 2016 and 2015, property, plant and equipment consisted of (dollars in thousands):

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Cable systems, equipment and customer devices	\$ 2,314,715	\$ 2,250,245
Vehicles	42,334	41,924
Buildings and leasehold improvements	36,708	35,870
Furniture, fixtures and office equipment	34,092	37,128
Land and land improvements	7,841	7,908
Property, plant and equipment, gross	<u>\$ 2,435,690</u>	<u>\$ 2,373,075</u>
Accumulated depreciation	<u>(1,619,301)</u>	<u>(1,589,422)</u>
Property, plant and equipment, net	<u>\$ 816,389</u>	<u>\$ 783,653</u>

Depreciation expense related to fixed assets for the years ended December 31, 2016, 2015 and 2014 was \$147.0 million, \$143.7 million and \$153.5 million, respectively. As of each of December 31, 2016 and 2015, we had no property under capitalized leases. We incurred gross interest costs of \$80.9 million, \$95.7 million and \$101.7 million for the years ended December 31, 2016, 2015 and 2014, respectively, of which \$1.3 million, \$1.0 million and \$1.3 million were capitalized during the years ended December 31, 2016, 2015 and 2014, respectively. See Note 2.

Table of Contents**4. FAIR VALUE**

The tables below set forth our financial assets and liabilities measured at fair value on a recurring basis using a market-based approach. Our financial assets and liabilities, all of which represent interest rate exchange agreements (which we refer to as “interest rate swaps”) have been categorized according to the three-level fair value hierarchy established by ASC 820 – *Fair Value Measurement* – (“ASC 820”), which prioritizes the inputs used in measuring fair value, as follows (dollars in thousands):

- Level 1 — Quoted market prices in active markets for identical assets or liabilities.
- Level 2 — Observable market based inputs or unobservable inputs that are corroborated by market data.
- Level 3 — Unobservable inputs that are not corroborated by market data.

	Fair Value as of December 31, 2016			
	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Interest rate exchange agreements	\$ —	\$1,089	\$ —	\$1,089
<b>Liabilities</b>				
Interest rate exchange agreements	\$ —	\$1,763	\$ —	\$1,763
	Fair Value as of December 31, 2015			
	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Interest rate exchange agreements	\$ —	\$1,818	\$ —	\$1,818
<b>Liabilities</b>				
Interest rate exchange agreements	\$ —	\$3,695	\$ —	\$3,695

The fair value of our interest rate swaps represents the estimated amount that we would receive or pay to terminate such agreements, taking into account projected interest rates, based on quoted London Interbank Offered Rate (“LIBOR”) futures and the remaining time to maturity. While our interest rate swaps are subject to contractual terms that provide for the net settlement of transactions with counterparties, we do not offset assets and liabilities under these agreements for financial statement presentation purposes, and assets and liabilities are reported on a gross basis.

As of December 31, 2016, we recorded a long-term asset of \$1.1 million, a current liability in accounts payable, accrued expenses and other current liabilities of \$1.8 million and no current asset or long-term liability. As of December 31, 2015, we recorded a long-term asset of \$1.8 million, a current liability in accounts payable, accrued expenses and other current liabilities of \$3.7 million and no current asset or long-term liability.

As a result of the changes in the mark-to-market valuations on our interest rate swaps, we recorded net gains on derivatives of \$1.2 million, \$9.2 million and \$23.2 million for the years ended December 31, 2016, 2015 and 2014, respectively.

Table of Contents**5. ACCOUNTS PAYABLE, ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES**

Accounts payable, accrued expenses and other current liabilities consisted of the following as of December 31, 2016 and 2015 (dollars in thousands):

	<u>December 31,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
Accounts payable - trade	\$ 42,094	\$ 36,788
Accrued programming costs	25,856	26,347
Accrued taxes and fees	17,212	16,720
Advance customer payments	13,902	13,274
Accrued payroll and benefits	13,795	13,308
Accrued interest	10,080	12,457
Bank overdrafts (1)	7,387	4,617
Accrued service costs	6,810	7,871
Accrued administrative costs	5,381	3,435
Accrued property, plant and equipment	4,950	8,791
Accrued marketing costs	3,193	2,184
Liabilities under interest rate exchange agreements	1,763	3,695
Accrued telecommunications costs	878	986
Other accrued expenses	1,517	1,456
Accounts payable, accrued expenses and other current liabilities	<u>\$ 154,818</u>	<u>\$ 151,929</u>

- (1) Bank overdrafts represented outstanding checks in excess of funds on deposit at our disbursement accounts. We transfer funds from our depository accounts to our disbursement accounts upon daily notification of checks presented for payment. Changes in bank overdrafts are reported in "other financing activities" in our Consolidated Statement of Cash Flows.

**6. DEBT**

As of December 31, 2016 and 2015, our outstanding debt consisted of (dollars in thousands):

	<u>December 31,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
Bank credit facility	\$ 1,128,000	\$ 1,329,750
5 1/2% senior notes due 2021	200,000	200,000
6 3/8% senior notes due 2023	300,000	300,000
Total debt	\$ 1,628,000	\$ 1,829,750
Less: current portion	16,575	19,075
Total long-term debt, gross (less current portion)	\$ 1,611,425	\$ 1,810,675
Less: deferred financing costs, net	14,350	20,232
Total long-term debt, net (less current portion)	<u>\$ 1,597,075</u>	<u>\$ 1,790,443</u>

***Bank Credit Facility***

As of December 31, 2016, we maintained a \$1.384 billion bank credit facility (the "credit facility"), comprising:

- \$368.5 million of revolving credit commitments, which expire on October 10, 2019;
- \$143.9 million of outstanding borrowings under Term Loan A, which mature on January 15, 2021;
- \$579.0 million of outstanding borrowings under Term Loan H, which mature on January 29, 2021; and
- \$292.5 million of outstanding borrowings under Term Loan J, which mature on June 30, 2021.

## Table of Contents

The credit facility is collateralized by our ownership interests in our operating subsidiaries and is guaranteed by us on a limited recourse basis to the extent of such ownership interests. As of December 31, 2016, we had the ability to repay all outstanding debt under the credit facility at par value any time prior to maturity. As of December 31, 2016, the credit agreement governing the credit facility (the "credit agreement") required our operating subsidiaries to maintain a total leverage ratio (as defined in the credit agreement) of no more than 5.0 to 1.0 and an interest coverage ratio (as defined in the credit agreement) of no less than 2.0 to 1.0. For all periods through December 31, 2016, our operating subsidiaries were in compliance with all covenants under the credit agreement.

### *Revolving Credit Commitments*

On October 10, 2014, we terminated our existing revolving credit commitments and, on the same date, entered into an incremental facility agreement that provided for \$216.0 million of new revolving credit commitments, which are scheduled to expire on October 10, 2019. On December 9, 2014, August 12, 2015 and November 23, 2015, we entered into incremental facility agreements that provided for an additional \$40.0 million, \$25.0 million and \$87.5 million of revolving credit commitments, respectively.

Borrowings under our revolving credit commitments bear interest at a floating rate or rates equal to, at our discretion, LIBOR plus a margin ranging from 2.00% to 2.75%, or the Prime Rate plus a margin ranging from 1.00% to 1.75%. Commitment fees on the unused portion of our revolving credit commitments are payable at a rate of 0.50% or 0.63%. The applicable margin and commitment fees charged are determined by certain financial ratios pursuant to the credit agreement.

As of December 31, 2016, we had \$246.2 million of unused revolving credit commitments, all of which were available to be borrowed and used for general corporate purposes, after giving effect to \$112.6 million of outstanding loans and \$9.7 million of letters of credit issued to various parties as collateral.

### *Term Loan A*

On December 17, 2015, we entered into an incremental facility agreement that provided for a new term loan in the original principal amount of \$151.5 million ("Term Loan A"). Term Loan A matures on January 15, 2021 and, since March 31, 2016, has been subject to quarterly principal payments of \$1.9 million, representing 1.25% of the original principal amount, with a final payment at maturity of \$113.6 million, representing 75.00% of the original principal amount.

Borrowings under Term Loan A bear interest at a floating rate or rates equal to, at our discretion, LIBOR plus a margin ranging from 2.25% to 3.50%, or the Prime Rate plus a margin ranging from 1.25% to 2.50%. The applicable margin and commitment fees charged are determined by certain financial ratios pursuant to the credit agreement.

### *Term Loan H*

On May 29, 2013, we entered into an incremental facility agreement that provided for a new term loan in the original principal amount of \$600.0 million ("Term Loan H"). Term Loan H matures on January 29, 2021 and, since September 30, 2013, has been subject to quarterly principal payments of \$1.5 million, representing 0.25% of the original principal amount, with a final payment at maturity of \$555.0 million, representing 92.5% of the original principal amount.

Borrowings under Term Loan H bear interest at a floating rate or rates equal to, at our discretion, LIBOR plus a margin of 2.50% (subject to a minimum LIBOR of 0.75%), or the Prime Rate plus a margin of 1.50% (subject to a minimum Prime Rate of 1.75%).

### *Term Loan J*

On June 20, 2014, we entered into an amended and restated credit agreement that, among other things, provided for a new term loan in the original principal amount \$300.0 million ("Term Loan J"). Term Loan J matures on June 30, 2021 and, since September 30, 2014, has been subject to quarterly principal payments of \$0.8 million, representing 0.25% of the original principal amount, with a final payment at maturity of \$279.8 million, representing 93.25% of the original principal amount.

Borrowings under Term Loan J bear interest at a floating rate or rates equal to, at our discretion, LIBOR plus a margin of 2.75% or 3.00% (subject to a minimum LIBOR of 0.75%), or the Prime Rate plus a margin of 1.75% or 2.00% (subject to a minimum Prime Rate of 1.75%). The applicable margin charged is determined by certain financial ratios pursuant to the credit agreement.

## Table of Contents

### *Interest Rate Swaps*

We have entered into several interest rate exchange agreements (which we refer to as “interest rate swaps”) with various banks to fix the variable rate on a portion of our borrowings under the credit facility to reduce the potential volatility in our interest expense that may result from changes in market interest rates. Our interest rate swaps have not been designated as hedges for accounting purposes, and have been accounted for on a mark-to-market basis as of, and for the years ended, December 31, 2016, 2015 and 2014. As of December 31, 2016, we had current interest rate swaps that fixed the variable portion of \$600 million of borrowings at a rate of 1.5%, all of which are scheduled to expire during December 2018.

As of December 31, 2016, the weighted average interest rate on outstanding borrowings under the credit facility, including the effect of our interest rate swaps, was 3.5%.

### *Senior Notes*

As of December 31, 2016, we had \$500.0 million of outstanding senior notes, comprising \$200.0 million of 5 ½% senior notes due April 2021 (the “5 ½% Notes”), and \$300.0 million of 6 ¾% senior notes due April 2023 (the “6 ¾% Notes”).

Our senior notes are unsecured obligations and, as of December 31, 2016, the indentures governing our senior notes (the “indentures”) limits the incurrence of additional indebtedness based upon a maximum debt to operating cash flow ratio (as defined in the indentures) of 8.5 to 1.0. For all periods through December 31, 2016, we were in compliance with all of the covenants under the indentures.

#### *5 ½% Notes*

On March 17, 2014, we issued the 5 ½% Notes in the aggregate principal amount of \$200.0 million. Net proceeds from the 5 ½% Notes funded a partial repayment of certain previously existing term loans.

As a percentage of par value, the 5 ½% Notes are redeemable at 102.750% commencing April 15, 2017, 101.375% commencing April 15, 2018 and at par value commencing April 15, 2019.

#### *6 ¾% Notes*

On August 28, 2012, we issued the 6 ¾% Notes in the aggregate principal amount of \$300.0 million. Net proceeds from the 6 ¾% Notes were used to fund, in part, the redemption of certain previously existing senior notes.

As a percentage of par value, the 6 ¾% Notes are redeemable at 103.188% commencing April 1, 2018, 102.125% commencing April 1, 2019, 101.063% commencing April 1, 2020 and at par value commencing April 1, 2021.

### *Loss on Early Extinguishment of Debt*

Loss on early extinguishment of debt totaled \$1.2 million, \$4.4 million and \$0.3 million for the years ended December 31, 2016, 2015 and 2014, respectively, which represented the write-off of unamortized deferred financing costs as a result of the repayment of certain previously existing term loans under the credit facility.

### *Deferred Financing Costs*

We adopted ASU 2015-03 and ASU 2015-15 as of January 1, 2016, and implemented retrospectively as of December 31, 2015. In accordance with such guidance, we reclassified \$14.4 million and \$20.2 million of deferred financing costs from other assets, net to long-term debt, net (less current portion) as of December 31, 2016 and 2015, respectively.

### *Debt Ratings*

MCC’s corporate credit ratings are currently Ba3 by Moody’s, with a positive outlook, and BB by Standard and Poor’s (“S&P”), with a stable outlook, and our senior unsecured ratings are currently B2 by Moody’s, with a positive outlook, and B+ by S&P, with a stable outlook. There are no covenants, events of default, borrowing conditions or other terms in the credit agreement or indentures that are based on changes in our credit rating assigned by any rating agency.



## Table of Contents

### *Fair Value and Debt Maturities*

The fair values of our senior notes and outstanding debt under the credit facility (which were calculated based upon market prices of such issuances in an active market when available) were as follows as of December 31, 2016 and 2015 (dollars in thousands):

	December 31,	
	2016	2015
5 1/2% senior notes due 2021	\$ 205,500	\$ 191,500
6 3/8% senior notes due 2023	316,500	291,750
Total senior notes	<u>\$ 522,000</u>	<u>\$ 483,250</u>
Bank credit facility	<u>\$1,135,633</u>	<u>\$1,317,990</u>

The scheduled maturities of all debt outstanding as of December 31, 2016 are as follows (dollars in thousands):

	Bank Credit Facility		Senior Notes	Total
	Revolving Credit	Term Loans		
January 1, 2017 to December 31, 2017	\$ —	\$ 16,575	\$ —	\$ 16,575
January 1, 2018 to December 31, 2018	—	16,575	—	16,575
January 1, 2019 to December 31, 2019	112,575	16,575	—	129,150
January 1, 2020 to December 31, 2020	—	16,575	—	16,575
January 1, 2021 to December 31, 2021	—	949,125	200,000	1,149,125
Thereafter	—	—	300,000	300,000
Total	<u>\$ 112,575</u>	<u>\$1,015,425</u>	<u>\$500,000</u>	<u>\$1,628,000</u>

## 7. PREFERRED MEMBERS' INTEREST

In July 2001, we received a \$150.0 million preferred membership investment ("PMI") from the operating subsidiaries of Mediacom LLC, which has a 12% annual dividend, payable quarterly in cash. We may voluntarily repay the PMI at any time at par, and the operating subsidiaries of Mediacom LLC have the option to call for the redemption of the PMI upon the repayment of all of our outstanding senior notes. We paid \$18.0 million in cash dividends on the PMI during each of the years ended December 31, 2016, 2015, and 2014.

## 8. MEMBER'S EQUITY

As a wholly-owned subsidiary of MCC, our business affairs, including our financing decisions, are directed by MCC. See Note 9.

Capital contributions from parent and capital distributions to parent are reported on a gross basis in the Consolidated Statements of Changes in Member's Equity and the Consolidated Statements of Cash Flows. We received capital contributions from parent of \$75.0 million for the year ended December 31, 2016, and no capital contributions from parent during each of the years ended December 31, 2015 and 2014. We made capital distributions to parent in cash of \$7.0 million, \$0 and \$163.3 million during the years ended December 31, 2016, 2015 and 2014, respectively.

## 9. RELATED PARTY TRANSACTIONS

### Management Agreements

MCC manages us pursuant to management agreements with our operating subsidiaries. Under such agreements, MCC has full and exclusive authority to manage our day to day operations and conduct our business. We remain responsible for all expenses and liabilities relating to the construction, development, operation, maintenance, repair, and ownership of our systems.

As compensation for the performance of its services, subject to certain restrictions, MCC is entitled under each management agreement to receive management fees in an amount not to exceed 4.0% of the annual gross operating revenues of our operating subsidiaries. MCC is also entitled to the reimbursement of all expenses necessarily incurred in its capacity as manager. MCC charged us management fees of \$20.8 million, \$19.0 million and \$17.7 million during the years ended December 31, 2016, 2015 and 2014, respectively.

Mediacom LLC is a preferred equity investor in us. See Note 7.

## Table of Contents

### **10. EMPLOYEE BENEFIT PLANS**

Substantially all our employees are eligible to participate in MCC's defined contribution plan pursuant to the Internal Revenue Code Section 401(k) ("MCC's Plan"). Under MCC's Plan, eligible employees may contribute a portion of their current pretax compensation (as defined by MCC's Plan). MCC's Plan permits, but does not require, matching contributions and non-matching (profit sharing) contributions to be made by us up to a maximum dollar amount or maximum percentage of participant contributions, as determined annually by us. We presently match 50% on the first 6% of employee contributions. Our contributions under MCC's Plan totaled \$1.2 million, \$1.3 million and \$1.3 million for the years ended December 31, 2016, 2015 and 2014, respectively, which were recorded in service costs and selling, general and administrative expenses.

### **11. COMMITMENTS AND CONTINGENCIES**

#### *Leases*

Under various lease and rental agreements for offices, warehouses and computer terminals, we had rental expense of \$4.1 million, \$4.0 million and \$5.0 million for the years ended December 31, 2016, 2015 and 2014, respectively. Future minimum annual rental payments as of December 31, 2016 are as follows (dollars in thousands):

January 1, 2017 to December 31, 2017	\$2,055
January 1, 2018 to December 31, 2018	1,427
January 1, 2019 to December 31, 2019	1,077
January 1, 2020 to December 31, 2020	805
January 1, 2021 to December 31, 2021	668
Thereafter	<u>1,618</u>
Total	<u>\$7,650</u>

#### *Other Obligations*

In addition, we rent utility poles in our operations generally under short-term arrangements, but we expect these arrangements to recur. Total rental expense for utility poles was approximately \$4.2 million, \$4.3 million and \$4.2 million for the years ended December 31, 2016, 2015 and 2014, respectively.

#### *Letters of Credit*

As of December 31, 2016, \$9.7 million of letters of credit were issued to various parties to secure our performance relating to insurance and franchise requirements. The fair value of such letters of credit was approximately book value.

#### *Legal Proceedings*

We are involved in various legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our consolidated financial position, results of operations, cash flows or business.

## Table of Contents

### **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

### **ITEM 9A. CONTROLS AND PROCEDURES**

#### **Mediacom Broadband LLC**

Under the supervision and with the participation of the management of Mediacom Broadband LLC, including Mediacom Broadband LLC's Chief Executive Officer and Chief Financial Officer, Mediacom Broadband LLC evaluated the effectiveness of its disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based upon such evaluation, Mediacom Broadband LLC's Chief Executive Officer and Chief Financial Officer concluded that Mediacom Broadband LLC's disclosure controls and procedures were effective as of December 31, 2016.

There has not been any change in Mediacom Broadband LLC's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the year ended December 31, 2016 that has materially affected, or is reasonably likely to materially affect, Mediacom Broadband LLC's internal control over financial reporting.

#### ***Management's Report on Internal Control Over Financial Reporting***

Management of Mediacom Broadband LLC is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act as a process designed by, or under the supervision of Mediacom Broadband LLC's principal executive and principal financial officers and effected by Mediacom Broadband LLC's manager, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of Mediacom Broadband LLC;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of Mediacom Broadband LLC are being made only in accordance with authorizations of the management of Mediacom Broadband LLC; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of Mediacom Broadband LLC's assets that could have a material effect on the financial statements.

Because of Mediacom Broadband LLC's inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of Mediacom Broadband LLC's internal control over financial reporting as of December 31, 2016. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control-Integrated Framework* (2013 framework). Based on this assessment, management determined that, as of December 31, 2016, Mediacom Broadband LLC's internal control over financial reporting was effective.

This annual report does not include an attestation report of Mediacom Broadband LLC's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by Mediacom Broadband LLC's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit Mediacom Broadband LLC to provide only management's report in this Annual Report.

#### **Mediacom Broadband Corporation**

Under the supervision and with the participation of the management of Mediacom Broadband Corporation ("Mediacom Broadband"), including Mediacom Broadband's Chief Executive Officer and Chief Financial Officer, Mediacom Broadband evaluated the effectiveness of Mediacom Broadband's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based upon such evaluation, Mediacom

Broadband's Chief Executive Officer and Chief Financial Officer concluded that Mediacom Broadband's disclosure controls and procedures were effective as of December 31, 2016.

## Table of Contents

There has not been any change in Mediacom Broadband's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the year ended December 31, 2016 that has materially affected, or is reasonably likely to materially affect, Mediacom Broadband's internal control over financial reporting.

### *Management's Report on Internal Control Over Financial Reporting*

Management of Mediacom Broadband is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act as a process designed by, or under the supervision of Mediacom Broadband's principal executive and principal financial officers and effected by Mediacom Broadband's board of directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of Mediacom Broadband;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of Mediacom Broadband are being made only in accordance with authorizations of management and directors of Mediacom Broadband; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of Mediacom Broadband's assets that could have a material effect on the financial statements.

Because of Mediacom Broadband's inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of Mediacom Broadband's internal control over financial reporting as of December 31, 2016. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control-Integrated Framework* (2013 framework). Based on this assessment, management determined that, as of December 31, 2016, Mediacom Broadband's internal control over financial reporting was effective.

This annual report does not include an attestation report of Mediacom Broadband's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by Mediacom Broadband's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit Mediacom Broadband to provide only management's report in this annual report.

## **ITEM 9B. OTHER INFORMATION**

None.

Table of Contents**PART III****ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

MCC is our sole voting member and serves as manager of our operating subsidiaries. The Directors and Executive Officers for MCC, Mediacom Broadband LLC ("MBLLC") and Mediacom Broadband Corporation ("MBC") are indicated below:

<u>Name</u>	<u>Age</u>	<u>Position</u>
Rocco B. Commisso	67	Chairman, Chief Executive Officer and Director of MCC and MBC; Chief Executive Officer of MBLLC
Mark E. Stephan	60	Executive Vice President, Chief Financial Officer and Director of MCC; Executive Vice President and Chief Financial Officer of MBLLC and MBC
John G. Pascarelli	55	Executive Vice President, Operations of MCC, MBLLC and MBC
Italia Commisso Weinand	63	Executive Vice President, Programming and Human Resources and Director of MCC; Executive Vice President, Programming and Human Resources of MBLLC
Joseph E. Young	68	Senior Vice President, General Counsel and Secretary of MCC, MBLLC and MBC
Brian M. Walsh	51	Senior Vice President, Corporate Controller of MCC and MBLLC
Tapan Dandnaik	43	Senior Vice President, Customer Service and Financial Operations of MCC
Thomas J. Larsen	44	Senior Vice President, Government and Public Relations of MCC
Peter Lyons	47	Senior Vice President, Information Technology of MCC
David McNaughton	55	Senior Vice President, Marketing and Consumer Services of MCC
Ed Pardini	59	Senior Vice President, Field Operations of MCC
Dan Templin	53	Senior Vice President, Mediacom Business of MCC
JR Walden	45	Senior Vice President, Technology of MCC, CTO

*Rocco B. Commisso* has 38 years of experience with the cable industry, and has served as MCC's Chairman and Chief Executive Officer, and our Chief Executive Officer since founding our predecessor company in July 1995. From 1986 to 1995, he served as Executive Vice President, Chief Financial Officer and a director of Cablevision Industries Corporation. Prior to that time, Mr. Commisso served as Senior Vice President of Royal Bank of Canada's affiliate in the United States from 1981, where he founded and directed a specialized lending group to media and communications companies. Mr. Commisso began his association with the cable industry in 1978 at The Chase Manhattan Bank, where he managed the bank's lending activities to communications firms including the cable industry. Mr. Commisso serves on the board of directors of the National Cable & Telecommunications Association, C-SPAN and Cable Television Laboratories, Inc. He was inducted into the 2007 Broadcasting & Cable Hall of Fame. Mr. Commisso holds a Bachelor of Science in Industrial Engineering and a Master of Business Administration from Columbia University.

*Mark E. Stephan* has 30 years of experience with the cable industry, and has served as MCC's, and our Executive Vice President and Chief Financial Officer since July 2005. Prior to that time, he was Executive Vice President, Chief Financial Officer and Treasurer since November 2003 and MCC's Senior Vice President, Chief Financial Officer and Treasurer since the commencement of MCC's operations in March 1996. Before joining MCC, Mr. Stephan served as Vice President, Finance for Cablevision Industries from July 1993. Prior to that time, Mr. Stephan served as Manager of the telecommunications and media lending group of Royal Bank of Canada. Mr. Stephan has been a director of MCC since May 2011 and was previously a director of MCC from March 2000 to March 2011.

*John G. Pascarelli* has 35 years of experience in the cable industry, and has served as MCC's Executive Vice President, Operations since November 2003. Prior to that time, he was MCC's Senior Vice President, Marketing and Consumer Services from June 2000 and MCC's Vice President of Marketing from March 1998. Before joining MCC, Mr. Pascarelli served as Vice President, Marketing for Helicon Communications Corporation from January 1996 to February 1998 and as Corporate Director of Marketing for Cablevision Industries from 1988 to 1995. Prior to that time, Mr. Pascarelli served in various marketing and system management capacities for Continental Cablevision, Inc., Cablevision Systems and Storer Communications.

*Italia Commisso Weinand* has 40 years of experience in the cable industry, and serves on MCC's board, and is the Executive Vice President of Programming and Human Resources since May 2012. Prior to that time, she was MCC's Senior Vice President of Programming and Human Resources since February 1998 and MCC's Vice President of Operations since April 1996. Before joining MCC, Ms. Weinand served as Regional Manager for Comcast Corporation from July 1985. Prior to that time, Ms. Weinand held various management positions with Time Warner, Inc., Times Mirror Cable and Tele-Communications, Inc. For the past seven years she has been named among the "Most Powerful Women in Cable" by CableFax Magazine and presently serves on the Board of The Cable Center, the Emma Bowen Foundation and CTAM Educational Foundation Board. Ms. Weinand was inducted in 2004 into the

Wonder Women and into the 2014 Broadcasting & Cable Hall of Fame. Ms. Weinand is the sister of Mr. Commisso. Ms. Weinand has been a director of MCC since May 2011.

## Table of Contents

*Joseph E. Young* has 34 years of experience with the cable industry, and has served as Senior Vice President, General Counsel since November 2001. Prior to that time, Mr. Young served as Executive Vice President, Legal and Business Affairs, for LinkShare Corporation, an Internet-based provider of marketing services, from September 1999 to October 2001. Prior to that time, he practiced corporate law with Baker & Botts, LLP from January 1996 to September 1999. Previously, Mr. Young was a partner with the Law Offices of Jerome H. Kern and a partner with Shea & Gould.

*Brian M. Walsh* has 29 years of experience in the cable industry, and has served as MCC's Senior Vice President and Corporate Controller since February 2005. Prior to that time, he was MCC's Senior Vice President, Financial Operations from November 2003, MCC's Vice President, Finance and Assistant to the Chairman from November 2001, MCC's Vice President and Corporate Controller from February 1998 and MCC's Director of Accounting from November 1996. Before joining MCC in April 1996, Mr. Walsh held various management positions with Cablevision Industries from 1988 to 1995.

*Tapan Dandnaik* has 16 years of experience in the cable industry, and has served as MCC's Senior Vice President, Customer Service & Financial Operations since July 2008. In 2013, he also assumed responsibilities for our centralized field support operations. Prior to that time, he was MCC's Group Vice President, Financial Operations since July 2007 and MCC's Vice President, Financial Operations since May 2005. Before joining MCC, Mr. Dandnaik served as Director of Corporate Initiatives, Manager of Corporate Finance and as a Financial Analyst for RCN from July 2000 to April 2005. Prior to that time, Mr. Dandnaik served as a Product Engineer for Ingersoll-Rand in India. Mr. Dandnaik was the recipient of the National Cable & Telecommunication Association's Vanguard Award for Young Leadership in 2012 and serves on The Cable Center Customer Care Committee.

*Thomas J. Larsen* has 16 years of experience in the cable industry, and has served as MCC's Senior Vice President, Government and Public Relations since July 2015. Prior to that time, he was MCC's Group Vice President, Legal and Public Affairs since July 2010 and MCC's Vice President, Legal and Public Affairs since August 2006. Prior to joining MCC, Mr. Larsen worked as Vice President, Law and Public Policy for Adelphia Communications Corporation's Western Region. He serves on the board of directors of the American Cable Association

*Peter Lyons* has 10 years of experience in the cable industry, and has served as MCC's Senior Vice President, Information Technology since July 2015. Prior to that time, he was MCC's Group Vice President, Information Technology from July 2010, MCC's Vice President, Information Technology since March 2007. Before joining MCC in 2007, Mr. Lyons held various senior technology leadership positions at The College Board and Video Update and has 21 years of experience in education and retail businesses.

*David McNaughton* has 29 years of experience in the telecommunications industry, and has served as MCC's Senior Vice President, Marketing and Sales since May 2011. Before joining MCC, Mr. McNaughton served as Chief Marketing Officer for Ntelos Wireless, a Virginia-based regional wireless carrier from 2009 and Senior Vice President and General Manager at Cincinnati Bell from 2007, responsible for wireless, landline and DSL services. Prior to that time, he served as Senior Vice President, Acquisition Marketing at DirecTV, Vice President, Customer Lifecycle and Retention at Nextel Communications, and various executive positions at AirTouch Cellular and Andersen Consulting.

*Ed Pardini* has 34 years of experience in the cable industry, and has served as MCC's Senior Vice President of the Field Operations Group since May 2012. Prior to that time, he was Senior Vice President, Divisional Operations for the North Central Division from April 2006. Before joining MCC, Mr. Pardini served as an operating executive in several markets with Comcast since 1989, concluding his final assignment as a Senior Regional Vice President for Philadelphia and eastern Pennsylvania. Prior to that time, Mr. Pardini served in various financial management positions with Greater Media Cable and Viacom Cable.

*Dan Templin* has 25 years of experience in the cable and broadband industries, and has served as MCC's Senior Vice President, Mediacom Business and President of MCC's CLEC entities since April 2011. His responsibilities for Mediacom Business include SMB and Enterprise network services and also the OnMedia advertising sales unit. Prior to that time, he was MCC's Group Vice President, Strategic Marketing and Product Development since May 2008. Before joining MCC, Mr. Templin served in a number of senior operations, product and marketing roles with Susquehanna Communications, Comcast and Jones Intercable.

*JR Walden* has 21 years of experience in the cable industry, and 23 years of experience in Internet and Telecommunications technology. He has served as MCC's Senior Vice President, Technology since February 2008. Prior to that time, he was MCC's Group Vice President, IP Services from July 2004, MCC's Vice President, IP Services from July 2003, MCC's Senior Director of IP Services from June 2002 and MCC's IP Services Director from October 1998. Before joining MCC in 1998, Mr. Walden worked in the defense research industry holding various positions with the Department of Defense, Comarco and Science Applications International Corporation.



## Table of Contents

Our manager has adopted a code of ethics applicable to all of our employees, including our chief executive officer, chief financial officer and chief accounting officer. This code of ethics was filed as an exhibit to our Annual Report on Form 10-K for the year ended December 31, 2003.

### **ITEM 11. EXECUTIVE COMPENSATION**

The executive officers and directors of MCC are compensated exclusively by MCC and do not receive any separate compensation from Mediacom Broadband LLC or Mediacom Broadband Corporation. MCC acts as manager of our operating subsidiaries and in return receives management fees from each of such subsidiaries.

### **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Mediacom Broadband Corporation is a wholly-owned subsidiary of Mediacom Broadband LLC. MCC is the sole voting member of Mediacom Broadband. The address of MCC is 1 Mediacom Way, Mediacom Park, New York 10918.

### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

#### **Management Agreements**

Pursuant to management agreements between MCC and our operating subsidiaries, MCC is entitled to receive annual management fees in amounts not to exceed 4.0% of gross operating revenues, and MCC shall be responsible for, among other things, the compensation (including benefits) of MCC's executive management. For the year ended December 31, 2016, MCC charged us \$20.8 million of such management fees, approximately 2.0% of gross operating revenues.

#### **Other Relationships**

In July 2001, we received a \$150 million preferred membership interest from Mediacom LLC, a wholly owned subsidiary of MCC. The preferred membership interest has a 12% annual dividend, payable quarterly in cash. For the year ended December 31, 2016, we paid an aggregate of \$18 million in cash dividends on the preferred membership interest.

### **ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

Our allocated portion of fees from MCC for professional services provided by our independent auditor in each of the last two fiscal years, in each of the following categories are as follows (dollars in thousands):

	<u>Year Ended</u> <u>December 31,</u>	
	<u>2016</u>	<u>2015</u>
Audit fees	\$400	\$400
Audit-related fees	—	4
Tax fees	—	—
All other fees	<u>1</u>	<u>1</u>
Total	<u>\$401</u>	<u>\$405</u>

Audit fees include fees associated with the annual audit, the reviews of our quarterly reports on Form 10-Q and annual reports on Form 10-K. Audit-related fees include fees associated with the audit of an employee benefit plan and transaction reviews.

Table of Contents**PART IV****ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES****(a) Financial Statements**

Our financial statements as set forth in the Index to Consolidated Financial Statements under Part II, Item 8 of this Form 10-K are hereby incorporated by reference.

**(b) Exhibits**

The following exhibits, which are numbered in accordance with Item 601 of Regulation S-K, are filed herewith or, as noted, incorporated by reference herein:

<u>Exhibit Number</u>	<u>Exhibit Description</u>
3.1	Certificate of Formation of Mediacom Broadband LLC(1)
3.2	Amended and Restated Limited Liability Company Operating Agreement of Mediacom Broadband LLC(1)
3.3	Certificate of Incorporation of Mediacom Broadband Corporation(1)
3.4	By-Laws of Mediacom Broadband Corporation(1)
4.1	Indenture relating to 6 3/8% senior notes due 2023 of Mediacom Broadband LLC and Mediacom Broadband Corporation(2)
4.2	Indenture relating to 5 1/2% senior notes due 2023 of Mediacom Broadband LLC and Mediacom Broadband Corporation(3)
10.1	Incremental Facility Agreement, dated as of December 17, 2015, among Mediacom Communications Corporation, Mediacom Broadband LLC, the operating subsidiaries of Mediacom Broadband LLC, the lenders party thereto and JPMorgan Chase Bank, N.A., as administrative agent for the lenders(4)
10.2	Incremental Facility Agreement, dated as of November 23, 2015, among Mediacom Communications Corporation, Mediacom Broadband LLC, the operating subsidiaries of Mediacom Broadband LLC, the lenders party thereto and JPMorgan Chase Bank, N.A., as administrative agent for the lenders(4)
10.3	Incremental Facility Agreement, dated as of August 12, 2015, among Mediacom Communications Corporation, Mediacom Broadband LLC, the operating subsidiaries of Mediacom Broadband LLC, the lenders party thereto and JPMorgan Chase Bank, N.A., as administrative agent for the lenders(5)
10.4	Incremental Facility Agreement, dated as of December 9, 2014, among Mediacom Communications Corporation, Mediacom Broadband LLC, the operating subsidiaries of Mediacom Broadband LLC, the lenders party thereto and JPMorgan Chase Bank, N.A., as administrative agent for the lenders(6)
10.5	Incremental Facility Agreement, dated as of October 10, 2014, among Mediacom Communications Corporation, Mediacom Broadband LLC, the operating subsidiaries of Mediacom Broadband LLC, the lenders party thereto and JPMorgan Chase Bank, N.A., as administrative agent for the lenders(6)
10.6	Third Restatement Agreement to Credit Agreement, dated as of June 20, 2014, among Mediacom Communications Corporation, Mediacom Broadband LLC, the operating subsidiaries of Mediacom Broadband LLC, the lenders party thereto and JPMorgan Chase Bank, N.A., as administrative agent for the lenders(7)
10.7	Third Amended and Restated Credit Agreement, dated as of June 20, 2014, among the operating subsidiaries of Mediacom Broadband LLC, the lenders party thereto and JPMorgan Chase Bank, N.A., as administrative agent for the lenders(8)
12.1	Schedule of Computation of Ratio of Earnings to Fixed Charges and Preferred Dividends
14.1	Code of Ethics(8)
21.1	Subsidiaries of Mediacom Broadband LLC

**ITEM 16. SUMMARY**

None.



Table of Contents

<u>Exhibit Number</u>	<u>Exhibit Description</u>
31.1	Rule 15d-14(a) Certifications of Mediacom Broadband LLC
31.2	Rule 15d-14(a) Certifications of Mediacom Broadband Corporation
32.1	Section 1350 Certifications of Mediacom Broadband LLC
32.2	Section 1350 Certifications of Mediacom Broadband Corporation
101	The following is financial information from Mediacom Broadband LLC's and Mediacom Broadband Corporation's Annual Report on Form 10-K for the year ended December 31, 2015, formatted in eXtensible Business Reporting Language (XBRL): (i) Consolidated Balance Sheets as of December 31, 2015 and 2014; (ii) Consolidated Statements of Operations for the years ended December 31, 2015, 2014 and 2013; (iii) Consolidated Statements of Changes in Member's Deficit for the years ended December 31, 2015, 2014 and 2013; (iv) Consolidated Statements of Cash Flows for the years ended December 31, 2015, 2014 and 2013; and (v) Notes to Consolidated Financial Statements

- (1) Filed as an exhibit to the Registration Statement on Form S-4 (File No. 333-72440) of Mediacom Broadband LLC and Mediacom Broadband Corporation and incorporated herein by reference.
- (2) Filed as an exhibit to the Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2012 of Mediacom Broadband LLC and incorporated herein by reference.
- (3) Filed as an exhibit to the Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2014 of Mediacom Broadband LLC and incorporated herein by reference.
- (4) Filed as an exhibit to the Annual Report on Form 10-K for the fiscal year ended December 31, 2015 of Mediacom Broadband LLC and incorporated herein by reference.
- (5) Filed as an exhibit to the Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2015 of Mediacom Broadband LLC and incorporated herein by reference.
- (6) Filed as an exhibit to the Annual Report on Form 10-K for the fiscal year ended December 31, 2014 of Mediacom Broadband LLC and incorporated herein by reference.
- (7) Filed as an exhibit to the Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2014 of Mediacom Broadband LLC and incorporated herein by reference.
- (8) Filed as Exhibit A to Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2014 of Mediacom Broadband LLC and incorporated herein by reference.
- (9) Filed as an exhibit to the Annual Report on Form 10-K for the fiscal year ended December 31, 2003 of Mediacom Broadband LLC and incorporated herein by reference.

*(c) Financial Statement Schedule*

The following financial statement schedule — Schedule II — Valuation of Qualifying Accounts — is part of this Form 10-K.

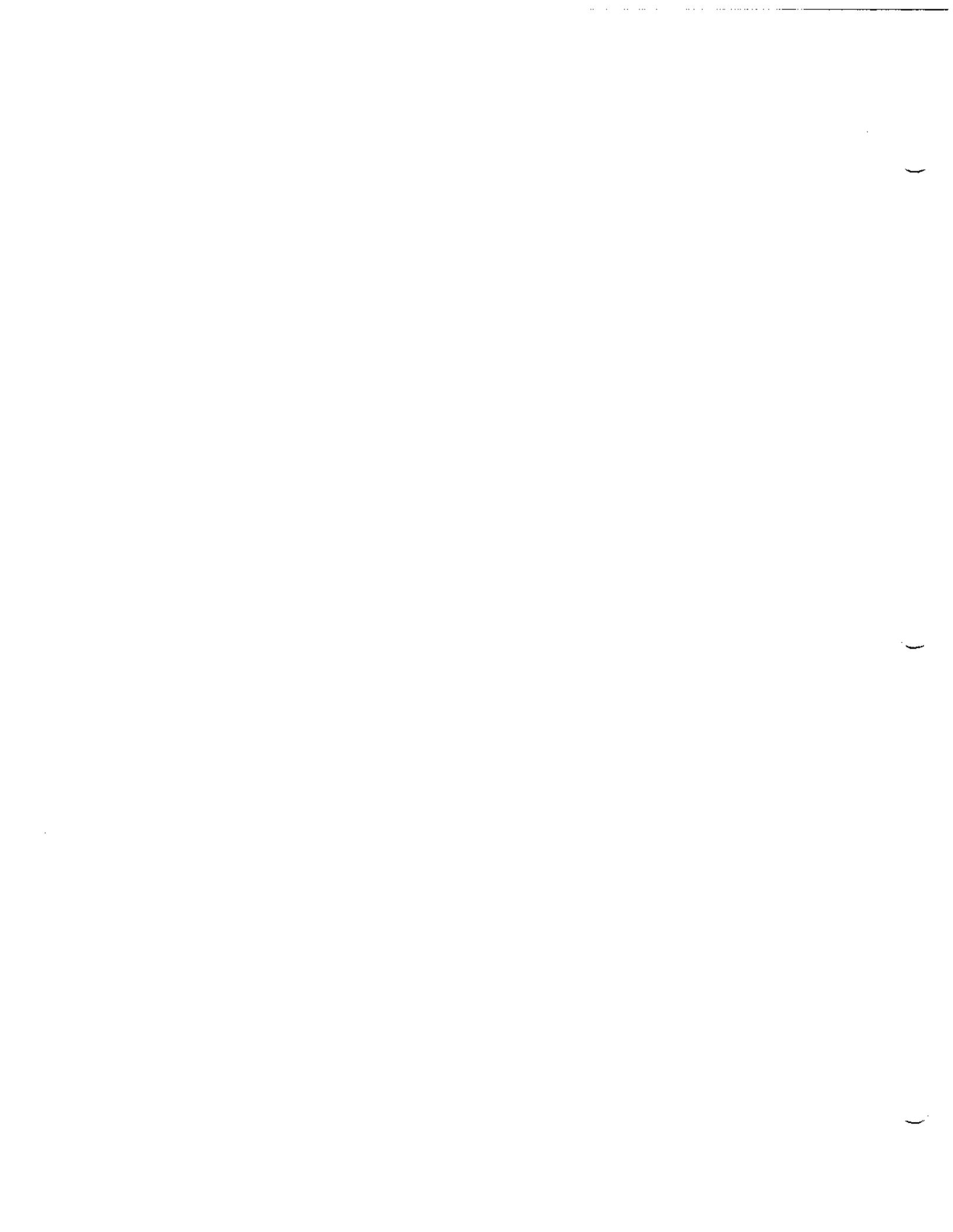
Table of Contents**Schedule II****MEDIACOM BROADBAND LLC AND SUBSIDIARIES****VALUATION AND QUALIFYING ACCOUNTS**

	<u>Balance at beginning of period</u>	<u>Additions - Charged to costs and expenses</u>	<u>Additions - Charged to other accounts</u>	<u>Deductions</u>	<u>Balance at end of period</u>
<b>December 31, 2014</b>					
Allowance for doubtful accounts:					
Current receivables	\$ 2,920	\$ 3,269	\$ —	\$ 3,132	\$ 3,057
<b>December 31, 2015</b>					
Allowance for doubtful accounts:					
Current receivables	\$ 3,057	\$ 10,046	\$ —	\$ 9,476	\$ 3,627
<b>December 31, 2016</b>					
Allowance for doubtful accounts:					
Current receivables	\$ 3,627	\$ 5,896	\$ —	\$ 5,666	\$ 3,857

71







10-K 1 sprintcorp201610-k.htm FORM 10-K

[Table of Contents](#)

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-K**

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

For the fiscal year ended March 31, 2017  
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 1-04721

**SPRINT CORPORATION**

*(Exact name of registrant as specified in its charter)*

Delaware  
*(State or other jurisdiction of incorporation or organization)*

46-1170005

*(I.R.S. Employer Identification No.)*

6200 Sprint Parkway, Overland Park, Kansas  
*(Address of principal executive offices)*

66251

*(Zip Code)*

Registrant's telephone number, including area code: (855) 848-3280

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common stock, \$0.01 par value	New York Stock Exchange

**Securities registered pursuant to Section 12(g) of the Act: None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendments to this Form 10-K.

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

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer (Do not check if smaller reporting company)	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.) Yes  No

Aggregate market value of voting and non-voting common stock equity held by non-affiliates of Sprint Corporation at September 30, 2016 was \$4,024,031,142

COMMON STOCK OUTSTANDING AT MAY 22, 2017: 3,990,960,531 shares

**DOCUMENTS INCORPORATED BY REFERENCE**

Part III of this Annual Report on Form 10-K incorporates by reference certain information from the registrant's definitive proxy statement with respect to the 2017 annual meeting of stockholders



Table of Contents

**SPRINT CORPORATION**  
**TABLE OF CONTENTS**

<b>Item</b>	<b>PART I</b>	<u>Page Reference</u>
1.	<u>Business</u>	<u>1</u>
1A.	<u>Risk Factors</u>	<u>12</u>
1B.	<u>Unresolved Staff Comments</u>	<u>20</u>
2.	<u>Properties</u>	<u>20</u>
3.	<u>Legal Proceedings</u>	<u>21</u>
4.	<u>Mine Safety Disclosures</u>	<u>21</u>
<b>PART II</b>		
5.	<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>22</u>
6.	<u>Selected Financial Data</u>	<u>24</u>
7.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>25</u>
7A.	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	<u>54</u>
8.	<u>Financial Statements and Supplementary Data</u>	<u>54</u>
9.	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>54</u>
9A.	<u>Controls and Procedures</u>	<u>54</u>
9B.	<u>Other Information</u>	<u>55</u>
<b>PART III</b>		
10.	<u>Directors, Executive Officers and Corporate Governance</u>	<u>56</u>
11.	<u>Executive Compensation</u>	<u>56</u>
12.	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>56</u>
13.	<u>Certain Relationships and Related Transactions, and Director Independence</u>	<u>57</u>
14.	<u>Principal Accounting Fees and Services</u>	<u>57</u>
<b>PART IV</b>		
15.	<u>Exhibits and Financial Statement Schedules</u>	<u>58</u>
16.	<u>Form 10-K Summary</u>	<u>58</u>

Table of Contents

**SPRINT CORPORATION**  
**SECURITIES AND EXCHANGE COMMISSION**  
**ANNUAL REPORT ON FORM 10-K**  
**PART I**

**Item 1. Business**  
**FORMATION**

Sprint Corporation, incorporated in 2012 under the laws of Delaware, is a holding company, with operations conducted by its subsidiaries. Our common stock trades on the New York Stock Exchange (NYSE) under the symbol "S."

On July 10, 2013, SoftBank Corp., which subsequently changed its name to SoftBank Group Corp., and certain of its wholly-owned subsidiaries (together, "SoftBank") completed the merger (SoftBank Merger) with Sprint Nextel Corporation (Sprint Nextel) as contemplated by the Agreement and Plan of Merger, dated as of October 15, 2012 (as amended, the Merger Agreement) and the Bond Purchase Agreement, dated as of October 15, 2012 (as amended, the Bond Agreement). As a result of the SoftBank Merger, Starburst II, Inc. (Starburst II) became the parent company of Sprint Nextel. Immediately thereafter, Starburst II changed its name to Sprint Corporation and Sprint Nextel changed its name to Sprint Communications, Inc. (Sprint Communications). As a result of the completion of the SoftBank Merger in which SoftBank acquired an approximate 78% interest in Sprint Corporation, and subsequent open market stock purchases, SoftBank owned approximately 83% of the outstanding common stock of Sprint Corporation as of March 31, 2017.

**OVERVIEW**

Sprint Corporation and its subsidiaries is a communications company offering a comprehensive range of wireless and wireline communications products and services that are designed to meet the needs of consumers, businesses, government subscribers and resellers. Unless the context otherwise requires, references to "Sprint," "we," "us," "our" and the "Company" mean Sprint Corporation and its consolidated subsidiaries for all periods presented and references to "Sprint Communications" are to Sprint Communications, Inc. and its consolidated subsidiaries. We are a large wireless communications company in the United States, as well as a provider of wireline services. Our services are provided through our ownership of extensive wireless networks, an all-digital global wireline network and a Tier 1 Internet backbone.

We offer wireless and wireline services to subscribers in all 50 states, Puerto Rico, and the U.S. Virgin Islands under the Sprint corporate brand, which includes our retail brands of Sprint®, Boost Mobile®, Virgin Mobile®, and Assurance Wireless® on our wireless networks utilizing various technologies including third generation (3G) code division multiple access (CDMA), and fourth generation (4G) services utilizing Long Term Evolution (LTE). We utilize these networks to offer our wireless subscribers differentiated products and services through the use of a single network or a combination of these networks.

**Our Business Segments**

We operate two reportable segments: Wireless and Wireline. For additional information regarding our segments, see "Part II, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and also refer to the Notes to the Consolidated Financial Statements.

*Wireless*

We offer wireless services on a postpaid and prepaid payment basis to retail subscribers and also on a wholesale basis, which represents the sale of wireless services that utilize the Sprint network but are sold under the wholesaler's brand.

*Postpaid*

In our postpaid portfolio, we offer several price plans for both consumer and business subscribers. Many of our price plans include unlimited talk, text and data or allow subscribers to purchase monthly data allowances. We also offer family plans that include multiple lines of service under one account. We currently offer these plans with subsidy, installment billing or leasing programs. The subsidy program requires a service contract and allows for a subscriber to purchase a handset at a discount for a new line of service. Our installment billing program does not require a service contract and offers service plans at lower monthly rates compared to subsidy plans, but requires the subscriber to pay full or near full price for the handset over monthly installments. Our leasing program also does not require a service contract, provides for service plans at lower monthly rates compared to subsidy plans and allows qualified subscribers to lease a device and make payments for use of the

Table of Contents

device over the term of the lease. At the end of the lease term, the subscriber can either turn in the device, continue leasing the device or purchase the device. The terms of our installment billing and lease contracts require that customers maintain service otherwise the balance of the note is due or they are in default under their lease respectively. See "Item 1A. Risk Factors—Subscribers who purchase a device on a financing basis are no longer required to sign a fixed-term service contract, which could result in higher churn, and higher bad debt expense" and "—Because we lease devices to subscribers, our device leasing program exposes us to risks, including those related to the actual residual value realized on returned devices, higher churn and increased losses on devices."

*Prepaid*

Our prepaid portfolio currently includes multiple brands, each designed to appeal to specific subscriber uses and demographics. Sprint prepaid primarily serves as a complementary offer to our Sprint postpaid offer for those subscribers who want plans that are affordable, simple and flexible without a long-term commitment. Boost Mobile primarily serves subscribers that are looking for value without data limits. Virgin Mobile primarily serves subscribers that are looking to optimize spend but need solutions that offer control, flexibility and connectivity through various plans with high speed data options. Virgin Mobile is also designated as a Lifeline-only Eligible Telecommunications Carrier in certain states and provides service for the Lifeline program under our Assurance Wireless brand. Assurance Wireless provides eligible subscribers who meet income requirements or are receiving government assistance with a free wireless phone, 350 free local and long distance voice minutes each month and unlimited free texts under the Lifeline Program. The Lifeline Program requires applicants to meet certain eligibility requirements and existing subscribers must recertify as to those requirements annually.

*Wholesale*

We have focused our wholesale business on enabling our diverse network of customers to successfully grow their business by providing them with an array of network, product and device solutions. This allows our customers to customize this full suite of value-added solutions to meet the growing demands of their businesses. As part of these growing demands, some of our wholesale mobile virtual network operators (MVNO) are also selling prepaid services under the Lifeline program.

We continue to support the open development of applications, content, and devices on the Sprint platform. In addition, we enable a variety of business and consumer third-party relationships through our portfolio of machine-to-machine solutions, which we offer on a retail postpaid and wholesale basis. Our machine-to-machine solutions portfolio provides a secure, real-time and reliable wireless two-way data connection across a broad range of connected devices.

**Services and Products***Data & Voice Services*

Wireless data communications services are provided throughout the U.S. and include mobile productivity applications, such as Internet access, messaging and email services; wireless photo and video offerings; location-based capabilities, including asset and fleet management, dispatch services and navigation tools; and mobile entertainment applications, including the ability to listen to satellite radio, download and listen to music, and play games. Wireless voice communications services provided throughout the U.S. include basic local and long-distance wireless voice services, as well as voicemail, call waiting, three-way calling, caller identification, directory assistance and call forwarding. We also provide voice and data services in numerous countries outside of the U.S. through roaming arrangements. We offer customized design, development, implementation and support for wireless services provided to large companies and government agencies.

*Products*

Our services are provided using a broad array of devices, applications and services that run on these devices to meet the growing needs of subscriber mobility. Our device portfolio includes many cutting edge handsets from various original equipment manufacturers as well as hotspots, which allow the connection of multiple Wi-Fi enabled devices to the Sprint platform and embedded tablets and laptop devices. Prior to commencing our installment billing and leasing programs, we historically sold devices at prices below our cost in response to competition to attract new subscribers and as retention inducements for existing subscribers. Subscribers also have the option to purchase eligible devices through our installment billing program, or to lease eligible devices through our leasing program. In addition, we sell accessories, such as carrying cases, hands-free devices and other items to subscribers, and we sell devices and accessories to agents and other third-party distributors for resale.

Table of Contents**Wireless Network Technologies**

We deliver wireless services to subscribers primarily through our Sprint platform network. Our Sprint platform uses primarily 3G CDMA and 4G LTE wireless technologies. Our 3G CDMA wireless technology uses a digital spread-spectrum technique that allows a large number of users to access the band by assigning a code to all voice and data bits, sending a scrambled transmission of the encoded bits over the air and reassembling the voice and data into its original format. Our 4G LTE wireless data communications technology utilizes an all-internet protocol (IP) network to deliver high-speed data communications. We provide nationwide service through a combination of operating our own network in both major and smaller U.S. metropolitan areas and rural connecting routes, affiliations under commercial arrangements with third-party affiliates and roaming on other providers' networks.

**Sales, Marketing and Customer Care**

We focus the marketing and sales of wireless services on targeted groups of retail subscribers: individual consumers, businesses and government.

We use a variety of sales channels to attract new subscribers of wireless services, including:

- direct sales representatives whose efforts are focused on marketing and selling wireless services;
- retail outlets, owned and operated by us, that focus on sales to the small business and consumer markets;
- indirect sales agents and third-party retailers that primarily consist of local and national non-affiliated dealers and independent contractors that market and sell services to businesses and the consumer market, and are generally paid through commissions; and
- subscriber-convenient channels, including Internet sales and telesales.

We market our postpaid services under the Sprint brand. We market our prepaid services under the Sprint, Boost Mobile, Virgin Mobile, and Assurance Wireless brands as a means to provide value-driven prepaid service plans. Our wholesale customers are resellers of our wireless services rather than end-use subscribers and market their products and services using their own brands.

Although we market our services using traditional print, digital and television advertising, we also provide exposure to our brand names and wireless services through various sponsorships. The goal of these marketing initiatives is to increase brand awareness and sales.

Our customer care organization works to improve our subscribers' experience, with the goal of retaining subscribers of our wireless services and growing their long-term relationships with Sprint. Customer service call centers receive and resolve inquiries from subscribers and proactively address subscriber needs.

**Competition**

We believe that the market for wireless services has been and will continue to be characterized by competition on the basis of price, the types of services and devices offered and quality of service. We compete with a number of wireless carriers, including three other national wireless companies: AT&T, Verizon Wireless and T-Mobile. Our prepaid services compete with a number of carriers and resellers, which offers competitively-priced calling plans that include unlimited local calling. AT&T, T-Mobile and Verizon Wireless offer competitive prepaid services and wholesale services to resellers. Competition may intensify as a result of mergers and acquisitions, as new firms enter the market, and as a result of the introduction of other technologies, the availability of additional commercial spectrum bands, such as the 600 megahertz (MHz) band, the AWS-3 band and the AWS-4 band, and the potential introduction of new services using unlicensed spectrum. Wholesale services and products also contribute to increased competition. In some instances, resellers that use our network and offer similar services compete against our offerings. The wireless industry also faces competition from other communications, cable and technology companies seeking to increase their brand recognition and capture customer revenue with respect to the provision of wireless products and services, in addition to non-traditional offerings in mobile data. For example, Comcast and Charter recently announced a cooperation agreement with respect to their wireless businesses, and Microsoft, Google, Apple and others are offering alternative means for making wireless voice calls that, in certain cases, can be used in lieu of the wireless provider's voice or text services, as well as alternative means of accessing video content.

Most markets in which we operate have high rates of penetration for wireless services, thereby limiting the growth of subscribers of wireless services. In addition to attracting new subscribers, particularly in less saturated growth markets such as those with non-traditional data demands, it has become increasingly important to retain existing subscribers as the wireless market has matured. Wireless carriers also try to appeal to subscribers by offering certain devices at prices lower than their acquisition cost, which we refer to as our traditional subsidy program. We may offer higher cost devices at greater discounts than our competitors, with the expectation that the loss incurred on the cost of the device will be offset by future service

## Table of Contents

revenue. Wireless carriers now also offer plans that allow subscribers to purchase a device at or near full retail price or lease a device in exchange for lower monthly service fees, early upgrade options, or both. AT&T, Verizon Wireless and T-Mobile also offer programs that include an option to purchase a device using an installment billing program. Our installment billing and device leasing programs do not require a service contract, provide for service plans at lower monthly rates compared to the traditional subsidy program and allow qualified subscribers to either purchase a device by paying monthly installments generally over 24 months or lease a device and make payments for the use of the device over the term of the lease. At the end of the lease term, the subscriber has the option to turn in their device, continue leasing their device, or purchase the device. See "Item 1A. Risk Factors—If we are not able to retain and attract profitable wireless subscribers, our financial performance will be impaired" and "—Because we lease devices to subscribers, our device leasing program exposes us to risks including those related to the actual residual value realized on returned devices, higher churn and increased losses on devices" and "—Subscribers who purchase a device on a financing basis are not required to sign a fixed-term service contract, which could result in higher churn, and higher bad debt expense."

### *Wireline*

We provide a broad suite of wireline voice and data communication services to other communications companies and targeted business subscribers. In addition, our Wireline segment provides voice, data and IP communication services to our Wireless segment. We provide long distance services and operate all-digital global long distance and Tier 1 IP networks.

#### **Services and Products**

Our services and products include domestic and international data communications using various protocols such as multiprotocol label switching technologies (MPLS), IP, managed network services, Voice over Internet Protocol (VoIP), Session Initiated Protocol (SIP) and traditional voice services. Our IP services can also be combined with wireless services. Such services include our Sprint Mobile Integration service, which enables a wireless handset to operate as part of a subscriber's wireline voice network, and our DataLink<sup>SM</sup> service, which uses our wireless networks to connect a subscriber location into their primarily wireline wide-area IP/MPLS data network, making it easier for businesses to adapt their network to changing business requirements. In addition to providing services to our business customers, the wireline network is carrying increasing amounts of voice and data traffic for our Wireless segment as a result of growing usage by our wireless subscribers.

We continue to assess the portfolio of services provided by our Wireline business and are focusing our efforts on IP-based data services and de-emphasizing stand-alone voice services and non-IP-based data services. However, we continue to provide stand-alone voice services primarily to business subscribers. Our Wireline segment markets and sells its services primarily through direct sales representatives.

#### **Competition**

Our Wireline segment competes with AT&T, Verizon Communications, CenturyLink, other major local incumbent operating companies and cable operators, as well as a host of smaller competitors in the provision of wireline services. Over the past few years, our voice services have experienced an industry-wide trend of lower revenue from lower prices and increased competition from other wireline and wireless communications companies, as well as cable multiple system operators, Internet service providers, and other general contracting IT companies.

Some competitors are targeting the high-end data market and are offering deeply discounted rates in exchange for high-volume traffic as they attempt to utilize excess capacity in their networks. In addition, we face increasing competition from other wireless and IP-based service providers. Many carriers, including cable companies, are competing in the residential and small business markets by offering bundled packages of both voice and data services. Competition in wireline services is based on price and pricing plans, the types of services offered, customer service and communications quality, reliability and availability. Our ability to compete successfully will depend on our ability to anticipate and respond to various competitive factors affecting the industry, including new services that may be introduced, changes in consumer preferences, demographic trends, economic conditions and pricing strategies. See "Item 1A. Risk Factors—Competition, industry consolidation, and technological changes in the market for wireless services could negatively affect our operations, resulting in adverse effects on our revenues, cash flows, growth, and profitability."

### **Legislative and Regulatory Developments**

#### *Overview*

Communications services are subject to regulation at the federal level by the Federal Communications Commission (FCC) and in certain states by public utilities commissions (PUCs). Since the SoftBank Merger, we have been subject to regulatory conditions imposed by the Committee on Foreign Investment in the United States (CFIUS) pursuant to a National

## Table of Contents

Security Agreement (NSA) among SoftBank, Sprint, the Department of Justice, the Department of Homeland Security and the Department of Defense (the latter three collectively, the USG Parties). Other federal agencies, such as the Federal Trade Commission (FTC) and Consumer Financial Protection Bureau (CFPB), have also asserted jurisdiction over our business.

The following is a summary of the regulatory environment in which we operate and does not describe all present and proposed federal, state and local legislation and regulations affecting the communications industry. Some legislation and regulations are the subject of judicial proceedings, legislative hearings and administrative proceedings that could change the way our industry operates. We cannot predict the outcome of any of these matters or their potential impact on our business. See "Item 1A. Risk Factors—Government regulation could adversely affect our prospects and results of operations; the federal and state regulatory commissions may adopt new regulations or take other actions that could adversely affect our business prospects, future growth or results of operations."

### ***Regulation and Wireless Operations***

The FCC regulates the licensing, construction, operation, acquisition and sale of our wireless operations and wireless spectrum holdings. FCC requirements impose operating and other restrictions on our wireless operations that increase our costs. The FCC does not currently regulate rates for services offered by commercial mobile radio service (CMRS) providers, and states are legally preempted from regulating such rates and entry into any market, although states may regulate other terms and conditions. The Communications Act of 1934 (Communications Act) and FCC rules also require the FCC's prior approval of the assignment or transfer of control of an FCC license, although the FCC's rules permit spectrum lease arrangements for a range of wireless radio service licenses, including our licenses, with FCC oversight. Approval from the FTC and the Department of Justice, as well as state or local regulatory authorities, also may be required if we sell or acquire spectrum interests. The FCC sets rules, regulations and policies to, among other things:

- grant and renew licenses in the 800 MHz, 1.9 gigahertz (GHz) and 2.5 GHz bands;
- rule on assignments and transfers of control of FCC licenses, and leases covering our use of FCC licenses held by other persons and organizations;
- govern the interconnection of our networks with other wireless and wireline carriers;
- establish access and universal service funding provisions;
- impose rules related to unauthorized use of and access to subscriber information;
- impose fines and forfeitures for violations of FCC rules;
- regulate the technical standards governing wireless services; and
- impose other obligations that it determines to be in the public interest.

We hold 800 MHz, 1.9 GHz and 2.5 GHz FCC licenses authorizing the use of radio frequency spectrum to deploy our wireless services. We also hold FCC point-to-point microwave licenses that enable us to provide backhaul for our wireless network.

#### **800 MHz License Conditions**

Spectrum in our 800 MHz band originally was licensed in small groups of channels, therefore, we hold thousands of these licenses, which together allow us to provide coverage across much of the continental U.S. Our 800 MHz licenses are subject to requirements that we meet population coverage benchmarks tied to the initial license grant dates. To date, we have met all of the construction requirements applicable to these licenses, except in the case of licenses that are not material to our business. Our 800 MHz licenses have ten-year terms, at the end of which each license is subject to renewal requirements that are similar to those for our 1.9 GHz licenses described below.

#### **1.9 GHz PCS License Conditions**

All PCS licenses are granted for ten-year terms. For purposes of issuing PCS licenses, the FCC utilizes major trading areas (MTAs) and basic trading areas (BTAs) with several BTAs making up each MTA. Each license is subject to build-out requirements, which we have met in all of our MTA and BTA markets.

If applicable build-out conditions are met, these licenses may be renewed for additional ten-year terms. Renewal applications are not subject to auctions. If a renewal application is challenged, the FCC grants a preference commonly referred to as a license renewal expectancy to the applicant if the applicant can demonstrate that it has provided "substantial service" during the past license term and has substantially complied with applicable FCC rules and policies and the Communications Act.

Table of Contents**2.5 GHz License Conditions**

We hold licenses for or lease spectrum located within the 2496 to 2690 MHz band, commonly referred to as the 2.5 GHz band, which is designated for the Broadband Radio Service (BRS) and the Educational Broadband Service (EBS). Most BRS and EBS licenses are allocated to specific, relatively small geographic service areas. Other BRS licenses provide for one of 493 separate BTAs. Under current FCC rules, we can access BRS spectrum either through outright ownership of a BRS license issued by the FCC or through a leasing arrangement with a BRS license holder. The FCC rules generally limit eligibility to hold EBS licenses to accredited educational institutions and certain governmental, religious and nonprofit entities, but permit those license holders to lease up to 95% of their capacity for non-educational purposes. Therefore, we primarily access EBS spectrum through long-term leasing arrangements with EBS license holders. Our EBS spectrum leases typically have an initial term equal to the remaining term of the EBS license, with an option to renew the lease for additional terms, for a total lease term of up to 30 years. Our leases are generally transferable, assuming we obtain required governmental approvals. Achieving optimal broadband network speeds, capacity and coverage using 2.5 GHz spectrum relies in significant part on operationalizing a complex mixture of BRS and EBS spectrum licenses and leases in the desired service areas, which is subject to the EBS licensing limitations described above and the technical limitations of the frequencies in the 2.5 GHz range.

**Spectrum Reconfiguration Obligations**

In 2004, the FCC adopted a Report and Order that included new rules regarding interference in the 800 MHz band and a comprehensive plan to reconfigure the 800 MHz band. The Report and Order provides for the exchange of a portion of our 800 MHz FCC spectrum licenses, and requires us to fund the cost incurred by public safety systems and other incumbent licensees to reconfigure the 800 MHz spectrum band. Also, in exchange, we received licenses for 10 MHz of nationwide spectrum in the 1.9 GHz band.

The minimum cash obligation is \$2.8 billion under the Report and Order. We are, however, obligated to pay the full amount of the costs relating to the reconfiguration plan, even if those costs exceed \$2.8 billion. As required under the terms of the Report and Order, a letter of credit has been secured to provide assurance that funds will be available to pay the relocation costs of the incumbent users of the 800 MHz spectrum. The letter of credit was initially \$2.5 billion, but has been reduced during the course of the proceeding to \$165 million as of March 31, 2017. Since the inception of the program, we have incurred payments of approximately \$3.5 billion directly attributable to our performance under the Report and Order. When incurred, substantially all costs are accounted for as additions to FCC licenses with the remainder as property, plant and equipment. Although costs incurred through March 31, 2017 have exceeded \$2.8 billion, not all of those costs have been reviewed and accepted as eligible by the FCC's transition administrator.

Completion of the 800 MHz band reconfiguration was initially required by June 26, 2008 and public safety reconfiguration is complete across the country with the exception of the States of Arizona, California, Texas and New Mexico. The FCC continues to grant the remaining 800 MHz public safety licensees additional time to complete their band reconfigurations which, in turn, delays our access to our 800 MHz replacement channels in these areas, which are all along the U.S. - Mexico border. In the non-border impacted areas where band reconfiguration is complete, Sprint has received its replacement spectrum in the 800 MHz band and Sprint is deploying 3G CDMA and 4G LTE on this spectrum in combination with its spectrum in the 1.9 GHz and 2.5 GHz bands.

**911 Services**

Pursuant to FCC rules, CMRS providers, including us, are required to provide enhanced 911 (E911) services that deliver the location of the cell site from which a 911 call is being made or the location of the subscriber's handset using latitude and longitude, depending upon the capabilities of the requesting public safety answering point (PSAP). The FCC has also imposed enhanced location accuracy standards for the provision of wireless 911 services indoors and these requirements impose additional costs on Sprint. CMRS providers are also now required to provide text-to-911 services upon request by a capable PSAP.

**Cybersecurity**

Cybersecurity continues to receive attention at federal, state and local government levels. Congress has passed and continues to consider various forms of cybersecurity legislation to increase the security and resiliency of the nation's digital infrastructure and several federal agencies are examining cybersecurity matters. Legislation or regulation imposing new obligations related to cybersecurity may impose additional costs on Sprint. See "Item 1A. Risk Factors—Our reputation and business may be harmed and we may be subject to legal claims if there is a loss, disclosure, misappropriation of, unauthorized access to, or other security breach of our proprietary or sensitive information."

Table of Contents**National Security Agreement**

As a precondition to CFIUS approval of the SoftBank Merger, the USG Parties required that SoftBank and Sprint enter into the NSA, under which SoftBank and Sprint have agreed to implement certain measures to protect national security, certain of which may materially and adversely affect our operating results due to the increased cost of compliance with security measures, and limits over our control of certain U.S. facilities, contracts, personnel, vendor selection and operations. If we fail to comply with our obligations under the NSA, our ability to operate our business may be adversely affected. See "Item 1A. Risk Factors—Regulatory authorities have imposed measures to protect national security and classified projects as well as other conditions that could have an adverse effect on Sprint."

**State and Local Regulation**

While the Communications Act generally preempts state and local governments from regulating entry of, or the rates charged by, wireless carriers, certain state PUCs and local governments regulate infrastructure siting, customer billing, termination of service arrangements, advertising, certification of operation, use of handsets when driving, service quality, sales practices, management of customer call records and protected information and many other areas. Also, state attorneys general may bring lawsuits related to the sales practices and services of wireless carriers. Varying practices among the states may make it more difficult for us to implement national sales and marketing programs. States also may impose their own universal service support requirements on wireless and other communications carriers, similar to the contribution requirements that have been established by the FCC, and some states are requiring wireless carriers to help fund additional programs, including the implementation of E911 and the provision of intrastate relay services for consumers who are hearing impaired. We anticipate that these trends will continue to require us to devote legal and other resources to work with the states to respond to their concerns while attempting to minimize any new regulation and enforcement actions that could increase our costs of doing business.

**Regulation and Wireline Operations****Competitive Local Service**

The Telecommunications Act of 1996 (Telecom Act), which was the first comprehensive update of the Communications Act, was designed to promote competition, and it eliminated legal and regulatory barriers for entry into local and long distance communications markets. It also required incumbent local exchange carriers (ILECs) to allow resale of specified local services at wholesale rates, negotiate interconnection agreements, provide nondiscriminatory access to certain unbundled network elements and allow co-location of interconnection equipment by competitors. The rules implementing the Telecom Act continue to be interpreted by the courts, state PUCs and the FCC, and Congress is considering possible changes to the Telecom Act. Further restrictions on the pro-competition aspects of the Telecom Act could adversely affect Sprint's operations.

**International Regulation**

The wireline services we provide outside the U.S. are subject to the regulatory jurisdiction of foreign governments and international bodies. In general, we are required to obtain licenses to provide wireline services and comply with certain government requirements.

**Other Regulations****Network Neutrality**

On February 26, 2015, the FCC issued an order reclassifying broadband Internet access service as a telecommunications service subject to Title II of the Communications Act and promulgated new net neutrality rules applicable to both mobile and fixed service providers. The rules prohibit: (1) blocking of lawful content, applications, services and non-harmful devices; (2) impairing or degrading Internet traffic on the basis of content, application, or service, or use of a non-harmful device; and (3) prioritization or favoring of some network traffic over other traffic either in exchange for consideration (monetary or otherwise) from a third party, or to benefit an affiliated entity. All of these prohibitions are subject to a "reasonable network management" exception. The rules also include a "transparency" rule that requires us to disclose information about our commercial terms, performance characteristics, and network practices. In addition, the order established a future conduct rule, to be applied on a case by case basis, prohibiting broadband Internet access providers from unreasonably interfering with or disadvantaging end users' ability to use the Internet to access lawful content, applications, service, or devices of their choice, or edge providers' ability to make such content applications, services, or devices available to end users. FCC Chairman Pai recently announced his intention to initiate a proceeding to reconsider the application of

Table of Contents

these rules to broadband Internet access services. Depending upon the interpretation and application of these rules, we may incur additional costs or be limited in the services we can provide.

**Truth in Billing and Consumer Protection**

The FCC's Truth in Billing rules require both wireline and wireless telecommunications carriers, such as us, to provide full and fair disclosure of all charges on their bills, including brief, clear, and non-misleading plain language descriptions of the services provided. In addition, the FCC regularly opens proceedings or conducts investigations to address consumer protection issues (i.e., cramming). Depending upon FCC or individual state proceedings in these areas, our billing and customer service costs could increase.

**Access Charges**

ILECs and competitive local exchange carriers (CLECs) impose access charges for the origination and termination of calls upon wireless and long distance carriers, including our Wireless and Wireline segments. In addition, ILECs and CLECs charge other carriers special access charges for access to dedicated facilities that are paid by both our Wireless and Wireline segments. These fees and charges are a significant cost for our Wireless and Wireline segments and continue to be the subject of interpretation and litigation.

The FCC also recently concluded a proceeding to consider whether special access pricing rules need to be changed, and whether the terms and conditions governing the provision of special access are just and reasonable. The resulting order largely deregulates the business data services or special access market, including both Ethernet and TDM services. These actions may increase Sprint's costs of providing service as they are implemented.

**Universal Service**

Communications carriers contribute to and receive support from various Universal Service Funds (USF) established by the FCC and many states. The federal USF program funds services provided in high-cost areas, reduced-rate services to low-income consumers, and discounted communications and Internet services for schools, libraries and rural health care facilities. Similarly, many states have established their own USFs to which we contribute. The FCC has considered changing its USF contribution methodology, which could impact the amount of our assessments.

The Lifeline program is included within the USFs. Virgin Mobile was designated as a Lifeline-only Eligible Telecom Carrier (ETC) in 42 jurisdictions as of March 31, 2017, and provides service under our Assurance Wireless brand. As a Lifeline provider, Assurance Wireless receives support from the USF. Changes in the Lifeline program, including adoption of minimum service standards and the phase-out of Lifeline support for standalone voice service, and enforcement actions by the FCC and other regulatory/legislative bodies could negatively impact growth in the Assurance Wireless and wholesale subscriber base and/or the profitability of the Assurance Wireless and wholesale business overall. The decline in standalone voice support, which is expected to begin in December 2019 and will decline annually for all existing subscribers through December 2021, may be offset by the expansion of the Lifeline program to include support for broadband service.

**Electronic Surveillance Obligations**

The Communications Assistance for Law Enforcement Act (CALEA) requires telecommunications carriers in the United States, including us, to modify equipment, facilities and services to allow for authorized electronic surveillance based on either industry or FCC standards. Our CALEA obligations have been extended to data and VoIP networks, and we comply with these requirements. Certain laws and regulations require that we assist various government agencies with electronic surveillance of communications and provide records concerning those communications. We do not disclose customer information to the government or assist government agencies in electronic surveillance unless we have been provided a lawful request for such information. If our obligations under these laws and regulations were to change or were to become the focus of any inquiry or investigation, it could require us to incur additional costs and expenses, which could adversely affect our financial condition or results of operation. Certain non-U.S. laws and regulations also require that we comply with requirements to assist non-U.S. government agencies with electronic surveillance of communications and provide records concerning those communications.

**Environmental Compliance**

Our environmental compliance and remediation obligations relate primarily to the operation of standby power generators, batteries and fuel storage for our telecommunications equipment. These obligations require compliance with storage and related standards, obtaining of permits and occasional remediation. Although we cannot assess with certainty the impact of any future compliance and remediation obligations, we do not believe that any such expenditures will adversely affect our financial condition or results of operations.

Table of Contents**Patents, Trademarks and Licenses**

We own numerous patents, patent applications, service marks, trademarks and other intellectual property in the U.S. and other countries, including "Sprint<sup>®</sup>," "Boost Mobile<sup>®</sup>," and "Assurance Wireless<sup>®</sup>." Our services often use the intellectual property of others, such as licensed software, and we often license copyrights, patents and trademarks of others, like "Virgin Mobile." In total, these licenses and our copyrights, patents, trademarks and service marks are of material importance to our business. Generally, our trademarks and service marks endure and are enforceable so long as they continue to be used. Our patents and licensed patents have remaining terms of up to 10 years. We occasionally license our intellectual property to others, including licenses to others to use the "Sprint" trademark.

We have received claims in the past, and may in the future receive claims, that we, or third parties from whom we license or purchase goods or services, have infringed on the intellectual property of others. These claims can be time-consuming and costly to defend, and divert management resources. If these claims are successful, we could be forced to pay significant damages or stop selling certain products or services or stop using certain trademarks. We, or third parties from whom we license or purchase goods or services, also could enter into licenses with unfavorable terms, including royalty payments, which could adversely affect our business.

**Access to Public Filings and Board Committee Charters**

Important information is routinely posted on our website at [www.sprint.com](http://www.sprint.com). Public access is provided to our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports filed with or furnished to the SEC under the Exchange Act. These documents may be accessed free of charge on our website at the following address: <http://www.sprint.com/investors>. These documents are available as soon as reasonably practicable after filing with the SEC and may also be found at the SEC's website at [www.sec.gov](http://www.sec.gov). Information contained on or accessible through our website or the SEC's website is not part of this annual report on Form 10-K.

Our Code of Ethics, the Sprint Code of Conduct (Code of Conduct), our Corporate Governance Guidelines and the charters of the following committees of our board of directors: the Audit Committee, the Compensation Committee, the Finance Committee, and the Nominating and Corporate Governance Committee may be accessed free of charge on our website at the following address: [www.sprint.com/governance](http://www.sprint.com/governance). Copies of any of these documents can be obtained free of charge by writing to: Sprint Shareholder Relations, 6200 Sprint Parkway, Mailstop KSOPHF0302-3B679, Overland Park, Kansas 66251 or by email at [shareholder.relations@sprint.com](mailto:shareholder.relations@sprint.com). If a provision of the Code of Conduct required under the NYSE corporate governance standards is materially modified, or if a waiver of the Code of Conduct is granted to a director or executive officer, a notice of such action will be posted on our website at the following address: [www.sprint.com/governance](http://www.sprint.com/governance). Only the Audit Committee may consider a waiver of the Code of Conduct for an executive officer or director.

**Employee Relations**

As of March 31, 2017, we had approximately 28,000 employees.

**Executive Officers of the Registrant**

The following people were serving as our executive officers as of May 26, 2017. These executive officers were elected to serve until their successors have been elected. There is no familial relationship between any of our executive officers and directors.

Name	Business Experience	Current Position Held Since	Age
Marcelo Claure	President and Chief Executive Officer. Mr. Claure was named President and CEO, effective August 11, 2014, and has served on the Sprint board of directors since January 2014. Prior to this, he was CEO of Brightstar, a company he founded in 1997 and grew from a small Miami-based distributor of mobile devices into a global business with more than \$10 billion in gross revenue for the year ended 2013. Mr. Claure serves as vice chairman of the board of directors of CTIA-The Wireless Association. He also is a member of the board of directors of My Brother's Keeper Alliance.	2014	46

Table of Contents

Name	Business Experience	Current Position Held Since	Age
Tarek Robbiati	Chief Financial Officer. Mr. Robbiati was appointed Chief Financial Officer in August 2015. From January 2013 until August 2015, Mr. Robbiati served as Chief Executive Officer and Managing Director of FlexiGroup Limited in Australia, where he oversaw all segments of the company and reported to the board of directors. From December 2009 until December 2012, Mr. Robbiati was Group Managing Director and Regional President of Telstra International Group, where he oversaw all operating and financial aspects of the telecommunications company. From December 2009 until December 2012, Mr. Robbiati was Executive Chairman of Hong Kong CSL Limited ("CSL"), a subsidiary of Telstra Corporation Limited, and from July 2007 until May 2010, Mr. Robbiati served as the Chief Executive Officer of CSL, during which time he spearheaded and implemented transformation strategies and strengthened CSL's position as a Market Leader in Hong Kong.	2015	51
Guenther Ottendorfer	Chief Operating Officer, Technology. Mr. Ottendorfer was appointed Chief Operating Officer, Technology in August 2015. He is responsible for overseeing Sprint's network, technology, product development, and IT organizations, including related strategy, network operations and performance, as well as partnerships with network, technology and IT vendors. From September 2013 until April 2015, he served as Group CTO at Telekom Austria Group, where he was responsible for driving major wireless expansion, convergence and network function virtualization projects across the countries of the group. From January 2011 until July 2013, Mr. Ottendorfer served as Managing Director - Networks at Optus Singtel, Australia's second largest telecommunications provider with over 11 million customers in cable, fixed, mobile and satellite networks, where he was responsible for the day-to-day running of all Optus networks.	2015	48
Nestor Cano	Chief Operating Officer. Mr. Cano was appointed Chief Operating Officer effective February 2, 2017. Mr. Cano is responsible for delivering operational excellence, driving further expense reductions, and strengthening systems and processes across the business. From June 2007 until January 2017 Mr. Cano served as President, Europe of Tech Data Corporation, which is one of the world's largest wholesale distributors of technology products. Mr. Cano also held other senior executive roles at Tech Data Corporation, where he helped fix management processes and controls to drive the best-ever profits in the Tech Data Corporation's European operations.	2017	53
Kevin Crull	President, Omnichannel Sales. Mr. Crull was appointed President, Omnichannel Sales in November 2016, and previously served as both President of the Central and Northeast regions and Chief Marketing Officer since his arrival at Sprint in May 2015. Mr. Crull is responsible for Direct Sales, Indirect Sales and Digital Sales/Marketing, Postpaid Distribution, Omnichannel Operations, Omnichannel Customer Experience and Customer Management. From October 2010 until April 2015, Mr. Crull served as the Chief Operating Officer and then President of Bell Media, Canada's largest media and broadcasting company.	2016	52
Roger Sole	Chief Marketing Officer. Mr. Sole was appointed Chief Marketing Officer in January 2016. From May 2015 until December 2015, Mr. Sole served as Senior Vice President of Marketing, Innovation, and Hispanic Market. From August 2011 until May 2015, Mr. Sole served as the Chief Marketing Officer of TIM Brasil. Under his leadership, TIM Brasil, Telecom Italia's mobile carrier in Brazil, emerged as one of that country's fastest growing mobile operators by introducing new offers and services and providing innovative ways for customers to get new smartphones. Mr. Sole helped grow TIM Brasil to become the top seller of smartphones in Brazil with a 40% market share and nearly 75 million customers.	2016	43

Table of Contents

Name	Business Experience	Current Position Held Since	Age
Dow Draper	President - Sprint Prepaid Group. Mr. Draper was appointed President - Sprint Prepaid Group in October 2016. Since his arrival at Sprint in September 2013, Mr. Draper served as President - Global Wholesale and Prepaid Services and in May 2016, Mr. Draper was temporarily appointed as CEO of Virgin Mobile USA returning to his current role as President - Sprint Prepaid Group in October 2016. Mr. Draper manages the sales and marketing for Sprint's prepaid brands, Virgin Mobile USA, Boost Mobile and Assurance Wireless. From 2009 through September 2013, he was Senior Vice President and General Manager of Retail for CLEAR, the retail brand of Clearwire Corporation, where he oversaw the brand's sales, marketing, customer care and product development. Before joining Clearwire Corporation, Mr. Draper held various roles at Alltel Wireless, including senior vice president of Voice & Data Solutions and senior vice president of Financial Planning and Analysis. He has also held various roles at Western Wireless and McKinsey & Company.	2016	47
Yuriko Ishihara	Chief Strategy Officer. Ms. Ishihara was appointed to her position in April 2017. In this role, she oversees various strategic, regulatory, and operational matters and provides advice to senior management on various matters. Prior to joining Sprint, Ms. Ishihara served as GM, Global Business (Sprint) at SoftBank Group Corp. from July 2015 to April 2017, Vice President of SoftBank Mobile from June 2013 until April 2017, and GM - Corporate Planning at SoftBank Mobile from January 2003 until May 2013.	2017	53
Jorge Gracia	Senior Vice President, General Counsel and Chief Ethics Officer. Mr. Gracia was appointed to his position in January 2016. He oversees all strategic, transactional, dispute, and preventative legal and government affairs matters, provides advice to the board and senior management on various matters, and has responsibility for ethics training and legal compliance. Mr. Gracia has over 25 years of experience in international corporate law, most recently with Samsung Electronics America, Inc., where he served as Senior Vice President and General Counsel from October 2013 until December 2015. Mr. Gracia previously spent 17 years at Alcatel-Lucent, where he held a series of positions, each with increasing responsibility. Mr. Gracia last served as Deputy General Counsel - Global Commercial Law, a role in which he led an international team of approximately 200 professionals supporting all commercial matters, including serving as general counsel for global sales and marketing, the team responsible for worldwide revenue-generating activities.	2016	51
Paul Schieber, Jr.	Controller. Mr. Schieber was appointed Controller in December 2013. Mr. Schieber previously served in various positions at Sprint since 1991. Most recently, he served as Vice President, Access and Roaming Planning, where he was responsible for managing Sprint's roaming costs as well as its wireless and wireline access costs. Prior to that, Mr. Schieber held various leadership roles in Sprint's Finance organization including heading Sprint's internal audit function as well as serving in various Vice President - Finance roles. He was also a director in Sprint's Tax department and a director on its Mergers and Acquisitions team. Before joining Sprint, Mr. Schieber was a senior manager with the public accounting firm Ernst & Young, where he worked as an auditor and a tax consultant. In addition, he served as corporate controller for a small publicly held company.	2013	59

Table of Contents**Item 1A. Risk Factors**

In addition to the other information contained in this annual report on Form 10-K, the following risk factors should be considered carefully in evaluating us. Our business, financial condition, liquidity or results of operations could be materially adversely affected by any of these risks.

***If we are not able to retain and attract profitable wireless subscribers, our financial performance will be impaired.***

Our success is based on our ability to retain current subscribers and attract new subscribers. If we are unable to attract and retain profitable wireless subscribers, our financial performance will be impaired, and we could fail to meet our financial obligations. From January 1, 2008 through March 31, 2017, we have experienced an aggregate net decrease of approximately 11.0 million subscribers in our total retail postpaid subscriber base (excluding the impact of our acquisitions).

Our ability to retain our existing subscribers, to compete successfully for new subscribers, and reduce our churn rate depends on, among other things:

- our ability to anticipate and respond to various competitive factors, including our successful execution of marketing and sales strategies; the acceptance of our value proposition; service delivery and customer care activities, including new account set up and billing; and execution under credit and collection policies;
- actual or perceived quality and coverage of our network;
- public perception about our brands;
- our ability to anticipate, develop, and deploy new or enhanced technologies, products, and services that are attractive to existing or potential subscribers;
- our ability to continue to access spectrum and acquire additional spectrum capacity; and
- our ability to maintain our current MVNO relationships and to enter into new MVNO arrangements.

Our ability to retain subscribers may be negatively affected by industry trends related to subscriber contracts. Recently, we have seen aggressive customer acquisition efforts by our competitors. For example, most service providers, including us, are offering wireless service plans without any long-term commitment. Furthermore, some service providers are reimbursing contract termination fees, including paying off the outstanding balance on devices, incurred by new customers in connection with such customers terminating service with their current wireless service providers. Our competitors' aggressive customer contract terms, such as those described above, could negatively affect our ability to retain subscribers and could lead to an increase in our churn rates if we are not successful in providing an attractive product, price, and service mix, which could adversely affect our operating results.

We expect to continue to incur expenses such as the reimbursement of subscriber termination fees, and other subscriber acquisition and retention expenses, to attract and retain subscribers, but there can be no assurance that our efforts will generate new subscribers or result in a lower churn rate. Subscriber losses and a high churn rate could adversely affect our business, financial condition, and results of operations because they result in lost revenues and cash flow.

Moreover, we and our competitors continue to gain a greater proportion of new subscribers from each other's existing subscriber bases rather than from first-time purchasers. To the extent we cannot compete effectively for new subscribers or if we attract more subscribers that are not creditworthy, our revenues and results of operations could be adversely affected.

***The success of our network improvements will depend on the timing, extent, and cost of implementation; access to spectrum; the performance of third-parties and related parties; upgrade requirements; and the availability and reliability of the various technologies required to provide such modernization.***

We must continually invest in our wireless network, including expanding our network capacity and coverage through macro sites and small cells, in order to improve our wireless services and remain competitive. The development and deployment of new technologies and services requires us to anticipate the changing demands of our customers and to respond accordingly, which we may not be able to do in a timely or efficient manner.

Improvements in our service depend on many factors, including our ability to predict and adapt to future changes in technologies, changes in consumer demands, changes in pricing and service offerings by our competitors, and continued access to and deployment of adequate spectrum, including any leased spectrum. If we are unable to access spectrum to increase capacity or to deploy the services subscribers desire on a timely basis or at acceptable costs while maintaining network quality levels, our ability to attract and retain subscribers could be adversely affected, which would negatively impact our operating results.

Table of Contents

If we fail to provide a competitive network, our ability to provide wireless services to our subscribers, to attract and retain subscribers, and to maintain and grow our subscriber revenues could be adversely affected. For example, achieving optimal broadband network speeds, capacity, and coverage using 2.5 GHz spectrum relies in significant part on operationalizing a complex mixture of BRS and EBS spectrum licenses and leases in the desired service areas. We primarily access EBS spectrum through long-term leasing arrangements with EBS license holders. The EBS is subject to licensing limitations and the technical limitations of the frequencies in the 2.5 GHz range. See "Item 1. Business-Legislative and Regulatory Developments-Regulation and Wireless Operations-2.5 GHz License Conditions." If we are unable to operationalize this mixture of licenses and leases, our targeted network modernization goals could be adversely affected.

Using new and sophisticated technologies on a very large scale entails risks. For example, deployment of new technologies from time to time has adversely affected, and in the future may adversely affect, the performance of existing services on our network and result in increased churn or failure to attract wireless subscribers. Should implementation of our modernized network, which also includes expanding our network through densification using both macro sites and small cells, fail, be delayed or result in incurring costs in excess of expected amounts, our margins could be adversely affected and such effects could be material. Should the delivery of services expected to be deployed on our modernized network be delayed due to technological constraints or changes, performance of third-party suppliers, regulatory restrictions, including zoning and leasing restrictions, or permit issues, subscriber dissatisfaction, or other reasons, the cost of providing such services could become higher than expected, ultimately increasing our cost to subscribers and resulting in decreases in net subscribers or our margins, or both, which would adversely affect our revenues, profitability, and cash flow from operations.

*Our high debt levels and restrictive debt covenants could negatively impact our ability to access future financing at attractive rates or at all, which could limit our operating flexibility and ability to repay our outstanding debt as it matures.*

As of March 31, 2017, our consolidated principal amount of indebtedness was \$40.8 billion, and we had \$1.8 billion of undrawn borrowing capacity under the secured revolving bank credit facility. Our high debt levels and debt service requirements are significant in relation to our revenues and cash flow, which may reduce our ability to respond to competition and economic trends in our industry or in the economy generally. Our high debt levels and debt service requirements may also limit our financing options as a result of the restrictions placed on certain of our assets in our recent financing transactions. In addition, certain agreements governing our indebtedness impose operating restrictions on us, subject to exceptions, including our ability to:

- pay dividends;
- create liens on our assets;
- receive dividend or other payments from certain of our subsidiaries;
- enter into transactions with affiliates; and
- engage in certain asset sale or business combination transactions.

Our secured revolving bank credit facility and other financing facilities also require that we maintain certain financial ratios, including a leverage ratio, which could limit our ability to incur additional debt. Our failure to comply with our debt covenants would trigger defaults under those obligations, which could result in the maturities of those debt obligations being accelerated and could in turn result in cross defaults with other debt obligations. If we are forced to refinance our debt obligations prior to maturity on terms that are less favorable or if we were to experience difficulty in refinancing the debt prior to maturity, our results of operations or financial condition could be materially harmed. In addition, our recent asset-backed financings could subject us to an increased risk of loss of assets secured under those facilities. We continue to expect to rely on asset-backed financings as a source of funds, however, there can be no assurance that we will be able to continue to do so. For instance, although we have leveraged certain of our spectrum assets as collateral in an asset-backed financing transaction, certain limitations such as our leasing arrangements on 2.5 GHz spectrum may significantly reduce our ability to further leverage our spectrum. Limitations on our ability to obtain suitable financing when needed, or at all, or a failure to execute on our cost-reduction initiatives, could result in an inability to continue to expand our business, timely execute network modernization plans, and meet competitive challenges.

*Subscribers who purchase a device on a financing basis are not required to sign a fixed-term service contract, which could result in higher churn and higher bad debt expense.*

Our service plans allow certain subscribers to purchase or finance the use of an eligible device under an installment or lease contract payable generally over a period of up to 24 months. Subscribers who take advantage of these plans are not required to sign a fixed-term service contract to obtain postpaid service; rather, their service is provided on a month-to-month basis with no early termination fee. These service plans may not meet our subscribers' or potential

Table of Contents

subscribers' needs, expectations, or demands. In addition, subscribers on these plans can discontinue their service at any time without penalty, other than the obligation of any residual commitment they may have for unpaid service or for amounts due under the installment contract for the device. We could experience a higher churn rate than we expect due to the ability of subscribers to more easily change service providers, which could adversely affect our results of operations. Our operational and financial performance may be adversely affected if we are unable to grow our customer base and achieve the customer penetration levels that we anticipate with this business model.

Because our lease and installment billing contracts permit customers to pay for devices over time, we maintain a certain level of debt to support our investment in these contracts. We fund our customer device financing activities through a combination of cash on hand and proceeds from monetizing customer receivables and leased devices.

In addition, subscribers who have financed their devices through installment billing plans have the option to pay for their devices in installments generally over a period of up to 24 months. This program subjects us to increased risks relating to consumer credit issues, which could result in increased costs, including increases to our bad debt expense and write-offs of installment billing receivables. These arrangements may be particularly sensitive to changes in general economic conditions, and any declines in the credit quality of our subscriber base could have a material adverse effect on our financial position and results of operations.

*Because we lease devices to subscribers, our device leasing program exposes us to risks, including those related to the actual residual value realized on returned devices, higher churn and increased losses on devices.*

We also lease devices to certain of our subscribers. Our financial condition and results of operations depend, in part, on our ability to appropriately assess the credit risk of our lease subscribers and the ability of our lease subscribers to perform under our device leases. In addition to monthly lease payments, we expect to realize economic benefit from the estimated residual value of a leased device, which is the estimated value of a leased device at the time of the expiration of the lease term. Changes in residual value assumptions made at lease inception would affect the amount of depreciation expense and the net amount of equipment under operating leases. If estimated residual values, in the aggregate, significantly decline due to economic factors, obsolescence, or other circumstances, we may not realize such residual value, which could have a material adverse effect on our financial position and results of operations. We may also suffer negative consequences including increased costs and increased losses on devices as a result of a lease subscriber default, the related termination of a lease, and the attempted repossession of the device, including failure of a lease subscriber to return a leased device at the end of the lease. Sustained failure of subscribers to return leased devices could also negatively impact our ability to obtain financing based on leased devices in the future. In addition, subscribers who lease a device are not required to sign a fixed-term service contract, which could result in higher churn, and increased losses on devices.

*Adverse economic conditions may negatively impact our business and financial performance, as well as our access to financing on acceptable terms or at all.*

Our business and financial performance are sensitive to changes in macro-economic conditions, including changes in interest rates, consumer credit conditions, consumer debt levels, consumer confidence, inflation rates (or concerns about deflation), unemployment rates, energy costs, and other factors. Concerns about these and other factors may contribute to market volatility and economic uncertainty.

Market turbulence and weak economic conditions may materially adversely affect our business and financial performance in a number of ways. Our services are available to a broad customer base, a significant portion of which may be more vulnerable to weak economic conditions. We may have greater difficulty in gaining new subscribers within this segment and existing subscribers may be more likely to terminate service due to an inability to pay.

We will need to reduce costs and raise additional capital in the future to provide us with sufficient capital resources and liquidity to meet our commitments and execute our business strategy. Our ability to raise additional capital will depend on, among other things, conditions in the capital markets at that time, which are outside of our control, and our financial performance. Instability in the global financial markets has resulted in periodic volatility in the credit, equity, and fixed income markets. This volatility could limit our access to the credit markets, leading to higher borrowing costs or, in some cases, the inability to obtain financing on terms that are acceptable to us, or at all.

Weak economic conditions and credit conditions may also adversely impact various third parties on which we rely, some of which have filed for or may be considering bankruptcy, experiencing cash flow or liquidity problems, or are unable to obtain credit such that they may no longer be able to operate. Any of these could adversely impact our ability to distribute, market, or sell our products and services.

Table of Contents

***Government regulation could adversely affect our prospects and results of operations; federal and state regulatory commissions may adopt new regulations or take other actions that could adversely affect our business prospects, future growth, or results of operations.***

The FCC, FTC, CFPB, and other federal, state and local, as well as international, governmental authorities assert jurisdiction over our business and could adopt regulations or take other actions that would adversely affect our business prospects or results of operations.

The licensing, construction, operation, sale and interconnection arrangements of wireless telecommunications systems are regulated by the FCC and, depending on the jurisdiction, international, state and local regulatory agencies. In particular, the FCC imposes significant regulation on licensees of wireless spectrum with respect to how radio spectrum is used by licensees, the nature of the services that licensees may offer and how the services may be offered, and resolution of issues of interference between spectrum bands. The FCC grants wireless licenses for terms of generally ten years that are subject to renewal and revocation. There is no guarantee that our licenses will be renewed. Failure to comply with the FCC requirements applicable to a given license could result in revocation of that license and, depending on the nature of the non-compliance, other Sprint licenses.

The FCC uses its transactional "spectrum screen" to identify prospective wireless transactions that may require additional competitive scrutiny. If a proposed transaction would exceed the spectrum screen threshold, the FCC undertakes a more detailed analysis of relevant market conditions in the impacted geographic areas to determine whether the transaction would reduce competition without offsetting public benefits. The screen includes substantial portions of the 2.5 GHz band previously excluded from the screen and that are licensed or leased to Sprint in numerous markets. As a result, future Sprint spectrum acquisitions may exceed the spectrum screen trigger for additional FCC review. Such additional review could extend the duration of the regulatory review process and there can be no assurance that such transactions will ultimately be completed in whole or in part.

Over the past few years, the FCC and other federal and state agencies have engaged in increased regulatory and enforcement activity as well as investigations of the industry generally. Enforcement activities or investigations could make it more difficult and expensive to operate our business, and could increase the costs of our wireless operations. In addition, we may offer products that include highly regulated financial services, which subject us to additional state and federal regulations. The costs to comply with such regulations and failure to remain compliant with such regulations could adversely affect our results of operations.

Degradation in network performance caused by compliance with government regulation, loss of spectrum, or additional rules associated with the use of spectrum in any market could result in an inability to attract new subscribers or higher subscriber churn in that market, which could adversely affect our revenues and results of operations. Furthermore, additional costs or fees imposed by governmental regulation could adversely affect our revenues, future growth, and results of operations.

The Company recruits professionals, including senior management, on a global basis to work in the U.S. and, therefore, must comply with the U.S. immigration and work permit/visa laws and regulations. An inability to obtain sufficient work permits/visas due to the impact of these regulations, including any changes to immigration and work permit/visa regulations in the U.S., could have a material adverse effect on the Company's business, results of operations and financial condition.

***Competition, industry consolidation, effectiveness of our cost optimization efforts, and technological changes in the market for wireless services could negatively affect our operations, resulting in adverse effects on our revenues, cash flows, growth, and profitability.***

We compete with a number of other wireless service providers in each of the markets in which we provide wireless services. Competition is expected to continue to increase as additional spectrum, including the recent auction of 600 MHz spectrum, is made available for commercial wireless services, and we have experienced and expect to continue to experience an increased customer demand for data usage on our network. Competition in pricing, service, and product offerings may adversely impact subscriber retention and our ability to attract new subscribers. A decline in the average revenue per subscriber coupled with a decline in the number of subscribers would negatively impact our revenues, cash flows, and profitability. In addition, consolidation by our competitors and roaming partners could lead to fewer companies controlling access to network infrastructure, enabling our competitors to control usage and rates, which could negatively affect our revenues and profitability.

Table of Contents

We are executing on a multi-year plan to transform the way we do business and to lower our cost structure. If we are unable to achieve our cost optimization goals and to maintain process and system changes resulting from cost optimization objectives already established, our profitability could be negatively affected.

The wireless industry also faces competition from other communications, cable, and technology companies seeking to increase their brand recognition and capture customer revenue with respect to the provision of wireless products and services, in addition to non-traditional offerings in mobile data. Further, some of our current competitors now provide content services in addition to voice and broadband services, and consumers are increasingly accessing video content from alternative sources via Internet-based providers and applications, all of which create increased competition in this area.

The wireless communications industry continues to experience significant technological change, including improvements in the capacity, quality, and types of technology. These developments cause uncertainty about future subscriber demand for our wireless services and the prices that we will be able to charge for these services. As services, technology, and devices evolve, we also expect continued pressure on voice, text, and other service revenues. Rapid changes in technology may lead to the development of wireless communications technologies, products, or alternative services that are superior to our technologies, products, or services, or that consumers prefer over ours. In addition, technological advances have caused long distance, local, wireless, video, and Internet services to become more integrated, which has contributed to increased competition, new competitors, new products, and the expansion of services offered by our competitors in each of these markets. If we are unable to meet future advances in competing technologies on a timely basis, or at an acceptable cost, we may not be able to compete effectively and could lose subscribers to our competitors.

*The trading price of our common stock has been, and may continue to be, volatile and may not reflect our actual operations and performance.*

Market and industry factors may adversely impact the market price of our common stock, regardless of our actual operations and performance. Stock price volatility and sustained decreases in our share price could subject our stockholders to losses and may adversely impact our ability to issue equity. The trading price of our common stock has been, and may continue to be, subject to fluctuations in response to various factors, some of which are beyond our control, including, but not limited to:

- market and pricing risks due to concentrated ownership of our stock;
- the ability to raise additional capital through the issuance of additional debt or equity or otherwise, including the cost and availability or perceived availability of additional capital;
- announcements by us or our competitors or market speculation of acquisitions, spectrum acquisitions, new products, technologies, significant contracts, commercial relationships, or capital commitments;
- the performance of SoftBank and SoftBank's ordinary shares or speculation about the possibility of future actions SoftBank may take in connection with us;
- disruption to our operations or those of other companies critical to our network operations;
- our ability to develop and market new and enhanced technologies, products and services on a timely and cost-effective basis, including any network improvement efforts;
- recommendations by securities analysts or changes in their estimates concerning us;
- changes in the ratings of our debt by rating agencies;
- litigation;
- changes in governmental actions, regulations, or approvals; and
- perceptions of general market conditions in the technology and communications industries, the U.S. economy, and global market conditions.

*We have entered into, or may enter into, agreements with various parties for certain business operations. Any difficulties experienced by us in these arrangements could result in additional expense, loss of subscribers and revenue, interruption of our services, or a failure or delay in the roll-out of new technology.*

We have entered into, and may in the future enter into, agreements with various third parties for the day-to-day execution of services, provisioning, maintenance, modernization, and densification of our wireless and wireline networks, including the permitting, building, installation, and ownership of certain portions of our new network densification; leases and subleases for space on communications towers; the development and maintenance of certain systems necessary for the operation of our business; customer service, related support to our wireless subscribers, outsourcing aspects of our wireline

Table of Contents

network and back office functions; and to provide network equipment, handsets, devices, and other equipment. For example, we depend heavily on local access facilities obtained from ILECs to serve our data and voice subscribers, and payments to ILECs for these facilities are a significant cost of service for both our Wireless and Wireline segments. We also expect our dependence on key suppliers to continue as more advanced technologies are developed, which may lead to additional significant costs. If our key vendors fail to meet their contractual obligations or experience financial difficulty, or if we fail to adequately diversify our reliance among vendors, we may experience disruptions to our business operations or incur significant costs implementing alternative arrangements.

***The products and services utilized by us and our suppliers and service providers may infringe on intellectual property rights owned by others.***

Some of our products and services use intellectual property that we own. We also purchase products from suppliers, including device suppliers, and outsource services to service providers, including billing and customer care functions, that incorporate or utilize intellectual property. We and some of our suppliers and service providers have received, and may receive in the future, assertions and claims from third parties that the products or software utilized by us or our suppliers and service providers infringe on the patents or other intellectual property rights of these third parties. These claims could require us or an infringing supplier or service provider to cease certain activities or to cease selling the relevant products and services. These claims can be time-consuming and costly to defend and divert management resources. If these claims are successful, we could be forced to pay significant damages or stop selling certain products or services or stop using certain trademarks, which could adversely affect our results of operations.

***Negative outcomes of legal proceedings may adversely affect our business and financial condition.***

We are regularly involved in a number of legal proceedings before various state and federal courts, the FCC, the FTC, the CFPB, and other federal, state, and local regulatory agencies. These proceedings may be complicated, costly, and disruptive to our business operations. We may incur significant expenses in defending these matters and may be required to pay significant fines, awards, or settlements. In addition, litigation or other proceedings could result in restrictions on our current or future manner of doing business. Any of these potential outcomes, such as judgments, awards, settlements, or orders could have a material adverse effect on our business, financial condition, operating results, or ability to do business.

***Our reputation and business may be harmed and we may be subject to legal claims if there is a loss, disclosure, misappropriation of, unauthorized access to, or other security breach of our proprietary or sensitive information.***

Our information technology and other systems—including those of our third-party service providers—that maintain and transmit our proprietary information and our subscribers' information, including credit card information, location data, or other personal information may be compromised by a malicious third-party penetration of our network security or impacted by advertent or inadvertent actions or inactions by our employees and agents. As a result, our subscribers' information may be lost, disclosed, accessed, used, corrupted, destroyed, or taken without the subscribers' consent. Cyber attacks, such as the use of malware, computer viruses, denial of service attacks, or other means for disruption or unauthorized access, have increased in frequency, scope, and potential harm in recent years. We also purchase equipment and software from third parties that could contain software defects, Trojan horses, malware, or other means by which third parties could access our network or the information stored or transmitted on such network or equipment.

While to date we have not been subject to cyber attacks or other cyber incidents that, individually or in the aggregate, have been material to our operations or financial condition, the preventive actions we take to reduce the risk of cyber incidents and protect our information technology and networks may be insufficient to repel a cyber attack in the future. In addition, the costs of such preventative actions may be significant, which may adversely affect our results of operations. Any major compromise of our data or network security, failure to prevent or mitigate a loss of our services or network, our proprietary information, or our subscribers' information, and delays in detecting any such compromise or loss, could disrupt our operations, impact our reputation and subscribers' willingness to purchase our service, and subject us to significant additional expenses. Such expenses could include incentives offered to existing subscribers and other business relationships in order to retain their business, increased expenditures on cyber security measures and the use of alternate resources, lost revenues from business interruption, and litigation, which could be material. Furthermore, the potential costs associated with any such cyber attacks could be greater than the insurance coverage we maintain.

In addition to cyber attacks, major equipment failures, natural disasters, including severe weather, terrorist acts or other disruptions that affect our wireline and wireless networks, including transport facilities, communications switches, routers, microwave links, cell sites, or other equipment or third-party owned local and long-distance networks on which we rely, could disrupt our operations, require significant resources to remedy, result in a loss of subscribers or impair our ability

Table of Contents

to attract new subscribers, which in turn could have a material adverse effect on our business, results of operations and financial condition.

*If we are unable to improve our results of operations and as we continue to modernize our networks, we may be required to recognize an impairment of our long-lived assets, goodwill, or other indefinite-lived intangible assets, which could have a material adverse effect on our financial position and results of operations.*

As a result of the SoftBank Merger, Sprint recognized goodwill at its acquisition-date estimate of fair value of approximately \$6.6 billion, which has been entirely allocated to the wireless segment. Since goodwill was reflected at its estimate of fair value, there was no excess fair value over book value as of the date of the close of the SoftBank Merger. Additionally, we recorded \$14.6 billion and \$41.7 billion of long-lived assets and indefinite-lived intangible assets, respectively, as of the close of the SoftBank Merger. We evaluate the carrying value of our indefinite-lived assets, including goodwill, at least annually or more frequently whenever events or changes in circumstances indicate that the asset may be impaired, or in the case of goodwill, that the fair value of the reporting unit is below its carrying amount. During the year ended March 31, 2015, we recorded an impairment loss of \$1.9 billion and \$233 million for the Sprint trade name and Wireline long-lived assets, respectively. Continued, sustained declines in the Company's operating results, number of wireless subscribers, future forecasted cash flows, growth rates and other assumptions, as well as significant, sustained declines in the Company's stock price and related market capitalization could impact the underlying key assumptions and our estimated fair values, potentially leading to a future material impairment of long-lived assets, goodwill, or other indefinite-lived assets, which could adversely affect our financial position and results of operations. In addition, as we continue to refine our network strategy, management may conclude, in future periods, that certain equipment assets in use will not be utilized as long as originally intended, which could result in an acceleration of depreciation expense. Moreover, certain equipment assets may never be deployed or redeployed, in which case cash and/or non-cash charges that could be material to our consolidated financial statements would be recognized.

*Any acquisitions, strategic investments, or mergers may subject us to significant risks, any of which may harm our business.*

As part of our long-term strategy, we regularly evaluate potential acquisitions, strategic investments, and mergers, and we actively engage in discussions with potential counterparties. Over time, we may acquire, make investments in, or merge with companies that complement or expand our business. Some of these potential transactions could be significant relative to the size of our business and operations. Any such acquisitions would involve a number of risks and present financial, managerial and operational challenges, including:

- diversion of management attention from running our existing business;
- possible material weaknesses in internal control over financial reporting;
- increased costs to integrate the networks, spectrum, technology, personnel, subscriber base, and business practices of the company involved in the acquisition, strategic investment, or merger with our business;
- potential exposure to material liabilities not discovered in the due diligence process or as a result of any litigation arising in connection with such transactions;
- significant transaction expenses in connection with any such transaction, whether consummated or not;
- risks related to our ability to obtain any required regulatory approvals necessary to consummate any such transaction;
- acquisition financing may not be available on reasonable terms or at all and any such financing could significantly increase our outstanding indebtedness or otherwise affect our capital structure or credit ratings; and
- any acquired or merged business, technology, service, or product may significantly under-perform relative to our expectations, and we may not achieve the benefits we expect from our transaction, which could, among other things, also result in a write-down of goodwill and other intangible assets associated with such transaction.

For any or all of these reasons, our pursuit of an acquisition, investment, or merger may cause our actual results to differ materially from those anticipated.

Table of Contents**Controlled Company Risks**

***As long as SoftBank controls us, other holders of our common stock will have limited ability to influence matters requiring stockholder approval and SoftBank's interest may conflict with ours and our other stockholders.***

As of March 31, 2017, SoftBank beneficially owned approximately 83% of the outstanding common stock of Sprint. As a result, until such time as SoftBank and its controlled affiliates hold shares representing less than a majority of the votes entitled to be cast by the holders of our outstanding common stock at a stockholder meeting, SoftBank generally will have the ability to control the outcome of any matter submitted for the vote of our stockholders, except in certain circumstances set forth in our certificate of incorporation or bylaws.

So long as SoftBank and its controlled affiliates hold shares of our common stock representing at least a majority of the votes entitled to be cast by the holders of our common stock at a stockholder meeting, SoftBank will be able to freely nominate and elect all the members of our board of directors, subject only to a requirement that a certain number of directors qualify as "Independent Directors," as such term is defined in the NYSE listing rules and applicable laws. The directors elected by SoftBank will have the authority to make decisions affecting the capital structure of the Company, including the issuance of additional equity, the incurrence of additional indebtedness, the implementation of stock repurchase programs, and the declaration of dividends.

The interests of SoftBank may not coincide with the interests of our other stockholders or with holders of our indebtedness. SoftBank's ability, subject to the limitations in our certificate of incorporation and bylaws, to control all matters submitted to our stockholders for approval limits the ability of other stockholders to influence corporate matters and, as a result, we may take actions that our stockholders or holders of our indebtedness do not view as beneficial. As a result, the market price of our common stock or terms upon which we issue indebtedness could be adversely affected. In addition, the existence of a controlling stockholder may have the effect of making it more difficult for a third-party to acquire, or discouraging a third-party from seeking to acquire, the Company. A third-party would be required to negotiate any such transaction with SoftBank, and the interests of SoftBank with respect to such transaction may be different from the interests of our other stockholders or with holders of our indebtedness. In addition, the performance of SoftBank and SoftBank's ordinary shares or speculation about the possibility of future actions SoftBank may take in connection with us may adversely affect our share price or the trading price of our debt securities.

Subject to limitations in our certificate of incorporation that limit SoftBank's ability to engage in certain competing businesses in the U.S. or take advantage of certain corporate opportunities, SoftBank is not restricted from competing with us or otherwise taking for itself or its other affiliates certain corporate opportunities that may be attractive to the Company.

***SoftBank's ability to control our board of directors may make it difficult for us to recruit independent directors.***

For so long as SoftBank and its controlled affiliates hold shares of our common stock representing at least a majority of the votes entitled to be cast by the holders of our common stock at a stockholders' meeting, SoftBank will be able to elect all of the members of our board of directors. Further, the interests of SoftBank and our other stockholders may diverge. Under these circumstances, persons who might otherwise accept an invitation to join our board of directors may decline.

***Any inability to resolve favorably any disputes that may arise between the Company and SoftBank or its affiliates may adversely affect our business.***

Disputes may arise between SoftBank or its affiliates and the Company in a number of areas, including:

- business combinations involving the Company;
- sales or dispositions by SoftBank of all or any portion of its ownership interest in us;
- the nature, quality and pricing of services SoftBank or its affiliates may agree to provide to the Company;
- arrangements with third parties that are exclusionary to SoftBank or its affiliates or the Company; and
- business opportunities that may be attractive to both SoftBank or its affiliates and the Company.

We may not be able to resolve any potential conflicts, and even if we do, the resolution may be less favorable than if we were dealing with an unaffiliated party.

Table of Contents

*We are a "controlled company" within the meaning of the NYSE rules and, as a result, rely on exemptions from certain corporate governance requirements that provide protection to stockholders of companies that are not "controlled companies."*

SoftBank owns more than 50% of the total voting power of our common shares and, accordingly, we have elected to be treated as a "controlled company" under the NYSE corporate governance standards. As a controlled company, we are exempt under the NYSE standards from the obligation to comply with certain NYSE corporate governance requirements, including the requirements that:

- a majority of our board of directors consists of independent directors;
- we have a corporate governance and nominating committee that is composed entirely of independent directors with a written charter addressing the committee's purpose and responsibilities;
- we have a compensation committee that is composed entirely of independent directors with a written charter addressing the committee's purpose and responsibilities; and
- an annual performance evaluation of the nominating and governance committee and compensation committee be performed.

As a result of our use of the "controlled company" exemptions, holders of our common stock and debt securities may not have the same protection afforded to stockholders of companies that are subject to all of the NYSE corporate governance requirements.

*Regulatory authorities have imposed measures to protect national security and classified projects as well as other conditions that could have an adverse effect on Sprint.*

As a precondition to approval of the SoftBank Merger, certain U.S. government agencies required that SoftBank and Sprint enter into certain agreements, including the NSA, under which SoftBank and Sprint have agreed to implement certain measures to protect national security, certain of which may materially and adversely affect our operating results due to increasing the cost of compliance with security measures, and limiting our control over certain U.S. facilities, contracts, personnel, vendor selection, and operations. If we fail to comply with our obligations under the NSA or other agreements, our ability to operate our business may be adversely effected.

**Item 1B. Unresolved Staff Comments**

None.

**Item 2. Properties**

Our corporate headquarters are located in Overland Park, Kansas and consist of approximately 3,853,000 square feet. Our gross property, plant and equipment at March 31, 2017 totaled \$33.7 billion, as follows:

	<b>March 31, 2017</b>
	<i>(in billions)</i>
Wireless	\$ 30.4
Wireline	1.3
Corporate and other	2.0
Total	<u>\$ 33.7</u>

Properties utilized by our Wireless segment generally consist of either leased or owned assets in the following categories: switching equipment, radio frequency equipment, cell site towers and related leasehold improvements, site development costs, network software, leased devices, internal-use software, retail fixtures and retail leasehold improvements.

Properties utilized by our Wireline segment generally consist of either leased or owned assets in the following categories: digital fiber optic cable, transport facilities, transmission-related equipment and network buildings.

Table of Contents**Item 3. Legal Proceedings**

In March 2009, a stockholder brought suit, *Bennett v. Sprint Nextel Corp.*, in the U.S. District Court for the District of Kansas, alleging that Sprint Communications and three of its former officers violated Section 10(b) of the Exchange Act and Rule 10b-5 by failing adequately to disclose certain alleged operational difficulties subsequent to the Sprint-Nextel merger, and by purportedly issuing false and misleading statements regarding the write-down of goodwill. The district court granted final approval of a settlement in August 2015, which did not have a material impact to our financial statements. Five stockholder derivative suits related to this 2009 stockholder suit were filed against Sprint Communications and certain of its present and/or former officers and directors. The first, *Murphy v. Forsee*, was filed in state court in Kansas on April 8, 2009, was removed to federal court, and was stayed by the court pending resolution of the motion to dismiss the *Bennett* case; the second, *Randolph v. Forsee*, was filed on July 15, 2010 in state court in Kansas, was removed to federal court, and was remanded back to state court; the third, *Ross-Williams v. Bennett, et al.*, was filed in state court in Kansas on February 1, 2011; the fourth, *Price v. Forsee, et al.*, was filed in state court in Kansas on April 15, 2011; and the fifth, *Hartleib v. Forsee, et al.*, was filed in federal court in Kansas on July 14, 2011. These cases were essentially stayed while the *Bennett* case was pending, and we have reached an agreement in principle to settle the matters, by agreeing to some governance provisions and by paying plaintiffs' attorneys fees in an immaterial amount. The court approved the settlement but reduced the plaintiffs' attorneys fees; the attorneys fees issue is on appeal.

Sprint Communications, Inc. is also a defendant in a complaint filed by several stockholders of Clearwire Corporation (Clearwire), asserting claims for breach of fiduciary duty by Sprint Communications, and related claims and otherwise challenging the Clearwire acquisition. *ACP Master, LTD, et al. v. Sprint Nextel Corp., et al.*, was filed April 26, 2013 in Chancery Court in Delaware. Plaintiffs in the *ACP Master, LTD* suit have also filed suit requesting an appraisal of the fair value of their Clearwire stock. Trial of those cases took place in October and November 2016; the parties have submitted their post-trial briefing, and oral argument was held on April 25, 2017. We are awaiting decision. We do not expect the resolution of these matters to have a material adverse effect on our financial position or results of operations.

Various other suits, inquiries, proceedings, and claims, either asserted or unasserted, including purported class actions typical for a large business enterprise and intellectual property matters, are possible or pending against us. If our interpretation of certain laws or regulations, including those related to various federal or state matters such as sales, use or property taxes, or other charges were found to be mistaken, it could result in payments by us. While it is not possible to determine the ultimate disposition of each of these proceedings and whether they will be resolved consistent with our beliefs, we expect that the outcome of such proceedings, individually or in the aggregate, will not have a material adverse effect on our financial position or results of operations.

**Item 4. Mine Safety Disclosures**

None.

Table of Contents**PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities****Common Share Data**

The common stock of Sprint Corporation is traded under the stock symbol "S" on the NYSE. We currently have no non-voting common stock outstanding. The high and low common stock prices, as reported on the NYSE composite, were as follows:

	Year Ended March 31, 2017		Year Ended March 31, 2016	
	High	Low	High	Low
<b>Common stock market price</b>				
First quarter	\$ 4.56	\$ 3.30	\$ 5.39	\$ 4.41
Second quarter	7.03	4.36	5.29	3.10
Third quarter	8.98	5.83	5.12	3.50
Fourth quarter	9.65	8.13	4.19	2.18

**Number of Stockholders of Record**

As of May 22, 2017, we had approximately 28,000 common stock record holders.

**Dividends**

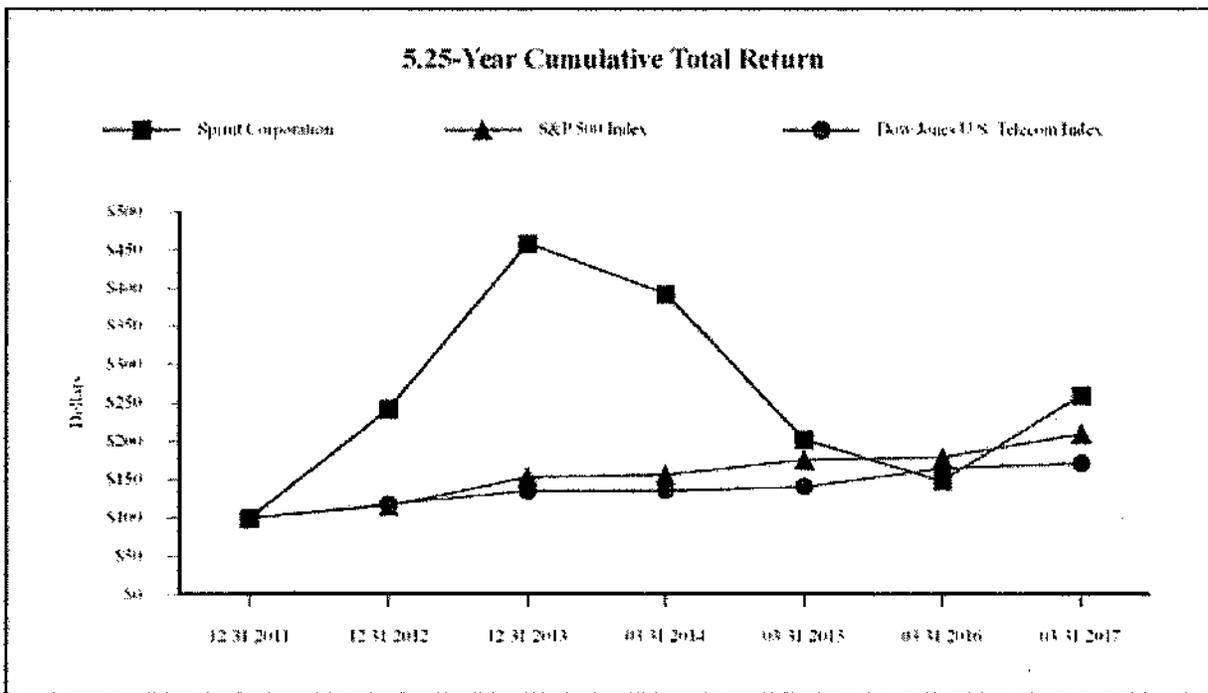
We did not declare any dividends on our common stock for all periods presented in the consolidated financial statements. We are currently restricted from paying cash dividends by the terms of our secured revolving bank credit facility as described under "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources."

**Issuer Purchases of Equity Securities**

None.

Table of Contents**Performance Graph**

The graph below compares the cumulative total shareholder return for the Company's common stock with the S&P<sup>®</sup> 500 Stock Index and the Dow Jones U.S. Telecommunications Index for the two fiscal years ended December 31, 2012 and 2013, the three-month transition period ended March 31, 2014 and the fiscal years ended March 31, 2015, 2016 and 2017. Because Sprint Corporation common stock did not commence trading until after the SoftBank Merger, the graph below reflects the cumulative total shareholder return on the Series 1 common stock of Sprint Communications, Inc., our predecessor, through July 10, 2013 and, thereafter, reflects the total shareholder return on the common stock of Sprint Corporation. The graph assumes an initial investment of \$100 on December 31, 2011 and, if any, the reinvestment of all dividends.



Value of \$100 Invested on December 31, 2011

	12/31/2011	12/31/2012	12/31/2013	3/31/2014	3/31/2015	3/31/2016	3/31/2017
Sprint Corporation	\$ 100.00	\$ 242.31	\$ 459.40	\$ 392.74	\$ 202.56	\$ 148.72	\$ 260.95
S&P 500 Index	\$ 100.00	\$ 116.00	\$ 153.58	\$ 156.35	\$ 176.26	\$ 179.40	\$ 210.21
Dow Jones U.S. Telecom Index	\$ 100.00	\$ 118.48	\$ 135.22	\$ 135.71	\$ 141.25	\$ 165.43	\$ 172.10

Table of Contents**Item 6. Selected Financial Data**

The Company's selected financial data presented below distinguishes between the predecessor period (Predecessor) relating to Sprint Communications (formerly known as Sprint Nextel Corporation) for periods prior to the SoftBank Merger and the successor period (Successor) relating to Sprint Corporation, formerly known as Starburst II, for periods subsequent to the incorporation of Starburst II on October 5, 2012. The Successor financial information represents the activity and accounts of Sprint Corporation, which includes the activity and accounts of Starburst II prior to the close of the SoftBank Merger on July 10, 2013 and Sprint Communications, inclusive of the consolidation of Clearwire Corporation, prospectively following completion of the SoftBank Merger, beginning on July 11, 2013. The accounts and operating activity of Starburst II prior to the close of the SoftBank Merger primarily related to merger expenses that were incurred in connection with the SoftBank Merger (recognized in selling, general and administrative expense) and interest related to the \$3.1 billion convertible bond Sprint Communications, Inc. issued to Starburst II. The Predecessor financial information represents the historical basis of presentation for Sprint Communications for all periods prior to the SoftBank Merger.

The selected financial data presented below is not comparable for all periods presented primarily as a result of transactions such as the SoftBank Merger and acquisitions of Clearwire and certain assets of United States Cellular Corporation in 2013. All acquired companies' results of operations subsequent to their acquisition dates are included in our consolidated financial statements.

	Successor							Predecessor		
	Year Ended March 31,			Three Months Ended March 31,		Year Ended December 31,		191 Days Ended July 10,	Three Months Ended March 31,	Year Ended December 31,
	2017	2016	2015	2014	2013	2013	2012	2013	2013	2012
	<i>(in millions, except per share amounts)</i>									
<b>Results of Operations</b>										
Service revenue	\$ 25,368	\$ 27,174	\$ 29,542	\$ 7,876	\$ —	\$ 15,094	\$ —	\$ 16,895	\$ 7,980	\$ 32,097
Equipment revenue	7,979	5,006	4,990	999	—	1,797	—	1,707	813	3,248
Net operating revenues	33,347	32,180	34,532	8,875	—	16,891	—	18,602	8,793	35,345
Depreciation	7,098	5,794	3,797	868	—	2,026	—	3,098	1,422	6,240
Amortization	1,052	1,294	1,552	429	—	908	—	147	70	303
Operating income (loss)	1,764	310	(1,895)	420	(14)	(970)	(33)	(885)	29	(1,820)
Net loss	(1,206)	(1,995)	(3,345)	(151)	(9)	(1,860)	(27)	(1,158)	(643)	(4,326)
<b>Loss per Share</b>										
Basic and diluted loss per common share	\$ (0.30)	\$ (0.50)	\$ (0.85)	\$ (0.04)		\$ (0.54)		\$ (0.38)	\$ (0.21)	\$ (1.44)
<b>Financial Position</b>										
Total assets	\$ 85,123	\$ 78,975	\$ 82,841	\$ 84,549	\$ 3,122	\$ 85,953	\$ 3,115	N/A	\$ 50,474	\$ 51,278
Property, plant and equipment, net	19,209	20,297	19,721	16,299	—	16,164	—	N/A	14,025	13,607
Intangible assets, net	50,484	51,117	52,455	55,919	—	56,272	—	N/A	22,352	22,371
Total debt, capital lease and financing obligations (including equity unit notes)	40,914	33,958	33,642	32,638	—	32,869	—	N/A	24,217	24,049
Stockholders' equity	18,808	19,783	21,710	25,312	3,122	25,584	3,110	N/A	6,474	7,087
<b>Cash Flow Data</b>										
Net cash provided by (used in) operating activities	\$ 4,168	\$ 3,897	\$ 2,450	\$ 522	\$ (2)	\$ (61)	\$ —	\$ 2,671	\$ 940	\$ 2,999
Capital expenditures - network and other	1,950	4,680	5,422	1,488	—	3,847	—	3,140	1,381	4,261
Capital expenditures - leased devices	1,925	2,292	582	—	—	—	—	—	—	—



Table of Contents**Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations*****OVERVIEW****Business Overview**

Sprint is a communications company offering a comprehensive range of wireless and wireline communications products and services that are designed to meet the needs of individual consumers, businesses, government subscribers, and resellers. Unless the context otherwise requires, references to "Sprint," "we," "us," "our" and the "Company" mean Sprint Corporation and its consolidated subsidiaries for all periods presented, and references to "Sprint Communications" are to Sprint Communications, Inc. and its consolidated subsidiaries.

Wireless segment earnings represented almost all of our total consolidated segment earnings for the year ended March 31, 2017. Within the Wireless segment, postpaid wireless service revenue represents the most significant contributor to earnings, and is driven by the number of postpaid subscribers to our services, as well as the average revenue per user (ARPU).

***Strategies and Key Priorities***

Our business strategy is to be responsive to changing customer mobility demands of existing and potential customers, and to expand our business into new areas of customer value and economic opportunity through innovation and differentiation. To help lay the foundation for these future growth opportunities, our strategy revolves around targeted investment, in the following key priority areas:

- Unlock the value of our substantial spectrum holdings by densifying and optimizing our network to provide customers with the best experience;
- Achieve our cost reduction goals by significantly transforming our business;
- Deliver an attractive value proposition and substantially enhance our distribution through use of innovative models;
- Create an alternative financial structure that leverages our assets to fuel our growth and maximize stockholder value;
- Attract and retain world-class talent and establish strategic partnerships to create the optimal, engaged, and winning team; and
- Deliver an exceptional wireless experience so customers stay longer, buy more, and tell their friends.

To provide a network that delivers the consistent reliability, capacity and speed that customers demand, we expect to continue to optimize our 3G data network and invest in LTE deployment across all of our spectrum bands. We also expect to deploy new technologies that will help strengthen our competitive position, including the expected use of High Performance User Equipment, the Magic Box which is an LTE booster, Voice over LTE, more extensive use of Wi-Fi and the use of small cells to further densify our network.

To achieve a more competitive cost position, we have established an Office of Cost Management with responsibility for identifying, operationalizing, and monitoring sustained improvements in operating costs and efficiencies. Also, we have deployed new cost management and planning tools across the entire organization to more effectively monitor expenditures.

We are focused on attracting and retaining subscribers by improving our sales and marketing initiatives. We have demonstrated our value proposition through our evolving price plans, promotions, and payment programs and have deployed new local marketing and civic engagement initiatives in key markets.

Our current strategy also includes transactions that continue to leverage our assets such as the Accounts Receivable Facility, the Handset Sale-Leaseback transactions, the Network Equipment Sale-Leaseback and the Spectrum Financing transaction. Each of these transactions are described in more detail in "Liquidity and Capital Resources."

We have recruited leaders in our industry from around the globe and employ an organizational focus to ensure Sprint has a work environment employees recommend.

To deliver a simplified and improved customer experience, we are focusing on key subscriber touch points, pursuing process improvements and deploying platforms to simplify and enhance the interactions between us and our customers. In addition, we have established a customer experience team to support our focus on net promoter score as an important key measure of customer satisfaction.

Table of Contents**Network**

We continue to increase coverage and capacity by densifying and optimizing our existing network. Densification, which includes increasing the number of small cells and antennas, is intended to enhance coverage and capacity across the network. We expect the densification efforts to cost significantly less than our historical macro cell site builds (*i.e.*, adding traditional cell towers). We are also deploying new technologies, such as carrier aggregation, which allows us to move more data at faster speeds over the same spectrum. Additionally, our introduction of tri-band devices, which support each of our spectrum bands, allows us to manage and operate our network more efficiently and at a lower cost. We have continued to see positive results from these infrastructure upgrades in key U.S. markets.

The 2.5 GHz spectrum band carries the highest percentage of Sprint's LTE data traffic. We have significant additional capacity to grow the use of our 2.5 GHz spectrum holdings into the future. Sprint believes it is well-positioned with spectrum holdings of more than 160 MHz of 2.5 GHz spectrum in the top 100 markets in the U.S.

Overall, our densification and optimization efforts are expected to continue to enhance the customer experience by adding data capacity, increasing the wireless data speeds available to our customers, and improving network performance for both voice and data services. While circumstances may change in the future, we believe that our substantial spectrum holdings are sufficient to allow us to continue to provide consistent network reliability, capacity, and speed, as well as to provide current and future customers a highly competitive wireless experience. As we continue to refine our network strategy and evaluate other potential network initiatives, we may incur future material charges associated with lease and access exit costs, loss from asset dispositions or accelerated depreciation, among others.

**Shentel Transaction**

On August 10, 2015, Shenandoah Telecommunications Company (Shentel) entered into a definitive agreement to acquire one of our wholesale partners, NTELOS Holdings Corp (nTelos). In connection with this definitive agreement, we entered into a series of agreements with Shentel to, among other things, acquire certain assets such as spectrum, terminate our existing wholesale arrangement with nTelos, and amend our existing affiliate agreement with Shentel to primarily include the subscribers formerly under the wholesale arrangement with nTelos. The agreements also expanded the area in which Shentel provides wireless service to Sprint customers and provided for more favorable economic terms. In April 2016, we received regulatory approval and the transaction closed in May 2016. The total consideration for this transaction included \$181 million, on a net present value basis, of notes payable to Shentel. Sprint will satisfy its obligations under the notes payable over an expected term of five to six years. FCC licenses acquired from Shentel had a total value of \$85 million. \$96 million of the total purchase was recorded in "Other, net" in the consolidated statements of operations as a contract termination in the quarter ended June 30, 2016, which related to the termination of our pre-existing wholesale arrangement with nTelos.

**RESULTS OF OPERATIONS****Consolidated Results of Operations**

The following table provides an overview of the consolidated results of operations.

	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Wireless segment earnings	\$ 9,814	\$ 8,051	\$ 5,894
Wireline segment earnings	119	92	113
Corporate, other and eliminations	1	3	(7)
Consolidated segment earnings	9,934	8,146	6,000
Depreciation	(7,098)	(5,794)	(3,797)
Amortization	(1,052)	(1,294)	(1,552)
Impairments	—	—	(2,133)
Other, net <sup>(1)</sup>	(20)	(748)	(413)
Operating income (loss)	1,764	310	(1,895)
Interest expense	(2,495)	(2,182)	(2,051)
Other (expense) income, net	(40)	18	27
Income tax (expense) benefit	(435)	(141)	574
Net loss	<u>\$ (1,206)</u>	<u>\$ (1,995)</u>	<u>\$ (3,345)</u>

(1) Other, net for the years ended March 31, 2017 and 2016 excludes \$481 million and \$321 million of losses, respectively, related to losses on disposal of property, plant and equipment which is included in Wireless segment earnings.



Table of Contents***Depreciation Expense***

Depreciation expense increased \$1.3 billion, or 23%, in the year ended March 31, 2017 compared to the same period in 2016 and increased \$2.0 billion, or 53%, in the year ended March 31, 2016 compared to same period in 2015 primarily due to increased depreciation on leased devices as a result of the continued growth of the device leasing program that was introduced in September 2014. In addition, depreciation expense increased in the year ended March 31, 2016 compared to the same period in 2015 due to network asset additions, partially offset by a decrease due to assets being retired or fully depreciated. Depreciation expense incurred on all leased devices for the years ended March 31, 2017, 2016, and 2015 was \$3.1 billion, \$1.8 billion, and \$206 million, respectively.

***Amortization Expense***

Amortization expense decreased \$242 million, or 19%, in the year ended March 31, 2017 compared to the same period in 2016 and decreased \$258 million, or 17%, in the year ended March 31, 2016 compared to the same period in 2015 primarily due to customer relationship intangible assets that are amortized using the sum-of-the-months'-digits method, which results in higher amortization rates in early periods that decline over time.

***Impairments***

During the year ended March 31, 2015, we determined that recoverability of the carrying amount of the Sprint trade name should be evaluated for impairment due to changes in circumstances surrounding our Wireless reporting unit. As a result, we recorded an impairment loss of \$1.9 billion, which is included in "Impairments" in our consolidated statements of operations. During the year ended March 31, 2015, we also tested the recoverability of the Wireline asset group, which consists primarily of property, plant and equipment, due to continued declines in our Wireline segment earnings and our forecast that projected continued losses in future periods. As a result, we recorded an impairment loss of \$233 million to reduce the carrying value of Wireline's property, plant and equipment to its estimated fair value, which is included in "Impairments" in our consolidated statements of operations.

***Other, net***

The following table provides additional information regarding items included in "Other, net."

	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Severance and exit costs	\$ (66)	\$ (409)	\$ (304)
Litigation and other contingencies	(140)	(193)	(91)
Loss on disposal of property, plant and equipment	(28)	(166)	—
Contract terminations	(140)	—	—
Gains from asset dispositions and exchanges	354	—	—
Revision to estimate of a previously recorded reserve	—	20	41
Partial pension settlement	—	—	(59)
Total expense	<u>\$ (20)</u>	<u>\$ (748)</u>	<u>\$ (413)</u>

Other, net represented an expense of \$20 million in the year ended March 31, 2017. We recognized severance and exit costs of \$66 million. In addition, we recognized a \$140 million charge for a state tax matter combined with legal reserves related to other pending legal suits and proceedings, a \$354 million non-cash gain as a result of spectrum license exchanges with other carriers, and a \$28 million loss on disposal of property, plant and equipment primarily related to cell site construction costs that are no longer recoverable as a result of changes in our network plans. We also recognized \$140 million of contract terminations that were primarily related to the termination of our pre-existing wholesale arrangement with nTelos as a result of the Shentel transaction combined with the costs related to the termination of our relationship with General Wireless Operations Inc. (Radio Shack).

Other, net reflected an expense of \$748 million in the year ended March 31, 2016. We recognized litigation expense of \$193 million for ongoing legal matters. In addition, we recognized severance and exit costs which included \$216 million of severance primarily associated with reductions in work force and \$195 million of lease and access exit costs primarily associated with tower and cell site leases and backhaul access contracts for which we will no longer be receiving any economic benefit, of which \$2 million was recognized as "Cost of services" in the consolidated statements of operations. We also recorded \$166 million of loss on disposal of property, plant and equipment primarily related to cell site construction

Table of Contents

costs and other network costs that are no longer recoverable as a result of changes in the Company's network plans. In addition, we revised our estimate of a previously recorded reserve, resulting in approximately \$20 million of income.

Other, net reflected an expense of \$413 million in the in the year ended March 31, 2015. Severance and exit costs included \$253 million of severance primarily associated with reductions in work force and \$13 million of lease exit costs primarily associated with tower and cell sites as well as facility closures. In addition, we recognized \$38 million of costs during the period related to payments that will continue to be made under our backhaul access contracts for which we will no longer be receiving any economic benefit. Litigation of \$91 million represented legal reserves for various pending legal suits and proceedings. Partial pension settlement was the result of the Company's Board of Directors approving a plan amendment to the Sprint Retirement Pension Plan (Plan) to offer certain terminated participants, who had not begun to receive Plan benefits, the opportunity to voluntarily elect to receive their benefits as an immediate lump sum distribution. The lump sum distribution created a settlement event that resulted in a \$59 million charge. In addition, we revised our estimate of a previously recorded reserve, resulting in income of approximately \$41 million.

***Interest Expense***

Interest expense increased \$313 million, or 14%, in the year ended March 31, 2017 compared to the same period in 2016 primarily due to interest associated with the Network Equipment Sale-Leaseback, the Handset Sale-Leaseback Tranche 2, the unsecured financing facility and the Spectrum Financing transaction. Interest expense increased \$131 million, or 6%, in the year ended March 31, 2016 compared to same period in 2015 primarily due to interest associated with \$1.5 billion aggregate principal amount of notes issued in February 2015. The effective interest rate, which includes capitalized interest, on the weighted average long-term debt balance of \$37.9 billion, \$33.8 billion and \$32.5 billion was 6.7 % in the year ended March 31, 2017, and 6.5% for years ended March 31, 2016 and 2015, respectively. See "Liquidity and Capital Resources" for more information on the Company's financing activities.

***Other (Expense) Income, Net***

"Other (expense) income, net" represented an expense of \$40 million in the year ended March 31, 2017, and income of \$18 million and \$27 million in the years ended March 31, 2016 and 2015, respectively. The expense in the year ended March 31, 2017 was primarily due to recognizing the remaining debt finance costs of \$74 million associated with the terminated unsecured financing facility, partially offset by interest income of \$59 million which was primarily related to increased short-term investments.

***Income Tax Expense***

The income tax expense of \$435 million and \$141 million, and the benefit of \$574 million for the years ended March 31, 2017, 2016 and 2015, respectively, represented consolidated effective tax rates of approximately (56)%, (8)%, and 15%, respectively. The income tax expense for the year ended March 31, 2017 was primarily attributable to taxable temporary differences from the tax amortization of FCC licenses and tax expense of \$136 million on pre-tax gains from spectrum license exchanges which increased our deferred tax liability on FCC licenses temporary differences. In addition, income tax expense included an expense of \$89 million to increase our state income tax valuation allowance as a result of a shift in operations among wholly-owned subsidiaries and an organizational restructuring that occurred during the year. The income tax expense for the year ended March 31, 2016 was primarily attributable to tax expense resulting from taxable temporary differences from the tax amortization of FCC licenses, partially offset by tax benefits from the reversal of state income tax valuation allowance on deferred tax assets and changes in state income tax laws enacted during the year. The income tax benefit for the year ended March 31, 2015 was primarily attributable to recognition of a tax benefit on the \$1.9 billion Sprint trade name impairment loss, partially offset by tax expense on taxable temporary differences from the tax amortization of FCC licenses for income tax purposes.

**Segment Earnings - Wireless**

Wireless segment earnings are a function of wireless service revenue, the sale of wireless devices (handsets and tablets), broadband devices, connected devices and accessories, leasing wireless devices, in addition to costs to acquire subscribers and network and interconnection costs to serve those subscribers, as well as other Wireless segment operating expenses. The costs to acquire our subscribers include the cost at which we sell our devices, as well as the marketing and sales costs incurred to attract those subscribers. Network costs primarily represent switch and cell site costs, backhaul costs, and interconnection costs, which generally consist of per-minute usage fees and roaming fees paid to other carriers. The remaining costs associated with operating the Wireless segment include the costs to operate our customer care organization and administrative support. Wireless service revenue, costs to acquire subscribers, and variable network and interconnection

Table of Contents

costs fluctuate with the changes in our subscriber base and their related usage, but some cost elements do not fluctuate in the short-term with these changes.

As shown by the table above under "Consolidated Results of Operations," Wireless segment earnings represented almost all of our total consolidated segment earnings for the years ended March 31, 2017, 2016, and 2015. Within the Wireless segment, postpaid wireless services represent the most significant contributors to earnings, and is driven by the number of postpaid subscribers to our services, as well as ARPU. The wireless industry is subject to competition to retain and acquire subscribers of wireless services. Almost all markets in which we operate have high rates of penetration for wireless services.

***Device Financing Programs***

In September 2013, we introduced an installment billing program that allows subscribers to purchase a device by paying monthly installments generally over 24 months. In September 2014, we introduced a leasing program, whereby qualified subscribers can lease a device for a contractual period of time.

Under the installment billing program, we recognize a majority of the revenue associated with future expected installment payments at the time of sale of the device. As compared to our traditional subsidy program, this results in better alignment of the equipment revenue with the cost of the device. The impact to Wireless earnings from the sale of devices under our installment billing program is neutral except for the impact from promotional offers and the time value of money element related to the imputed interest on the installment receivable.

Under the leasing program, qualified subscribers can lease a device for a contractual period of time. At the end of the lease term, the subscriber has the option to turn in their device, continue leasing their device, or purchase the device. As of March 31, 2017, substantially all of our device leases were classified as operating leases. As a result, at lease inception, the devices are reclassified from inventory to property, plant and equipment when leased through Sprint's direct channels. For leases in the indirect channel, we purchase the devices at lease inception from the dealer, which is then capitalized to property, plant and equipment. While a majority of the revenue associated with installment sales is recognized at the time of sale along with the related cost of products, lease revenue is recorded monthly over the term of the lease and the cost of the device is depreciated to its estimated residual value generally over the lease term. During the years ended March 31, 2017, 2016 and 2015, we leased devices through our Sprint direct channels totaling \$2.9 billion, \$3.2 billion and \$1.2 billion, respectively. These devices were reclassified from inventory to property, plant and equipment and, as such, the cost of the device was not recorded as cost of products compared to when purchased under the installment billing or traditional subsidy program, which resulted in a significant positive impact to Wireless segment earnings. Depreciation expense incurred on all leased devices for the years ended March 31, 2017, 2016 and 2015 was \$3.1 billion, \$1.8 billion and \$206 million, respectively. If the mix of leased devices continues to increase, we expect this positive impact on the financial results of Wireless segment earnings to continue and depreciation expense to increase. However, this benefit to Wireless segment earnings was partially offset by the Handset Sale-Leaseback Tranche 1 (Tranche 1) transaction that was consummated in November 2015 whereby we sold and subsequently leased back certain devices leased to our customers (see *Handset Sale-Leaseback Tranche 1* in "Liquidity and Capital Resources" for further details). As a result, the cost to us of the devices sold to Mobile Leasing Solutions, LLC (MLS) was no longer recorded as depreciation expense, but rather recognized as rent expense within "Cost of products" in the consolidated statements of operations during the leaseback periods until Tranche 1 was terminated in conjunction with the repurchase of devices in December 2016.

Our device leasing and installment billing programs require a greater use of operating cash flows in the earlier part of the device contracts as our subscribers will generally pay less upfront than a traditional subsidy program. The Accounts Receivable Facility and the Handset Sale-Leaseback transactions discussed in "Liquidity and Capital Resources" were designed to mitigate the significant use of cash from purchasing devices from original equipment manufacturers (OEMs) to fulfill our installment billing and leasing programs.

***Wireless Segment Earnings Trends***

Sprint offers lower monthly service fees without a traditional contract as an incentive to attract subscribers to certain of our service plans. These lower rates for service are available whether the subscriber brings their own handset, pays the full or near full retail price of the handset, purchases the handset under our installment billing program, or leases their handset through our leasing program. As our base of subscribers shifts away from our traditional subsidy program to lower-priced service plans associated with device financing options, we expect our postpaid ARPU to continue to decline due to lower service revenue. However, we expect higher equipment revenue associated with the installment billing and leasing programs to substantially offset these declines. Since inception, the combination of lower priced plans and our installment

Table of Contents

billing and leasing programs have been accretive to Wireless segment earnings. We expect that trend to continue with the magnitude of the impact depending on subscriber adoption rates.

We began to experience net losses of postpaid handset subscribers in mid-2013. Since the release of our new price plans, results have shown improvement in trends of handset subscribers; however, there can be no assurance that this trend will continue. We have taken initiatives to provide the best value in wireless service while continuing to enhance our network performance, coverage and capacity in order to attract and retain valuable handset subscribers. In addition, we are evaluating our cost model to operationalize a more effective cost structure.

The following table provides an overview of the results of operations of our Wireless segment.

	Year Ended March 31,		
	2017	2016	2015
<b>Wireless Segment Earnings</b>	<i>(in millions)</i>		
Postpaid	\$ 18,677	\$ 19,463	\$ 21,181
Prepaid	4,438	4,986	4,905
Other <sup>(1)</sup>	—	178	458
Retail service revenue	23,115	24,627	26,544
Wholesale, affiliate and other	693	744	793
Total service revenue	23,808	25,371	27,337
Cost of services (exclusive of depreciation and amortization)	(6,674)	(8,069)	(7,945)
Service gross margin	17,134	17,302	19,392
Service gross margin percentage	72%	68%	71%
Equipment revenue	7,979	5,006	4,990
Cost of products (exclusive of depreciation and amortization)	(7,077)	(5,795)	(9,309)
Selling, general and administrative expense	(7,741)	(8,141)	(9,179)
Loss on disposal of property, plant and equipment	(481)	(321)	—
Wireless segment earnings	\$ 9,814	\$ 8,051	\$ 5,894

(1) Represents service revenue primarily related to the acquisition of Clearwire on July 9, 2013.

**Service Revenue**

Our Wireless segment generates service revenue from the sale of wireless services and the sale of wholesale and other services. Service revenue consists of fixed monthly recurring charges, variable usage charges and miscellaneous fees such as activation fees, directory assistance, roaming, equipment protection, late payment and early termination charges, and certain regulatory related fees, net of service credits.

The ability of our Wireless segment to generate service revenue is primarily a function of:

- revenue generated from each subscriber, which in turn is a function of the types and amount of services utilized by each subscriber and the rates charged for those services; and
- the number of subscribers that we serve, which in turn is a function of our ability to retain existing subscribers and acquire new subscribers.

Retail comprises those subscribers to whom Sprint directly provides wireless services, whether those services are provided on a postpaid or a prepaid basis. We also categorize our retail subscribers as prime and subprime based upon subscriber credit profiles. We use proprietary scoring systems that measure the credit quality of our subscribers using several factors, such as credit bureau information, subscriber credit risk scores and service plan characteristics. Payment history is subsequently monitored to further evaluate subscriber credit profiles. Wholesale and affiliates are those subscribers who are served through MVNO and affiliate relationships and other arrangements. Under the MVNO relationships, wireless services are sold by Sprint to other companies that resell those services to subscribers.

Effective January 1, 2017, we entered into a new Master Services Agreement with a vendor to provide post-sale device support services (including device insurance) to subscribers. Under the new agreement, the vendor bears the risk of loss with regards to claims and related costs, which Sprint will no longer incur. Sprint will remit premiums to the vendor who will pay Sprint a monthly recurring commission per subscriber for the duration of the agreement. Additionally, under the terms of the new agreement, the vendor will be the primary obligor in the agreement with the subscriber and, as such, revenue will be accounted for and presented on a net basis, whereas historically the amounts were presented on a gross basis. The change is expected to result in reductions in service revenue of approximately \$700 million in fiscal year 2017. Because

Table of Contents

the vendor, not Sprint, will be fulfilling the services, we expect the reductions in service revenue to be more than offset by greater reductions in cost of services expense.

Year Ended March 31, 2017 compared to Year Ended March 31, 2016

Retail service revenue decreased \$1.5 billion, or 6%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to a lower average revenue per postpaid subscriber driven by an increase in subscribers on lower price plans, combined with a decrease in average prepaid subscribers driven by higher churn and the impact of the shutdown of the Clearwire WiMAX network on March 31, 2016. The decrease was partially offset by an increase in average postpaid subscribers.

Wholesale, affiliate and other revenues decreased \$51 million, or 7%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to a decline in Lifeline and postpaid and prepaid resellers due to competitive pressures combined with the impact of the shutdown of the Clearwire WiMAX network, partially offset by growth in connected devices and an increase in imputed interest associated with installment billing on handsets. Approximately 67% of our total wholesale and affiliate subscribers represent connected devices. These devices generate revenue from usage which varies depending on the solution being utilized.

Year Ended March 31, 2016 compared to Year Ended March 31, 2015

Retail service revenue decreased \$1.9 billion, or 7%, for the year ended March 31, 2016 compared to the year ended March 31, 2015 primarily due to a lower average revenue per subscriber driven by growth in both postpaid subscribers on our new plans and tablet sales. The decrease was partially offset by an increase in average postpaid subscribers mostly due to improved churn.

Wholesale, affiliate and other revenues decreased \$49 million, or 6%, for the year ended March 31, 2016 compared to the year ended March 31, 2015 primarily due to a decline in prepaid resellers and the impact of the shutdown of the Clearwire WiMAX network, partially offset by growth in postpaid resellers and connected devices. Approximately 64% of our total wholesale and affiliate subscribers represent connected devices. These devices generate revenue from usage which varies depending on the solution being utilized.

Average Monthly Service Revenue per Subscriber and Subscriber Trends

The table below summarizes average number of retail subscribers. Additional information about the number of subscribers, net additions (losses) to subscribers, and average rates of monthly postpaid and prepaid subscriber churn for each quarter since the quarter ended March 31, 2014 may be found in the tables on the following pages.

	Year Ended March 31,		
	2017	2016	2015
	<i>(subscribers in thousands)</i>		
Average postpaid subscribers	31,272	30,561	30,068
Average prepaid subscribers	13,204	15,200	15,401
Average retail subscribers	44,476	45,761	45,469

The table below summarizes ARPU. Additional information about ARPU for each quarter since the quarter ended March 31, 2014 may be found in the tables on the following pages.

	Year Ended March 31,		
	2017	2016	2015
ARPU <sup>(1)</sup>			
Postpaid	\$ 49.77	\$ 53.30	\$ 59.32
Prepaid	\$ 28.01	\$ 27.85	\$ 27.81
Average retail	\$ 43.31	\$ 44.85	\$ 48.65

(1) ARPU is calculated by dividing service revenue by the sum of the monthly average number of subscribers in the applicable service category. Changes in average monthly service revenue reflect subscribers for either the postpaid or prepaid service category who change rate plans, the level of voice and data usage, the amount of service credits which are offered to subscribers, plus the net effect of average monthly revenue generated by new subscribers and deactivating subscribers.

Table of ContentsYear Ended March 31, 2017 compared to Year Ended March 31, 2016

Postpaid ARPU for the year ended March 31, 2017 decreased compared to the year ended March 31, 2016 primarily due to the impact of subscriber migration to our service plans associated with device financing options, resulting in lower service fees. We expect Sprint platform postpaid ARPU to continue to decline during fiscal year 2017 as a result of lower service fees associated with our price plans offered in conjunction with device financing options as well as lower device insurance program revenues resulting from entering into a new Master Services Agreement with a vendor to provide post-sale device support services to subscribers. However, as a result of our installment billing and leasing programs, we expect increasing equipment revenues to more than offset these declines. Prepaid ARPU for the year ended March 31, 2017 increased compared to the year ended March 31, 2016 primarily due to the removal of approximately 1.2 million low-engagement prepaid customers from our base as a result of aligning our churn and retention rules across our prepaid brands, excluding Assurance Wireless, late in the three-month period ended December 31, 2016 (See "Subscriber Results" below for more details). With this action, average prepaid subscribers decreased, however prepaid revenue was not proportionally impacted.

Year Ended March 31, 2016 compared to Year Ended March 31, 2015

Postpaid ARPU for the year ended March 31, 2016 decreased compared to the year ended March 31, 2015 primarily due to the impact of subscriber migration to many of our new service plans, resulting in lower service fees, combined with ongoing growth in sales of tablets, which carry a lower revenue per subscriber. Prepaid ARPU for the year ended March 31, 2016 increased compared to the year ended March 31, 2015 primarily due to an increase in average Boost Mobile subscribers which carry a higher ARPU as compared to other prepaid brands, partially offset by the revenue impact of subscribers choosing lower priced plans in both the Boost Mobile and Virgin Mobile brands due to increased competition combined with a decrease in average Virgin Mobile subscribers.

Table of Contents

The following table shows (a) net additions (losses) of wireless subscribers, (b) our total subscribers, and (c) end of period connected device subscribers as of the end of each quarterly period beginning with the quarter ended March 31, 2014.

	March 31, 2014	June 30, 2014	Sept 30, 2014	Dec 31, 2014	March 31, 2015	June 30, 2015	Sept 30, 2015	Dec 31, 2015	March 31, 2016	June 30, 2016	Sept 30, 2016	Dec 31, 2016	March 31, 2017
<b>Net additions (losses) (in thousands)<sup>(1)</sup></b>													
<b>Sprint platform<sup>(2)</sup>:</b>													
Postpaid	(231)	(181)	(272)	30	211	310	378	501	56	180	344	405	(118)
Prepaid	(364)	(542)	35	410	546	(366)	(188)	(491)	(264)	(331)	(427)	(501)	180
Wholesale and affiliates	212	503	827	527	492	731	866	481	655	528	823	673	125
<b>Total Sprint platform</b>	<b>(383)</b>	<b>(220)</b>	<b>590</b>	<b>967</b>	<b>1,249</b>	<b>675</b>	<b>1,056</b>	<b>491</b>	<b>447</b>	<b>377</b>	<b>740</b>	<b>577</b>	<b>187</b>
<b>Transactions:</b>													
Postpaid	(102)	(64)	(64)	(49)	(41)	(60)	(70)	(238)	—	—	—	—	—
Prepaid	(51)	(77)	(55)	(39)	(18)	(66)	(64)	(231)	—	—	—	—	—
Wholesale	69	27	13	13	22	(22)	(12)	(241)	—	—	—	—	—
<b>Total Transactions</b>	<b>(84)</b>	<b>(114)</b>	<b>(106)</b>	<b>(75)</b>	<b>(37)</b>	<b>(148)</b>	<b>(146)</b>	<b>(710)</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>
<b>Total retail postpaid</b>	<b>(333)</b>	<b>(245)</b>	<b>(336)</b>	<b>(19)</b>	<b>170</b>	<b>250</b>	<b>308</b>	<b>263</b>	<b>56</b>	<b>180</b>	<b>344</b>	<b>405</b>	<b>(118)</b>
<b>Total retail prepaid</b>	<b>(415)</b>	<b>(619)</b>	<b>(20)</b>	<b>371</b>	<b>528</b>	<b>(432)</b>	<b>(252)</b>	<b>(722)</b>	<b>(264)</b>	<b>(331)</b>	<b>(427)</b>	<b>(501)</b>	<b>180</b>
<b>Total wholesale and affiliate</b>	<b>281</b>	<b>530</b>	<b>840</b>	<b>540</b>	<b>514</b>	<b>709</b>	<b>854</b>	<b>240</b>	<b>655</b>	<b>528</b>	<b>823</b>	<b>673</b>	<b>125</b>
<b>Total Wireless</b>	<b>(467)</b>	<b>(334)</b>	<b>484</b>	<b>892</b>	<b>1,212</b>	<b>527</b>	<b>910</b>	<b>(219)</b>	<b>447</b>	<b>377</b>	<b>740</b>	<b>577</b>	<b>187</b>
<b>End of period subscribers (in thousands)<sup>(3)</sup></b>													
<b>Sprint platform<sup>(2)</sup>:</b>													
Postpaid <sup>(3)(4)</sup>	29,918	29,737	29,465	29,495	29,706	30,016	30,394	30,895	30,951	30,945	31,289	31,694	31,576
Prepaid <sup>(3)(5)</sup>	15,257	14,715	14,750	15,160	15,706	15,340	15,152	14,661	14,397	13,974	13,547	11,812	11,992
Wholesale and affiliates <sup>(3)(4)(5)(6)</sup>	8,376	8,879	9,706	10,233	10,725	11,456	12,322	12,803	13,458	14,534	15,357	16,009	16,134
<b>Total Sprint platform</b>	<b>53,551</b>	<b>53,331</b>	<b>53,921</b>	<b>54,888</b>	<b>56,137</b>	<b>56,812</b>	<b>57,868</b>	<b>58,559</b>	<b>58,806</b>	<b>59,453</b>	<b>60,193</b>	<b>59,515</b>	<b>59,702</b>
<b>Transactions<sup>(7)</sup>:</b>													
Postpaid	586	522	458	409	368	308	238	—	—	—	—	—	—
Prepaid	550	473	418	379	361	295	231	—	—	—	—	—	—
Wholesale	200	227	240	253	275	253	241	—	—	—	—	—	—
<b>Total Transactions</b>	<b>1,336</b>	<b>1,222</b>	<b>1,116</b>	<b>1,041</b>	<b>1,004</b>	<b>856</b>	<b>710</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>
<b>Total retail postpaid<sup>(3)(4)</sup></b>	<b>30,504</b>	<b>30,259</b>	<b>29,923</b>	<b>29,904</b>	<b>30,074</b>	<b>30,324</b>	<b>30,632</b>	<b>30,895</b>	<b>30,951</b>	<b>30,945</b>	<b>31,289</b>	<b>31,694</b>	<b>31,576</b>
<b>Total retail prepaid<sup>(3)</sup></b>	<b>15,807</b>	<b>15,188</b>	<b>15,168</b>	<b>15,539</b>	<b>16,067</b>	<b>15,635</b>	<b>15,383</b>	<b>14,661</b>	<b>14,397</b>	<b>13,974</b>	<b>13,547</b>	<b>11,812</b>	<b>11,992</b>
<b>Total wholesale and affiliates<sup>(3)(4)(5)(6)</sup></b>	<b>8,576</b>	<b>9,106</b>	<b>9,946</b>	<b>10,486</b>	<b>11,000</b>	<b>11,709</b>	<b>12,563</b>	<b>12,803</b>	<b>13,458</b>	<b>14,534</b>	<b>15,357</b>	<b>16,009</b>	<b>16,134</b>
<b>Total Wireless</b>	<b>54,887</b>	<b>54,553</b>	<b>55,037</b>	<b>55,929</b>	<b>57,141</b>	<b>57,668</b>	<b>58,578</b>	<b>58,359</b>	<b>58,806</b>	<b>59,453</b>	<b>60,193</b>	<b>59,515</b>	<b>59,702</b>



## Table of Contents

	March 31, 2014	June 30, 2014	Sept 30, 2014	Dec 31, 2014	March 31, 2015	June 30, 2015	Sept 30, 2015	Dec 31, 2015	March 31, 2016	June 30, 2016	Sept 30, 2016	Dec 31, 2016	March 31, 2017
<b>Supplemental data - connected devices</b>													
<b>End of period subscribers (in thousands)<sup>(1)</sup></b>													
Retail postpaid	968	988	1,039	1,180	1,320	1,439	1,576	1,676	1,771	1,822	1,874	1,960	2,001
Wholesale and affiliates	3,882	4,192	4,635	5,175	5,832	6,620	7,338	7,930	8,575	9,244	9,951	10,594	10,880
Total	4,850	5,180	5,674	6,355	7,152	8,059	8,914	9,606	10,346	11,066	11,825	12,554	12,881

- (1) A subscriber is defined as an individual line of service associated with each device activated by a customer. Subscribers that transfer from their original service category classification to another platform, or another service line within the same platform, are reflected as a net loss to the original service category and a net addition to their new service category. There is no net effect for such subscriber changes to the total wireless net additions (losses) or end of period subscribers.
- (2) Sprint platform refers to the Sprint network that supports the wireless service we provide through our multiple brands.
- (3) As part of the Shentel transaction, 186,000 and 92,000 subscribers were transferred from postpaid and prepaid, respectively, to affiliates. An additional 270,000 of nTelos' subscribers are now part of our affiliate relationship with Shentel and are being reported in wholesale and affiliate subscribers during the quarter ended June 30, 2016.
- (4) End of period connected devices are included in retail postpaid or wholesale and affiliates end of period subscriber totals for all periods presented.
- (5) During the three-month period ended December 31, 2016, the Company aligned all prepaid brands, excluding Assurance Wireless but including prepaid affiliate subscribers, under one churn and retention program. As a result of this change, end of period prepaid and affiliate subscribers as of December 31, 2016 were reduced by 1,234,000 and 21,000, respectively. See "Subscriber Results" below for more information.
- (6) Subscribers through some of our MVNO relationships have inactivity either in voice usage or primarily as a result of the nature of the device, where activity only occurs when data retrieval is initiated by the end-user and may occur infrequently. Although we continue to provide these subscribers access to our network through our MVNO relationships, approximately 2,054,000 subscribers at March 31, 2017 through these MVNO relationships have been inactive for at least six months, with no associated revenue during the six-month period ended March 31, 2017.
- (7) End of period transactions subscribers reflected postpaid, prepaid and wholesale subscribers acquired as a result of the acquisition of Clearwire. We had no remaining transaction subscribers primarily due to the shutdown of the WiMAX network on March 31, 2016.

The following table shows our average rates of monthly postpaid and prepaid subscriber churn as of the end of each quarterly period beginning with the quarter ended March 31, 2014.

	March 31, 2014	June 30, 2014	Sept 30, 2014	Dec 31, 2014	March 31, 2015	June 30, 2015	Sept 30, 2015	Dec 31, 2015	March 31, 2016	June 30, 2016	Sept 30, 2016	Dec 31, 2016	March 31, 2017
<b>Monthly subscriber churn rate<sup>(1)</sup></b>													
<b>Sprint platform:</b>													
Postpaid	2.11%	2.05%	2.18%	2.30%	1.84%	1.56%	1.54%	1.62%	1.72%	1.56%	1.52%	1.67%	1.75%
Prepaid <sup>(2)</sup>	4.33%	4.44%	3.76%	3.94%	3.84%	5.08%	5.06%	5.82%	5.65%	5.55%	5.63%	5.80%	4.99%
<b>Transactions<sup>(3)</sup>:</b>													
Postpaid	5.48%	4.15%	4.66%	4.09%	3.87%	6.07%	8.55%	NM	NM	NM	NM	NM	NM
Prepaid	5.11%	6.28%	5.70%	4.95%	3.77%	7.23%	8.51%	NM	NM	NM	NM	NM	NM
Total retail postpaid	2.18%	2.09%	2.22%	2.33%	1.87%	1.61%	1.61%	1.87%	1.72%	1.56%	1.52%	1.67%	1.75%
Total retail prepaid	4.35%	4.50%	3.81%	3.97%	3.84%	5.13%	5.12%	6.29%	5.65%	5.55%	5.63%	5.80%	4.99%

- (1) Churn is calculated by dividing net subscriber deactivations for the quarter by the sum of the average number of subscribers for each month in the quarter. For postpaid accounts comprising multiple subscribers, such as family plans and enterprise accounts, net deactivations are defined as deactivations in excess of subscriber activations in a particular account within 30 days. Postpaid and Prepaid churn consist of both voluntary churn, where the subscriber makes his or her own determination to cease being a subscriber, and involuntary churn, where the subscriber's service is terminated due to a lack of payment or other reasons.
- (2) In the quarter ended June 30, 2015, the Company revised its prepaid subscriber reporting to remove one of its rules that matches customers who disconnect and then re-engage within a specified period of time. This enhancement, which we believe represents a more precise churn calculation, had no impact on net additions, but did result in reporting higher deactivations and higher gross additions in the quarter. Without this revision, Sprint platform prepaid churn in the quarter would have been 4.33% and relatively flat compared to the same period in 2014. End of period prepaid subscribers and net prepaid subscriber additions for all periods presented were not impacted by the change.
- (3) Subscriber churn related to the acquisition of Clearwire.

Table of Contents

The following table shows our postpaid and prepaid ARPU as of the end of each quarterly period beginning with the quarter ended March 31, 2014.

	March 31, 2014	June 30, 2014	Sept 30, 2014	Dec 31, 2014	March 31, 2015	June 30, 2015	Sept 30, 2015	Dec 31, 2015	March 31, 2016	June 30, 2016	Sept 30, 2016	Dec 31, 2016	March 31, 2017
<b>ARPU</b>													
Sprint platform:													
Postpaid	\$ 63.52	\$62.07	\$60.58	\$58.90	\$56.94	\$55.48	\$53.99	\$52.48	\$ 51.68	\$51.54	\$50.54	\$49.70	\$ 47.34
Prepaid	\$ 26.45	\$27.38	\$27.19	\$27.12	\$27.50	\$27.81	\$27.66	\$27.44	\$ 27.72	\$27.34	\$27.31	\$27.61	\$ 30.08
Transactions <sup>(1)</sup>													
Postpaid	\$ 37.26	\$39.16	\$39.69	\$39.85	\$40.28	\$40.47	\$40.62	\$31.62	\$ —	\$ —	\$ —	\$ —	\$ —
Prepaid	\$ 43.80	\$45.15	\$45.52	\$45.80	\$46.68	\$46.10	\$45.82	\$34.61	\$ —	\$ —	\$ —	\$ —	\$ —
Total retail postpaid	\$ 62.98	\$61.65	\$60.24	\$58.63	\$56.72	\$55.31	\$53.87	\$52.41	\$ 51.68	\$51.54	\$50.54	\$49.70	\$ 47.34
Total retail prepaid	\$ 27.07	\$27.97	\$27.73	\$27.61	\$27.95	\$28.18	\$27.97	\$27.49	\$ 27.72	\$27.34	\$27.31	\$27.61	\$ 30.08

(1) Subscriber ARPU related to the acquisition of Clearwire.

Table of Contents**Subscriber Results***Sprint Platform Subscribers*

**Retail Postpaid** — During the year ended March 31, 2017, net postpaid subscriber additions were 811,000 compared to net additions of 1,245,000 and net losses of 212,000 in the years ended March 31, 2016 and 2015, respectively, inclusive of tablet net losses of 281,000, net additions of 545,000 and 1,334,000, respectively, which generally have a significantly lower ARPU as compared to other wireless subscribers. The primary driver for the net additions in the years ended March 31, 2017 and 2016 was our pricing plan promotions launched during the year combined with improvement in churn as subscribers benefit from the improved network quality. The primary driver for the net losses in the year ended March 31, 2015 was an increase in churn, primarily due to increased competition and network-related churn impacted by our network modernization program. Aggressive marketing efforts by other wireless carriers, including price reductions, to incent subscribers to switch carriers also negatively impact churn, which has a negative effect on earnings.

**Retail Prepaid** — During the year ended March 31, 2017, we lost 1,079,000 net prepaid subscribers compared to losing 1,309,000 and adding 449,000 net prepaid subscribers in the years ended March 31, 2016 and 2015, respectively. The net losses in the year ended March 31, 2017 were primarily due to subscriber losses across all prepaid brands due to continued competition in the market. The net losses in the year ended March 31, 2016 were primarily due to subscriber losses in the Virgin Mobile prepaid brand primarily due to increasing competition. Net additions in the year ended March 31, 2015 were primarily due to subscriber growth in our Boost Mobile brand as a result of new promotions in our indirect channels, partially offset by subscriber losses in the Virgin Mobile prepaid brands primarily due to continued competition.

Historically, prepaid subscribers were generally deactivated between 60 and 150 days from the later of the date of initial activation or replenishment; however, prior to account deactivation, targeted retention programs can be offered to qualifying subscribers to maintain ongoing service by providing up to an additional 150 days to make a replenishment. At September 30, 2016, each of our prepaid brands had different churn rules and retention programs. As a part of our ongoing efforts to simplify and drive consistency across our prepaid business, as well as tighten the customer engagement criteria, we have aligned all prepaid brands, excluding Assurance Wireless, under one churn and retention program as of December 31, 2016. Therefore, all prepaid and prepaid affiliate subscribers, excluding Assurance Wireless, are now deactivated 60 days from the later of the date of initial activation or the most recent replenishment date. As a result of these changes, we have approximately 1.2 million fewer prepaid subscribers and 21,000 fewer prepaid affiliate subscribers in the base as of December 31, 2016. However, because we have deactivated customers with no engagement, we do not expect a material impact to future prepaid revenue. If these changes had been implemented for our prepaid subscriber base at the beginning of the December 31, 2016 quarter rather than the end, and thus been in effect for the entire three-month period, we estimate churn would have been 5.84% versus 5.80% and ARPU would have been \$30.11 versus \$27.61.

**Wholesale and Affiliate Subscribers** — Wholesale and affiliate subscribers represent customers that are served on our networks through companies that resell our wireless services to their subscribers, customers residing in affiliate territories and connected devices that utilize our network. Of the 16.1 million Sprint Platform subscribers included in wholesale and affiliates, approximately 67% represent connected devices. Wholesale and affiliate subscriber net additions were 2,149,000 during the year ended March 31, 2017, compared to 2,733,000 and 2,349,000 during the years ended March 31, 2016 and 2015, respectively, inclusive of net additions of connected devices totaling 2,305,000, 2,743,000 and 1,950,000, respectively. The driver for net additions in the years ended March 31, 2017, 2016 and 2015 is primarily attributable to growth in connected devices.

*Transactions Subscribers*

As part of the acquisition of Clearwire in July 2013, we acquired 788,000 postpaid subscribers (exclusive of Sprint platform wholesale subscribers acquired through our MVNO relationship with Clearwire that were transferred to postpaid subscribers within Transactions), 721,000 prepaid subscribers, and 93,000 wholesale subscribers. We have no remaining transaction subscribers primarily due to the shutdown of the WiMAX network on March 31, 2016.

*Cost of Services*

Cost of services consists primarily of:

- costs to operate and maintain our networks, including direct switch and cell site costs, such as rent, utilities, maintenance, labor costs associated with network employees, and spectrum frequency leasing costs;
- fixed and variable interconnection costs, the fixed component of which consists of monthly flat-rate fees for facilities leased from local exchange carriers and other providers based on the number of cell sites and

Table of Contents

switches in service in a particular period and the related equipment installed at each site, and the variable component of which generally consists of per-minute use fees charged by wireline providers for calls terminating on their networks, which fluctuate in relation to the level and duration of those terminating calls;

- long distance costs paid to the Wireline segment;
- costs to service and repair devices;
- regulatory fees;
- roaming fees paid to other carriers; and
- fixed and variable costs relating to payments to third parties for the subscriber use of their proprietary data applications, such as messaging, music and cloud services and connected vehicle fees.

Year Ended March 31, 2017 compared to Year Ended March 31, 2016

Cost of services decreased \$1.4 billion, or 17%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to decreases in network costs such as rent, utilities, backhaul and labor associated with our network improvements and the shutdown of the WiMAX network on March 31, 2016, combined with decreases in roaming and interconnection costs primarily due to lower rates.

Year Ended March 31, 2016 compared to Year Ended March 31, 2015

Cost of services increased \$124 million, or 2%, for the year ended March 31, 2016 compared to the year ended March 31, 2015 primarily due to increased service and repair costs as a result of higher costs per unit of new and used devices. These increases were partially offset by decreases in roaming costs primarily due to lower rates.

***Equipment Revenue and Cost of Products***

We recognize equipment revenue and corresponding costs of devices when title and risk of loss passes to the indirect dealer or end-use subscriber, assuming all other revenue recognition criteria are met. Our devices are sold under the subsidy program and the installment billing program. Under the subsidy program, we offer certain incentives to retain and acquire subscribers such as new devices at discounted prices. The cost of these incentives is recorded as a reduction to equipment revenue upon activation of the device with a service contract. Under the installment billing program, the device is generally sold at or near full retail price and we recognize most of the future expected installment payments at the time of sale of the device.

Cost of products includes equipment costs (primarily devices and accessories), order fulfillment related expenses, and write-downs of device and accessory inventory related to shrinkage and obsolescence. Additionally, cost of products is reduced by any rebates that are earned from the equipment manufacturers. Cost of products in excess of the net revenue generated from equipment sales is referred to in the industry as equipment net subsidy. As subscribers migrate from acquiring devices through our subsidy program to installment billing or choose to lease under our leasing program, equipment net subsidy continues to decline. We also make incentive payments to certain indirect dealers who purchase devices directly from OEMs or other device distributors. Those payments are recognized as selling, general and administrative expenses when the device is activated with a Sprint service plan because Sprint does not recognize any equipment revenue or cost of products for those transactions. (See *Selling, General and Administrative Expense* below.)

The net impact to equipment revenue and cost of products from the sale of devices under our installment billing program is relatively neutral except for the impact from promotional offers and the time value of money element related to the imputed interest on the installment receivables. Under the leasing program, lease revenue is recorded over the term of the lease. The cost of the leased device is depreciated to its estimated residual value generally over the lease term. During the years ended March 31, 2017, 2016 and 2015, we leased devices through our Sprint direct channels totaling \$2.9 billion, \$3.2 billion and \$1.2 billion, respectively, which were reclassified from inventory to property, plant and equipment and, as such, the cost of the device was not recorded as cost of products compared to when purchased under the installment billing or traditional subsidy programs.

Year Ended March 31, 2017 compared to Year Ended March 31, 2016

Equipment revenue increased \$3.0 billion, or 59%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to higher revenue from the leasing program as more subscribers are choosing to lease their device, combined with an increase in the installment billing mix of sales, and an increase in the volume of used postpaid devices sold to third parties. Cost of products increased \$1.3 billion, or 22%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to an increase in the volume of used devices sold to third parties, combined with an increase in the installment billing mix of sales, partially offset by a decrease in prepaid devices sold.

Table of ContentsYear Ended March 31, 2016 compared to Year Ended March 31, 2015

Equipment revenue increased \$16 million, or remained relatively flat, and cost of products decreased \$3.5 billion, or 38%, for the year ended March 31, 2016 compared to the year ended March 31, 2015 primarily due to a higher average sales price per postpaid handset sold, partially offset by a decrease in postpaid handsets sold as a result of Brightstar Corp. (Brightstar) purchasing inventory from the OEMs to sell directly to our indirect dealers and more subscribers choosing to lease devices instead of purchasing them, combined with lower average sales price per prepaid handset sold. Cost of products also decreased due to a decrease in postpaid handsets sold as a result of Brightstar purchasing inventory from the OEMs to sell directly to our indirect dealers and subscribers choosing to lease devices instead of purchasing them.

*Selling, General and Administrative Expense*

Sales and marketing costs primarily consist of subscriber acquisition costs, including commissions paid to our indirect dealers, third-party distributors and retail sales force for new device activations and upgrades, residual payments to our indirect dealers, commission payments made to OEMs or other device distributors for direct source handsets, payroll and facilities costs associated with our retail sales force, marketing employees, advertising, media programs and sponsorships, including costs related to branding. General and administrative expenses primarily consist of costs for billing, customer care and information technology operations, bad debt expense and administrative support activities, including collections, legal, finance, human resources, corporate communications, and strategic planning.

Year Ended March 31, 2017 and Year Ended March 31, 2016

Sales and marketing expense decreased \$110 million, or 2%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to lower overall marketing spend as a result of cost reduction initiatives.

General and administrative costs decreased \$290 million, or 9%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to lower customer care and billing costs as a result of cost reduction initiatives, partially offset by higher bad debt expense. Bad debt expense increased \$109 million, or 24%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily related to increased installment billing accounts with higher reserve rates, partially offset by lower service revenue bad debt resulting from an improved aging and lower reserve rates. We reassess our allowance for doubtful accounts quarterly.

Year Ended March 31, 2016 and Year Ended March 31, 2015

Sales and marketing expense decreased \$272 million, or 5%, for the year ended March 31, 2016 compared to the year ended March 31, 2015 primarily due to lower media spend and a decrease in payments to OEMs for direct source handsets as a result of lower volume of device sales, partially offset by higher retail labor costs.

General and administrative costs for the year ended March 31, 2016 decreased \$766 million, or 20%, compared to the year ended March 31, 2015 primarily due to a decrease in bad debt expense combined with declines in other general and administrative expenses due to reduced headcount and other cost-savings initiatives. Bad debt expense decreased \$446 million, or 50%, for the year ended March 31, 2016 compared to the year ended March 31, 2015 primarily related to an improved aging as a result of customer credit profile improvement and fewer accounts written off due to improvements in churn, partially offset by a higher average balance of accounts written off.

*Loss on Disposal of Property, Plant and Equipment*

For the years ended March 31, 2017 and 2016, loss on disposal of property, plant and equipment, net of recoveries, of \$481 million and \$256 million, respectively, resulted from the write-off of leased devices associated with lease cancellations prior to their scheduled customer lease terms where customers did not return the devices to us. If customers continue to not return devices, we may have material losses in future periods. Similar charges are and have been incurred for devices sold under our subsidy program as equipment net subsidy. In addition, for the year ended March 31, 2016, \$65 million in net losses was recognized upon the sale of devices to MLS under the Tranche 1 transaction, which represented the difference between the fair value and net book value of the devices sold.

**Segment Earnings - Wireline**

We provide a broad suite of wireline voice and data communications services to other communications companies and targeted business subscribers. In addition, we provide voice, data and IP communication services to our Wireless segment. We provide long distance services and operate all-digital global long distance and Tier 1 IP networks. Our services and products include domestic and international data communications using various protocols such as multiprotocol label switching technologies (MPLS), IP, managed network services, Voice over Internet Protocol (VoIP), Session Initiated Protocol (SIP), and traditional voice services. Our IP services can also be combined with wireless services. Such services

Table of Contents

include our Sprint Mobile Integration service, which enables a wireless handset to operate as part of a subscriber's wireline voice network, and our DataLink<sup>SM</sup> service, which uses our wireless networks to connect a subscriber location into their primarily wireline wide-area IP/MPLS data network, making it easy for businesses to adapt their network to changing business requirements. In addition to providing services to our business customers, the wireline network is carrying increasing amounts of voice and data traffic for our Wireless segment as a result of growing usage by our wireless subscribers.

We continue to assess the portfolio of services provided by our Wireline business and are focusing our efforts on IP-based data services and de-emphasizing stand-alone voice services and non-IP-based data services. However, we continue to provide stand-alone voice services primarily to business customers. Our Wireline segment markets and sells its services primarily through direct sales representatives.

Wireline segment earnings are primarily a function of wireline service revenue, network and interconnection costs, and other Wireline segment operating expenses. Network costs primarily represent special access costs and interconnection costs, which generally consist of domestic and international per-minute usage fees paid to other carriers. The remaining costs associated with operating the Wireline segment include the costs to operate our customer care and billing organizations in addition to administrative support. Wireline service revenue and variable network and interconnection costs fluctuate with the changes in our customer base and their related usage, but some cost elements do not fluctuate in the short-term with the changes in our customer usage. Our wireline services provided to our Wireless segment are generally accounted for based on market rates, which we believe approximate fair value. The Company generally re-establishes these rates at the beginning of each fiscal year. Over the past several years, there has been an industry wide trend of lower rates due to increased competition from other wireline and wireless communications companies as well as cable and Internet service providers. Declines in wireline segment earnings related to intercompany pricing rates do not affect our consolidated results of operations as our Wireless segment benefits from an equivalent reduction in cost of service.

The following table provides an overview of the results of operations of our Wireline segment.

<u>Wireline Segment Earnings</u>	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Voice	\$ 649	\$ 840	\$ 1,174
Data	166	171	213
Internet	1,147	1,284	1,353
Other	81	87	74
Total net service revenue	2,043	2,382	2,814
Cost of services	(1,686)	(1,962)	(2,338)
Service gross margin	357	420	476
Service gross margin percentage	17%	18%	17%
Selling, general and administrative expense	(238)	(328)	(363)
Wireline segment earnings	\$ 119	\$ 92	\$ 113

**Wireline Revenue**Year Ended March 31, 2017 compared to Year Ended March 31, 2016*Voice Revenues*

Voice revenues for the year ended March 31, 2017 decreased \$191 million, or 23%, compared to the year ended March 31, 2016. The decrease was primarily driven by lower volume and overall rate declines due to lower international hubbing volumes as the Company continues to de-emphasize voice services, combined with the decline in prices for the sale of services to our Wireless segment. Voice revenues generated from the sale of services to our Wireless segment represented 38% of total voice revenues for the year ended March 31, 2017 compared to 39% in the year ended March 31, 2016.

*Data Revenues*

Data revenues reflect sales of data services, primarily Private Line and managed network services bundled with non-IP-based data access. Data revenues decreased \$5 million, or 3%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 as a result of customer churn, primarily related to Private Line. Data revenues generated from the provision of services to the Wireless segment represented 54% of total data revenue for each of the year ended March 31, 2017 compared to 40% in the year ended March 31, 2016.

Table of Contents*Internet Revenue*

IP-based data services revenue reflects sales of Internet services, including MPLS, VoIP, SIP, and managed services bundled with IP-based data access. IP-based data services decreased \$137 million, or 11%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to fewer IP customers. In addition, revenue was also impacted by a decline in prices for the sale of services to our Wireless segment. Sale of services to our Wireless segment represented 14% of total Internet revenues for the year ended March 31, 2017 compared to 15% in the year ended March 31, 2016.

*Other Revenues*

Other revenues, which primarily consist of sales of customer premises equipment, decreased \$6 million, or 7%, for the year ended March 31, 2017 compared to the year ended March 31, 2016.

*Year Ended March 31, 2016 compared to Year Ended March 31, 2015**Voice Revenues*

Voice revenues for the year ended March 31, 2016 decreased \$334 million, or 28%, compared to the year ended March 31, 2015. The decrease was primarily driven by lower volume and overall rate declines due to lower international hubbing volumes, combined with the decline in prices for the sale of services to our Wireless segment. Voice revenues generated from the sale of services to our Wireless segment represented 39% of total voice revenues for the year ended March 31, 2016 compared to 31% in the year ended March 31, 2015.

*Data Revenues*

Data revenues reflect sales of data services, primarily Private Line and managed network services bundled with non-IP-based data access. Data revenues decreased \$42 million, or 20%, for the year ended March 31, 2016 compared to the year ended March 31, 2015 as a result of customer churn, primarily related to Private Line. Data revenues generated from the provision of services to the Wireless segment represented 40% of total data revenue for the year ended March 31, 2016 compared to 41% in the year ended March 31, 2015.

*Internet Revenue*

IP-based data services revenue reflects sales of Internet services, including MPLS, VoIP, SIP, and managed services bundled with IP-based data access. IP-based data services decreased \$69 million, or 5%, for the year ended March 31, 2016 compared to the year ended March 31, 2015 primarily due to fewer IP customers. In addition, revenue was also impacted by a decline in the price of services sold to our Wireless segment. Sale of services to our Wireless segment represented 15% of total Internet revenues for the year ended March 31, 2016 compared to 12% in the year ended March 31, 2015.

*Other Revenues*

Other revenues, which primarily consist of sales of customer premises equipment, increased \$13 million, or 18%, for the year ended March 31, 2016 compared to the year ended March 31, 2015.

*Costs of Services*

Costs of services include access costs paid to local phone companies, other domestic service providers and foreign phone companies to complete calls made by our domestic subscribers, costs to operate and maintain our networks, and costs of customer premise equipment.

*Year Ended March 31, 2017 compared to Year Ended March 31, 2016*

Costs of services decreased \$276 million, or 14%, for the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to lower international voice volume and rates, combined with lower access expense as the result of savings initiatives and declining voice and IP rate and volumes. Service gross margin percentage decreased from 18% in the year ended March 31, 2016 to 17% in the year ended March 31, 2017.

*Year Ended March 31, 2016 compared to Year Ended March 31, 2015*

Costs of services increased \$376 million, or 16%, for the year ended March 31, 2016 compared to the year ended March 31, 2015 primarily due to international voice volume and rates, combined with lower access expense as the result of savings initiatives and declining voice and IP rate and volumes. Service gross margin percentage increased from 17% in the year ended March 31, 2015 to 18% in the year ended March 31, 2016.

Table of Contents***Selling, General and Administrative Expense******Year Ended March 31, 2017 compared to Year Ended March 31, 2016***

Selling, general and administrative expense decreased \$90 million, or 27%, in the year ended March 31, 2017 compared to the year ended March 31, 2016 primarily due to a decrease in shared administrative and employee-related costs required to support the Wireline segment as a result of the decline in revenue. Total selling, general and administrative expense as a percentage of net services revenue was 12% in the year ended March 31, 2017 compared to 14% in the year ended March 31, 2016.

***Year Ended March 31, 2016 compared to Year Ended March 31, 2015***

Selling, general and administrative expense decreased \$35 million, or 10%, in the year ended March 31, 2016 compared to the year ended March 31, 2015 primarily due to a decrease in shared administrative and employee-related costs required to support the Wireline segment as a result of the decline in revenue. Total selling, general and administrative expense as a percentage of net services revenue was 14% in the year ended March 31, 2016 compared to 13% in the year ended March 31, 2015.

**LIQUIDITY AND CAPITAL RESOURCES****Cash Flow**

	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Net cash provided by operating activities	\$ 4,168	\$ 3,897	\$ 2,450
Net cash used in investing activities	\$ (9,225)	\$ (5,735)	\$ (4,714)
Net cash provided by financing activities	\$ 5,286	\$ 469	\$ 1,304

***Operating Activities***

Net cash provided by operating activities of \$4.2 billion in the year ended March 31, 2017 increased \$271 million from the same period in 2016. This increase was primarily due to lower vendor and labor-related payments of \$1.6 billion, which were primarily due to reduced operating costs resulting from the Company's ongoing cost reduction initiatives, partially offset by \$1.1 billion of decreased cash received from customers primarily due to lower net advances on our Accounts Receivable Facility (Receivables Facility) prior to the February 2017 amendment, as described below in *Accounts Receivable Facility*. Also, during the year ended March 31, 2017, we had increased interest payments of \$254 million primarily due to the Network Equipment Sale-Leaseback, the unsecured financing facility, the Spectrum Financing transaction and the Receivables Facility.

Net cash provided by operating activities of \$3.9 billion in the year ended March 31, 2016 increased \$1.4 billion from the same period in 2015. This increase was due to lower vendor and labor-related payments of \$2.2 billion, which were primarily due to reduced operating costs, partially offset by reduced cash received from customers of \$669 million. The reduction in cash received from customers was driven by the \$2.4 billion decrease in net operating revenues primarily due to lower average revenue per subscriber, which was offset by the \$1.5 billion increase in operating cash flows resulting from the net changes in accounts and notes receivables and DPP during the year ended March 31, 2016 compared to the same period in 2015. In addition, we had increased interest payments of \$125 million primarily associated with \$1.5 billion aggregate principal amount of notes issued in February 2015.

***Investing Activities***

Net cash used in investing activities in the year ended March 31, 2017 increased by \$3.5 billion compared to the same period in 2016 primarily due to increased net purchases of short-term investments of \$5.6 billion. This increase was offset by decreased network and other capital expenditures of approximately \$2.7 billion and decreased purchases of \$844 million of leased devices from indirect dealers. The decreased purchases of leased devices from indirect dealers was partially offset by \$477 million of repurchased devices due to the termination of the Handset Sale-Leaseback Tranche 1.

Net cash used in investing activities in the year ended March 31, 2016 increased by approximately \$1.0 billion compared to the same period in 2015 primarily due to increased purchases of \$1.7 billion of leased devices from indirect dealers and decreased net proceeds from sales and maturities of short-term investments of \$2.7 billion. These increases were partially offset by \$1.1 billion of proceeds from MLS under the Handset Sale-Leaseback Tranche 1 transaction, \$1.8 billion in decreased purchases of short-term investments and decreased network and other capital expenditures of \$742 million.

Table of Contents***Financing Activities***

Net cash provided by financing activities was \$5.3 billion during the year ended March 31, 2017, which was primarily due to cash receipts of \$2.2 billion, \$1.1 billion, \$3.5 billion and \$4.0 billion from the Network Equipment Sale-Leaseback, Handset Sale-Leaseback Tranche 2, Spectrum Financing and the secured term loan, respectively. These receipts were partially offset by repayments of \$654 million, \$375 million, \$300 million and \$416 million for the Handset Sale-Leaseback Tranche 2, secured equipment credit facilities, Network Equipment Sale-Leaseback and Receivables Facility, respectively. We also retired \$2.0 billion in principal amount of Sprint Communications, Inc. 6% senior notes due 2016, \$1.0 billion in principal amount of Sprint Communications, Inc. 9.125% senior notes due 2017, \$300 million principal amount of Clearwire Communications LLC 14.75% secured notes due 2016, and repaid \$250 million of the EDC credit facility. In addition, we paid a total of \$358 million in debt finance costs for the unsecured financing facility, Network Equipment Sale-Leaseback, Spectrum Financing transaction, the secured term loan and secured revolving bank credit facility.

Net cash provided by financing activities was \$469 million during the year ended March 31, 2016, which was primarily due to sales of future lease receivables through our accounts receivables facility of \$600 million and draws of \$208 million, \$266 million and \$32 million on our Finnvera plc (Finnvera), K-sure and Delcredere | Ducroire (D/D) secured equipment credit facilities, respectively and a \$250 million draw on the Export Development Canada (EDC) credit facility. These draws were partially offset by repayments related to our secured equipment credit facilities of \$315 million, capital lease repayments of \$84 million, and a \$500 million repayment of the EDC credit facility.

Net cash provided by financing activities was \$1.3 billion during the year ended March 31, 2015, which was primarily due to the February 24, 2015 issuance of \$1.5 billion aggregate principal amount of 7.625% notes due 2025. In addition, we amended our unsecured Export Development Canada (EDC) agreement to, among other things, add an additional tranche totaling \$300 million due 2019, which was fully drawn as of March 31, 2015. These were partially offset by principal payments on the iPCS, Inc. Second Lien Secured Floating Rate Notes due 2014 of approximately \$181 million and scheduled principal payments on our secured equipment credit facilities of approximately \$282 million.

***Working Capital***

We had working capital of \$1.7 billion as of March 31, 2017 and negative working capital of \$5.1 billion as of March 31, 2016. The change in working capital was primarily the result of \$5.3 billion of net cash provided by financing activities as described above. In addition, the February 2017 amendment to the Receivables Facility, as described below in *Accounts Receivable Facility*, resulted in the derecognition of the DPP which caused a \$1.2 billion net increase to working capital. The remaining balance was due to changes to other working capital items.

**Long-Term Debt, Other Funding Sources and Scheduled Maturities**

Our device leasing and installment billing programs require a greater use of operating cash flows in the earlier part of the device contracts as our subscribers will generally pay less upfront than a traditional subsidy program. The Accounts Receivable Facility and the Handset Sale-Leaseback transactions described below were designed in large part to mitigate the significant use of cash from purchasing devices from OEMs to fulfill our installment billing and leasing programs.

***Accounts Receivable Facility******Transaction overview***

Our Receivables Facility provides us the opportunity to sell certain wireless service receivables, installment receivables, and future amounts due from customers who lease certain devices from us to unaffiliated third parties (the Purchasers). The maximum funding limit under the Receivables Facility is \$4.3 billion. While we have the right to decide how much cash to receive from each sale, the maximum amount of cash available to us varies based on a number of factors and currently represents approximately 50% of the total amount of the eligible receivables sold to the Purchasers. As of March 31, 2017, the total amount available to be drawn was \$826 million. The Receivables Facility was amended in November 2016 to, among other things, reallocate the Purchasers' commitments between wireless service, installment and future lease receivables to 33%, 39% and 28%, respectively. The amendment was in response to changing trends in the financing methods selected by customers. In February 2017, the Receivables Facility was amended to extend the maturity date to November 2018. Additionally, Sprint gained effective control over the receivables transferred to the Purchasers by obtaining the right under certain circumstances, to repurchase them. Subsequent to the February 2017 amendment, all proceeds received from the Purchasers in exchange for the transfer of our wireless service and installment receivables are recorded as borrowings and all cash inflows and outflows under the Receivables Facility are reported as financing activities in the consolidated statements of cash flows. As a result of the amendment, there was a non-cash derecognition of the DPP asset totaling \$1.5 billion, along with corresponding increases to "Accounts and notes receivable, net" of \$2.6 billion, "Other

Table of Contents

assets" of \$563 million and "Long-term debt, financing and capital lease obligations" of \$1.7 billion. During the year ended March 31, 2017 and subsequent to the February 2017 amendment, we elected to receive \$100 million of cash and also remitted \$161 million of funds to the Purchasers because the amount of cash proceeds received by us under the facility exceeded the maximum funding limit, which were reported as financing activities in the consolidated statements of cash flows.

Prior to the February 2017 amendment, wireless service and installment receivables sold to the Purchasers were treated as a sale of financial assets and we derecognized these receivables, as well as the related allowances, and recognized the net proceeds received in cash provided by operating activities in the consolidated statements of cash flows. The total proceeds from the sale of these receivables were comprised of a combination of cash and a DPP. The DPP was realized by us upon either the ultimate collection of the underlying receivables sold to the Purchasers or upon Sprint's election to receive additional advances in cash from the Purchasers subject to the total availability under the Receivables Facility. The fees associated with these sales were recognized in "Selling, general and administrative" in the consolidated statements of operations through the date of the February 2017 amendment. Subsequent to the February 2017 amendment, the sale of wireless service and installment receivables are reported as financings, which is consistent with our historical treatment for the sale of future lease receivables, and the associated fees are recognized as "Interest expense" in the consolidated statements of operations.

*Transaction Structure*

Sprint contributes certain wireless service, installment and future lease receivables as well as the associated leased devices to Sprint's wholly-owned consolidated bankruptcy-remote special purpose entities (SPEs). At Sprint's direction, the SPEs have sold, and will continue to sell, wireless service, installment and future lease receivables to Purchasers or to a bank agent on behalf of the Purchasers. Leased devices will remain with the SPEs, once sales are initiated, and continue to be depreciated over their estimated useful life. At March 31, 2017, wireless service and installment receivables contributed to the SPEs and included in "Accounts and notes receivable, net" in the consolidated balance sheets were \$2.9 billion and the long-term portion of installment receivables included in "Other assets" in the consolidated balance sheets was \$569 million. As of March 31, 2017, the net book value of devices contributed to the SPEs was approximately \$3.1 billion.

Each SPE is a separate legal entity with its own separate creditors who will be entitled, prior to and upon the liquidation of the SPE, to be satisfied out of the SPE's assets prior to any assets in the SPE becoming available to Sprint. Accordingly, the assets of the SPE are not available to pay creditors of Sprint or any of its affiliates (other than any other SPE), although collections from these receivables in excess of amounts required to repay the advances, yield and fees of the Purchasers and other creditors of the SPEs may be remitted to Sprint during and after the term of the Receivables Facility.

Sales of eligible receivables by the SPEs generally occur daily and are settled on a monthly basis. Sprint pays a fee for the drawn and undrawn portions of the Receivables Facility. A subsidiary of Sprint services the receivables in exchange for a monthly servicing fee, and Sprint guarantees the performance of the servicing obligations under the Receivables Facility.

*DPP*

Prior to the February 2017 amendment, the DPP was classified as a trading security within "Prepaid expenses and other current assets" in the consolidated balance sheets and was recorded at its estimated fair value. Subsequent to the February 2017 amendment, the Receivables Facility is accounted for as a financing and therefore the DPP is no longer recorded as a separate asset. The DPP related to our wireless service and installment receivables was \$1.2 billion as of March 31, 2016. The fair value of the DPP was estimated using a discounted cash flow model, which relies principally on unobservable inputs such as the nature and credit class of the sold receivables and subscriber payment history, and, for installment receivables sold, the estimated timing of upgrades and upgrade payment amounts for those with upgrade options. Changes in the fair value of the DPP did not have a material impact on our consolidated statements of operations for the years ended March 31, 2017 and 2016.

During the year ended March 31, 2017, prior to the February 2017 amendment, we remitted \$270 million of funds to the Purchasers because the amount of cash proceeds received by us under the facility exceeded the maximum funding limit, which increased the total amount of the DPP due to Sprint. We also elected to receive \$625 million of cash, which decreased the total amount of the DPP due to Sprint. In addition, during the year ended March 31, 2017, prior to the February 2017 amendment, sales of new receivables exceeded cash collections on previously sold receivables such that the DPP increased by \$644 million.

Table of Contents***Handset Sale-Leasebacks***

In December 2015 and May 2016, we sold certain iPhone® devices being leased by our customers to MLS, a company formed by a group of equity investors, including SoftBank Group Corp. (SoftBank), and then subsequently leased the devices back. Under the agreements, Sprint generally maintains the customer leases, continues to collect and record lease revenue from the customer and remits monthly rental payments to MLS during the leaseback periods.

Under the agreements, Sprint contributed the devices and the associated customer leases to wholly-owned consolidated bankruptcy-remote special purpose entities of Sprint (SPE Lessees). The SPE Lessees then sold the devices and transferred certain specified customer lease end rights and obligations, such as the right to receive the proceeds from customers who elect to purchase the device at the end of the customer lease term, to MLS in exchange for a combination of cash and DPP. Settlement for the DPP occurs near the end of the agreement and can be reduced to the extent that MLS experiences a loss on the device (either not returned or sold at an amount less than the expected residual value of the device), but only to the extent of the device's DPP balance. In the event that MLS sells the devices returned from our customers at a price greater than the expected device residual value, Sprint has the potential to share some of the excess proceeds.

The SPE Lessees retain all rights to the underlying customer leases, such as the right to receive the rental payments during the device leaseback period, other than the aforementioned certain specified customer lease end rights. Each SPE Lessee is a separate legal entity with its own separate creditors who will be entitled, prior to and upon the liquidation of the SPE Lessee, to be satisfied out of the SPE Lessee's assets prior to any assets in the SPE Lessee becoming available to Sprint. Accordingly, the assets of the SPE Lessee are not available to pay creditors of Sprint or any of its affiliates. The SPE Lessees are obligated to pay the full monthly rental payments under each device lease to MLS regardless of whether our customers make lease payments on the devices leased to them or whether the customer lease is canceled. Sprint has guaranteed to MLS the performance of the agreements and undertakings of the SPE Lessees under the transaction documents.

***Handset Sale-Leaseback Tranche 1 (Tranche 1)***

In December 2015, Sprint transferred devices with a net book value of approximately \$1.3 billion to MLS in exchange for proceeds totaling \$1.1 billion and a DPP of \$126 million. We recorded the sale, removed the device from our balance sheet, and classified the leasebacks as operating leases. The difference between the fair value and the net book value of the devices sold was recognized as a loss on disposal of property, plant and equipment in the amount of \$65 million and was included in "Other, net" in the consolidated statements of operations for the year ended March 31, 2016. The cash proceeds received in the transaction were reflected as cash provided by investing activities in the consolidated statements of cash flows and payments made to MLS under the leaseback are reflected as "Cost of products" in the consolidated statements of operations. Rent expense related to MLS totaled \$494 million and \$277 million during the years ended March 31, 2017 and 2016, respectively, and is reflected within cash flows from operations. In December 2016, Sprint terminated Tranche 1 by repurchasing the devices and related customer lease end rights and obligations from MLS for consideration of \$375 million of net cash payments and the DPP of \$126 million. As a result of the transaction, Sprint recorded \$477 million of property, plant and equipment, \$16 million of other assets, and was released from certain liabilities. Additionally, the leaseback was canceled and there will be no future rental payments owed to MLS related to Tranche 1. The impact to the consolidated statements of operations as a result of the termination was immaterial.

***Handset Sale-Leaseback Tranche 2 (Tranche 2)***

In May 2016, Sprint transferred devices with a net book value of approximately \$1.3 billion to MLS in exchange for cash proceeds totaling \$1.1 billion and a DPP of \$186 million. Unlike Tranche 1, Tranche 2 was accounted for as a financing. Accordingly, the devices remain in "Property, plant and equipment, net" in the consolidated balance sheets and we continue to depreciate the assets to their estimated residual values over the respective customer lease terms. At March 31, 2017, the net book value of devices transferred to MLS was approximately \$575 million.

The proceeds received are reflected as cash provided by financing activities in the consolidated statements of cash flows and payments made to MLS will be reflected as principal repayments and interest expense. We have elected to account for the financing obligation at fair value. Accordingly, changes in the fair value of the financing obligation are recognized in "Other (expense) income, net" in the consolidated statements of operations over the course of the arrangement.

Tranche 2 primarily includes devices from our iPhone Forever Program, whereas these devices were specifically excluded from Tranche 1. The iPhone Forever Program provides our leasing customers the ability to upgrade their devices and to enter into a new lease agreement, subject to certain conditions, upon Apple's release of a next generation device. Upon a customer exercising their iPhone Forever upgrade right, Sprint has the option to terminate the existing leaseback by immediately remitting all unpaid device leaseback payments and returning the device to MLS. Alternatively, Sprint has the option to transfer the title in the new device to MLS in exchange for the title in the original device (Exchange Option). If

Table of Contents

Sprint elects the Exchange Option, we are required to continue to pay existing device leaseback rental related to the original device, among other requirements.

To address the introduction of the upgrade feature into the sale-leaseback structure, among other factors, numerous contractual terms from Tranche 1 were modified, which shifted certain risks of ownership in the devices away from MLS to Sprint and resulted in Tranche 2 being accounted for as a financing. For instance, the device leaseback periods are generally longer in Tranche 2 as compared to Tranche 1, and the resulting amounts committed to be paid by the Company represent the initial proceeds received from MLS plus interest. This mitigates MLS's exposure to certain risks for non-returned and damaged devices, as well as to declines in device residual values.

***Network Equipment Sale-Leaseback***

In April 2016, Sprint sold and leased back certain network equipment to unrelated bankruptcy-remote special purpose entities (collectively, "Network LeaseCo"). The network equipment was used as collateral to raise approximately \$2.2 billion in borrowings from external investors, including SoftBank. Sprint's payments to Network LeaseCo during the leaseback period are used by Network LeaseCo to service debt.

Network LeaseCo is a variable interest entity for which Sprint is the primary beneficiary. As a result, Sprint is required to consolidate Network LeaseCo and our consolidated financial statements include Network LeaseCo's debt and the related financing cash inflows. The network assets included in the transaction, which had a net book value of approximately \$3.0 billion and consisted primarily of equipment located at cell towers, remain on Sprint's consolidated financial statements and continue to be depreciated over their respective estimated useful lives. At March 31, 2017, these network assets had a net book value of approximately \$2.4 billion.

The proceeds received were reflected as cash provided by financing activities in the consolidated statements of cash flows and payments made by Network LeaseCo are reflected as principal repayments and interest expense over the respective terms. Sprint has the option to purchase the equipment at the end of the leaseback term for a nominal amount. All intercompany transactions between Network LeaseCo and Sprint are eliminated in our consolidated financial statements. Principal and interest payments on the borrowings from the external investors will be repaid in staggered, unequal payments through January 2018. The first principal payment of \$300 million was made in March 2017 with the remaining \$1.9 billion of principal payments due in fiscal year 2017.

***Spectrum Financing***

In October 2016, Sprint transferred certain directly held and third-party leased spectrum licenses (collectively, "Spectrum Portfolio") to wholly-owned bankruptcy-remote special purpose entities (collectively, "Spectrum Financing SPEs"). The Spectrum Portfolio, which represents approximately 14% of Sprint's total spectrum holdings on a MHz-pops basis, was used as collateral to raise an initial \$3.5 billion in senior secured notes at 3.36% per annum from external investors under a \$7.0 billion program. Sprint can utilize this financing structure to potentially raise up to an additional \$3.5 billion subject to certain conditions. The notes will be repaid over a five-year term, with interest-only payments over the first four quarters and amortizing quarterly principal payments thereafter commencing in December 2017 through September 2021.

Sprint Communications, Inc. simultaneously entered into a long-term lease with the Spectrum Financing SPEs for the ongoing use of the Spectrum Portfolio. Sprint Communications, Inc. is required to make monthly lease payments to the Spectrum Financing SPEs at a market rate. Those lease payments are sufficient to service the senior secured notes. As the Spectrum Financing SPEs are wholly-owned Sprint subsidiaries, these entities are consolidated and all intercompany activity has been eliminated.

***Credit Facilities******Secured Term Loan and Revolving Bank Credit Facility***

On February 3, 2017, we entered into a new credit agreement for \$6.0 billion, consisting of a \$4.0 billion, seven-year secured term loan that matures in February 2024 and a \$2.0 billion secured revolving bank credit facility that expires in February 2021. The bank credit facility requires a ratio (Leverage Ratio) of total indebtedness to trailing four quarters earnings before interest, taxes, depreciation and amortization and other non-recurring items, as defined by the bank credit facility (adjusted EBITDA), not to exceed 6.0 to 1.0 through the quarter ending December 31, 2017. After December 31, 2017, the Leverage Ratio declines on a scheduled basis until the ratio becomes fixed at 3.5 to 1.0 for the fiscal quarter ended March 31, 2020 and each fiscal quarter ending thereafter through expiration of the facility. The term loan has an interest rate equal to LIBOR plus 250 basis points and the secured revolving bank credit facility has an interest rate equal to LIBOR plus a spread that varies depending on the Leverage Ratio. The secured revolving bank credit facility replaced the \$3.3 billion unsecured revolving bank credit facility that was due to expire in February 2018.

Table of Contents*Export Development Canada (EDC) agreement*

On February 3, 2017, we amended the EDC agreement to provide for security and covenant terms similar to our secured term loan and revolving bank credit facility. However, under the terms of the EDC agreement, repayments of outstanding amounts cannot be redrawn. In March 2017, the Company repaid \$250 million of aggregate principal of its outstanding Tranche 4 secured loan due December 15, 2017. As of March 31, 2017, the total principal amount of our borrowings under the EDC facility was \$300 million.

**Secured equipment credit facilities***Eksportkreditnamnden (EKN)*

During the year ended March 31, 2017 we made principal repayments totaling \$254 million on the facility, resulting in the total repayment of the principal amount at March 31, 2017. The facility has expired in accordance with its terms.

*Finnvera plc (Finnvera)*

The Finnvera secured equipment credit facility provides for the ability to borrow up to \$800 million to finance network-related purchases from Nokia Solutions and Networks US LLC, USA. The facility has one tranche remaining and available for borrowing through October 2017. Such borrowings are contingent upon the amount and timing of Sprint's network-related purchases. During the year ended March 31, 2017, we made principal repayments totaling \$56 million, resulting in a total principal amount of \$140 million outstanding at March 31, 2017.

*K-sure*

The K-Sure secured equipment credit facility provides for the ability to borrow up to \$750 million to finance network-related purchases from Samsung Telecommunications America, LLC. The facility can be divided in up to three consecutive tranches of varying size with borrowings available until May 2018, contingent upon the amount of network-related purchases made by Sprint. During the year ended March 31, 2017, we made principal repayments totaling \$65 million on the facility, resulting in a total principal amount of \$259 million outstanding at March 31, 2017.

*Delcredere | Ducroire (D/D)*

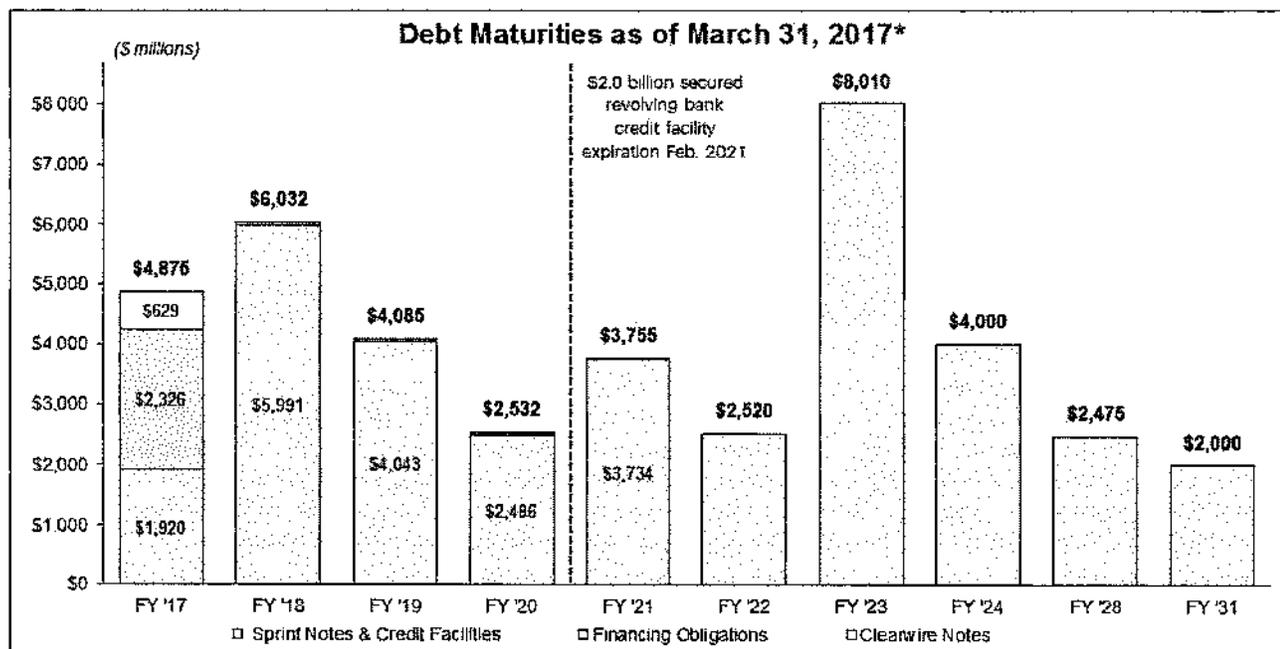
The D/D secured equipment credit facility provides for the ability to borrow up to \$250 million to finance network equipment-related purchases from Alcatel-Lucent USA Inc. The principal balance outstanding at March 31, 2017 was \$32 million.

Borrowings under the Finnvera, K-sure and D/D secured equipment credit facilities are each secured by liens on the respective equipment purchased pursuant to each of the facility's credit agreement. In addition, repayments of outstanding amounts borrowed under the secured equipment credit facilities cannot be redrawn. Each of these facilities is fully and unconditionally guaranteed by both Sprint Communications, Inc. and Sprint Corporation.

As of March 31, 2017, our Leverage Ratio, as defined by our secured revolving bank credit facility was 3.9 to 1.0. Because our Leverage Ratio exceeded 2.5 to 1.0 at period end, we were restricted from paying cash dividends.

Table of Contents

The following graph depicts our future fiscal year principal maturities of debt as of March 31, 2017:



\*This table excludes (i) our \$2.0 billion secured revolving bank credit facility, which will expire in 2021 and has no outstanding balance, (ii) \$215 million in letters of credit outstanding under the secured revolving bank credit facility, (iii) \$540 million of capital leases and other obligations, and (iv) net premiums and debt financing costs.

### Liquidity and Capital Resources

As of March 31, 2017, our liquidity, including cash and cash equivalents, short-term investments, available borrowing capacity under our secured revolving bank credit facility and availability under our Receivables Facility was \$10.9 billion. Our cash and cash equivalents and short-term investments totaled \$8.3 billion as of March 31, 2017 compared to \$2.6 billion as of March 31, 2016. As of March 31, 2017, we had approximately \$1.8 billion of borrowing capacity available under our secured revolving bank credit facility. Amounts available under our Receivables Facility as of March 31, 2017 totaled \$826 million.

In addition, we had a combined available borrowing capacity of \$1.2 billion under our Finnvera, K-sure and D/D secured equipment credit facilities as of March 31, 2017. However, utilization of these facilities is dependent upon the amount and timing of network-related purchases from the applicable suppliers, as well as the period of time remaining to complete any further borrowings available under each facility.

We offer two device financing programs which allow subscribers to forgo traditional service contracts and pay less upfront for devices in exchange for lower monthly service fees, early upgrade options, or both. While a majority of the revenue associated with the installment sales program is recognized at the time of sale along with the related cost of products, lease revenue associated with our leasing program is recorded monthly over the term of the lease and the cost of the device is depreciated to its estimated residual value generally over the lease term, which creates a positive impact to Wireless segment earnings. If the mix of leased devices continues to increase, we expect this positive impact on the financial results of Wireless segment earnings to continue and depreciation expense to increase. The installment billing and leasing programs will continue to require a greater use of operating cash flows in the earlier part of the contracts as the subscriber will generally pay less upfront than the traditional subsidy program because they are financing the device. The Receivables Facility and our relationship with MLS were established as mechanisms to mitigate the use of cash from purchasing devices from OEMs to fulfill our installment billing and leasing programs.

To meet our liquidity requirements, we look to a variety of sources. In addition to our existing cash and cash equivalents, short-term investments, and cash generated from operating activities, we raise funds as necessary from external sources. We rely on the ability to issue debt and equity securities, the ability to access other forms of financing, including

Table of Contents

debt financing, some of which is secured by our assets, proceeds from the sale of certain accounts receivable and future lease receivables, proceeds from future sale-leaseback transactions, such as spectrum, and equipment, and the borrowing capacity available under our credit facilities to support our short- and long-term liquidity requirements. We believe our existing available liquidity and cash flows from operations will be sufficient to meet our funding requirements over the next twelve months, including debt service requirements and other significant future contractual obligations.

To maintain an adequate amount of available liquidity and execute our current business plan, which includes, among other things, network deployment and maintenance, subscriber growth, data usage capacity needs and the expected achievement of a cost structure intended to improve profitability and to meet our long-term debt service requirements and other significant future contractual obligations, we will need to continue to raise additional funds from external sources. Possible future financing sources include, among others, additional receivables financing transactions and raising additional funds through spectrum-backed notes. In addition, we are pursuing extended payment terms and increased facilities with certain vendors. If we are unable to obtain external funding, execute on our cost reduction initiatives, or are not successful in attracting valuable subscribers such as postpaid handset subscribers, our operations would be adversely affected, which may lead to defaults under certain of our borrowings.

Depending on the amount of any difference in actual results versus what we currently expect, it may make it difficult for us to generate sufficient earnings before interest, taxes, depreciation and amortization and other non-recurring items (adjusted EBITDA) to remain in compliance with our financial covenants or be able to meet our debt service obligations, which could result in acceleration of our indebtedness, or adversely impact our ability to raise additional funding through the sources described above, or both. If such events occur, we may engage with our lenders to obtain appropriate waivers or amendments of our credit facilities or refinance borrowings, or seek funding from other external sources, although there is no assurance we would be successful in any of these actions.

A default under certain of our borrowings could trigger defaults under certain of our other financing obligations, which in turn could result in the maturities being accelerated. Certain indentures and other agreements governing our financing obligations require compliance with various covenants, including covenants that limit the Company's ability to sell certain of its assets, limit the Company and its subsidiaries' ability to incur indebtedness and liens, and require that we maintain certain financial ratios, each as defined by the terms of the indentures, related supplemental indentures and other agreements.

In determining our expectation of future funding needs in the next twelve months and beyond, we have made several assumptions regarding:

- projected revenues and expenses relating to our operations, including those related to our installment billing and leasing programs, along with the success of initiatives such as our expectations of achieving a more competitive cost structure through cost reduction initiatives and increasing our postpaid handset subscriber base;
- cash needs related to our installment billing and leasing programs;
- availability under the Receivables Facility, which terminates in November 2018;
- availability of our secured revolving bank credit facility, which expires in February 2021, less outstanding letters of credit;
- remaining availability of approximately \$1.2 billion of our secured equipment credit facilities for eligible capital expenditures, and any corresponding principal, interest and fee payments;
- scheduled principal payments on debt, credit facilities and financing obligations, including approximately \$21.3 billion coming due over the next five fiscal years;
- raising additional funds from external sources;
- the expected use of cash and cash equivalents in the near-term;
- anticipated levels and timing of capital expenditures, including assumptions regarding lower unit costs, network capacity additions and upgrades, and the deployment of new technologies in our networks, FCC license acquisitions, and purchases of leased devices from our indirect dealers;
- any additional contributions we may make to our pension plan;
- estimated residual values of devices related to our device lease program;
- finalization of our tender offers, which we expect to close in June 2017, to purchase for cash up to an aggregate principal amount of \$1.7 billion of our 9.000% Guaranteed Notes due in 2018 and our 8.375% Notes due in 2017; and
- other future contractual obligations and general corporate expenditures.



Table of Contents**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Sprint applies those accounting policies that management believes best reflect the underlying business and economic events, consistent with U.S. GAAP. Sprint's more critical accounting policies include estimated economic lives and residual values of property, plant and equipment, valuation and recoverability of long-lived assets and evaluation of goodwill and indefinite-lived assets for impairment. Inherent in such policies are certain key assumptions and estimates made by management. Management regularly updates its estimates used in the preparation of the financial statements based on its latest assessment of the current and projected business and general economic environment. Sprint's significant accounting policies and estimates are summarized in the Notes to the Consolidated Financial Statements.

***Depreciation***

Our property, plant and equipment balance represents a significant component of our consolidated assets. We record property, plant and equipment at cost and generally depreciate it on a straight-line basis over the estimated useful life of the assets. We expect that a one-year increase in estimated useful lives of our property, plant and equipment, exclusive of leased devices, would result in a decrease to our fiscal year 2017 depreciation expense of \$850 million and that a one-year decrease would result in an increase of \$1.4 billion in our fiscal year 2017 depreciation expense.

***Leased Devices***

Our accounting for device leases involves specific determinations under applicable lease accounting standards. These determinations affect the timing of revenue recognition and the timing and classification of the related cost of the device. If a lease is classified as an operating lease, revenue is recognized ratably over the lease term and the leased asset is included in property, plant and equipment and depreciated to its estimated residual value generally over the lease term. If the lease is classified as a sales-type lease, equipment revenue is recognized at the inception of the lease with a corresponding charge to cost of product. If the lease is classified as a direct-financing lease, there is no related revenue or cost of products recorded and the net investment in a leased asset is reported. The critical elements that we consider in determining the classification of our leased devices are the economic life and the fair value of the device, including the estimated residual value. For the purposes of assessing the economic life of a device, we consider both internal and external datasets including, but not limited to, the length of time subscribers use our devices, sales trends post launch, and transactions in the secondary market as there is currently a significant after-market for used telecommunication devices.

At lease inception, devices classified as operating leases are reclassified from inventory to property, plant and equipment when leased through Sprint's direct channels. For those devices leased through indirect channels, which are classified as operating leases, we purchase the devices at lease inception from the dealer, which is then capitalized to property, plant and equipment. Residual values associated with devices under operating leases represent the estimated fair value at the end of the lease term. We review residual values regularly and, when appropriate, adjust them based on, among other things, estimates of expected market conditions at the end of the lease, including the impacts of future product launches. Adjustments to residual values of leased devices are recognized as a revision in depreciation estimates. We estimate that a 10% increase or decrease in the estimated residual values of devices under operating leases at March 31, 2017 would not have a material effect on depreciation expense over the next twelve months. Through March 31, 2017, the effects of changes in the estimated residual value of devices currently under operating leases have been immaterial.

***Valuation and Recoverability of Long-lived Assets***

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized if the carrying amount of a long-lived asset or asset group is not recoverable and exceeds its fair value. Long-lived asset groups have been determined based upon certain factors including assessing the lowest level for which identifiable cash flows are largely independent of the cash flows of other groups of assets and liabilities. Impairment analyses, when performed, are based on our current business and technology strategy, views of growth rates for our business, anticipated future economic and regulatory conditions and expected technological availability.

During the years ended March 31, 2017 and 2016, no impairments were recorded. During the year ended March 31, 2015, we recorded an impairment loss of \$233 million, which is included in "Impairments" in our consolidated statements of operations, to reduce the carrying value of the Wireline asset group, which includes the Wireline long-lived assets, to its estimated fair value as of our testing date. The fair value of the Wireline long-lived assets was estimated using a market approach, which included significant unobservable inputs including liquidation curves, useful life assumptions, and scrap values. As the assumptions are largely unobservable, the estimate of fair value is considered to be unobservable within the fair value hierarchy.

Table of Contents

The determination of fair value requires considerable judgment and is highly sensitive to changes in underlying assumptions. While we believe our judgments and assumptions are reasonable, changes in future periods may impact our assumptions and lead to additional, future impairments.

*Evaluation of Goodwill and Indefinite-Lived Intangible Assets for Impairment*

As a result of the SoftBank Merger in July 2013, we recognized indefinite-lived assets at their acquisition-date estimates of fair value, including FCC licenses, goodwill, and trade names. All of the indefinite-lived assets, including goodwill, were allocated to our Wireless segment. As of March 31, 2017, the carrying values of these assets were \$36.6 billion, \$6.6 billion and \$4.0 billion, respectively.

Sprint evaluates the carrying value of our indefinite-lived assets, including goodwill, at least annually or more frequently whenever events or changes in circumstances indicate that the asset may be impaired, or in the case of goodwill, that the fair value of the reporting unit is below its carrying amount. During the quarter-ended March 31, 2017, the Company completed its annual impairment testing for goodwill, the Sprint and Boost Mobile trade names, and spectrum licenses using a qualitative evaluation. The results of the qualitative evaluation determine whether it is necessary to perform a quantitative test. If it is more likely than not that the asset may be impaired, or in the case of goodwill, that the fair value of a reporting unit is less than its carrying amount, we would be required to perform a quantitative test. As a result of our testing in the current period, we determined that it was not more likely than not that the fair value of each of our indefinite-lived intangible assets were less than their carrying values.

In performing the annual goodwill impairment test for the year ended March 31, 2016, we estimated the fair value of the Wireless reporting unit using income-based, market-based and asset-based valuation models. The determination of the fair value of the reporting unit requires significant estimates and assumptions, including significant unobservable inputs. The key inputs included, but were not limited to, discount rates, terminal growth rates, control premiums, market multiple data from selected guideline public companies, management's internal forecasts which include numerous assumptions such as share of industry gross additions, churn, mix of plans, rate changes, operating and capital expenditures and EBITDA margins, among others. Changes in certain assumptions or management's failure to execute on the current plan could have a significant impact to the estimated fair value of the Wireless reporting unit. Under the income-based approach, we note that our fair value cushion was in excess of 10% of the carrying value in regards to the annual impairment test for the year ended March 31, 2016.

We estimated the fair value of the Sprint and Boost Mobile trade names assigned to the Wireless segment using the relief-from-royalty method, which uses several significant assumptions, including management projections of future revenue, a royalty rate, a long-term growth rate and a discount rate. As these assumptions are largely unobservable, the estimate of fair value is considered to be unobservable within the fair value hierarchy. Changes in certain assumptions can have a significant effect on the estimated fair value. For both the Sprint and Boost Mobile trade names, we note that a 5% decrease in revenue across the long-term plans would not have resulted in an impairment in regards to the annual impairment test for the year ended March 31, 2016. Additionally, the Company has seen significant market pressures in recent periods that has contributed to a loss of Boost Mobile subscribers for the fiscal year ended March 31, 2017. The Boost Mobile trade name may be subject to future impairments if the Company continues to incur Boost Mobile subscriber losses, is unable to meet future revenue projections, or future revenue projections are markedly lower in prospective periods. There can be no assurance that future revenue projections will be sufficient to avoid future impairments.

During the year ended March 31, 2015, we determined that recoverability of the carrying amount of goodwill and the Sprint trade name should be evaluated for impairment and it was determined that the carrying value of the Sprint trade name exceeded its estimated fair value of \$3.3 billion. Accordingly, during the year ended March 31, 2015 we recorded an impairment loss of \$1.9 billion, which is included in "Impairments" in our consolidated statements of operations.

The determination of fair value requires considerable judgment and is highly sensitive to changes in underlying assumptions and execution of management's plan. Consequently, there can be no assurance that the estimates and assumptions made for the purposes of the goodwill, spectrum and trade name impairment tests will prove to be an accurate prediction of the future. Sustained declines in the Company's operating results, number of wireless subscribers, future forecasted cash flows, growth rates and other assumptions, as well as significant, sustained declines in the Company's stock price and related market capitalization could impact the underlying key assumptions and our estimated fair values, potentially leading to a future material impairment of goodwill or other indefinite-lived intangible assets.

Table of Contents**NEW ACCOUNTING PRONOUNCEMENTS**

See *Note 2. Summary of Significant Accounting Policies and Other Information*, in Notes to the Consolidated Financial Statements in Item 8. of Part II of this Annual Report on Form 10-K, for a full description of new accounting pronouncements, including the expected dates of adoption and estimated effects on financial condition and results of operations, which are hereby incorporated by reference.

**FINANCIAL STRATEGIES***General Risk Management Policies*

Our board of directors has adopted a financial risk management policy that authorizes us to enter into derivative transactions, and all transactions comply with the policy. We do not purchase or hold any derivative financial instruments for speculative purposes with the exception of equity rights obtained in connection with commercial agreements or strategic investments, usually in the form of warrants to purchase common shares.

Derivative instruments are primarily used for hedging and risk management purposes. Hedging activities may be done for various purposes, including, but not limited to, mitigating the risks associated with an asset, liability, committed transaction or probable forecasted transaction. We seek to minimize counterparty credit risk through credit approval and review processes, credit support agreements, continual review and monitoring of all counterparties, and thorough legal review of contracts. Exposure to market risk is controlled by regularly monitoring changes in hedge positions under normal and stress conditions to ensure they do not exceed established limits.

**OTHER INFORMATION**

We routinely post important information on our website at [www.sprint.com/investors](http://www.sprint.com/investors). Information contained on or accessible through our website is not part of this annual report.

**FORWARD-LOOKING STATEMENTS**

We include certain estimates, projections and other forward-looking statements in our annual, quarterly and current reports, and in other publicly available material. Statements regarding expectations, including performance assumptions and estimates relating to capital requirements, as well as other statements that are not historical facts, are forward-looking statements.

These statements reflect management's judgments based on currently available information and involve a number of risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements. With respect to these forward-looking statements, management has made assumptions regarding, among other things, subscriber and network usage, subscriber growth and retention, technologies, products and services, pricing, operating costs, the timing of various events, and the economic and regulatory environment.

Future performance cannot be assured. Actual results may differ materially from those in the forward-looking statements. Some factors that could cause actual results to differ include:

- our ability to obtain additional financing, including monetizing certain of our assets, including those under our existing or future programs to monetize a portion of our network or spectrum holdings, or to modify the terms of our existing financing, on terms acceptable to us, or at all;
- our ability to continue to receive the expected benefits of our existing financings such as receivable financings;
- our ability to retain and attract subscribers and to manage credit risks associated with our subscribers;
- the ability of our competitors to offer products and services at lower prices due to lower cost structures or otherwise;
- the effective implementation of our plans to improve the quality of our network, including timing, execution, technologies, costs, and performance of our network;
- failure to improve subscriber churn, bad debt expense, accelerated cash use, costs and write-offs, including with respect to changes in expected residual values related to any of our service plans, including installment billing and leasing programs;

Table of Contents

- the ability to generate sufficient cash flow to fully implement our plans to improve and enhance the quality of our network and service plans, improve our operating margins, implement our business strategies, and provide competitive new technologies;
- the effects of vigorous competition on a highly penetrated market, including the impact of competition on the prices we are able to charge subscribers for services and devices we provide and on the geographic areas served by our network;
- the impact of installment sales and leasing of handsets; the impact of increased purchase commitments; the overall demand for our service plans, including the impact of decisions of new or existing subscribers between our service offerings; and the impact of new, emerging, and competing technologies on our business;
- our ability to provide the desired mix of integrated services to our subscribers;
- our ability to continue to access our spectrum and acquire additional spectrum capacity;
- changes in available technology and the effects of such changes, including product substitutions and deployment costs and performance;
- volatility in the trading price of our common stock, current economic conditions, and our ability to access capital, including debt or equity;
- the impact of various parties not meeting our business requirements, including a significant adverse change in the ability or willingness of such parties to provide service and products, including distribution, or infrastructure equipment for our network;
- the costs and business risks associated with providing new services and entering new geographic markets;
- the effects of any future merger or acquisition involving us, as well as the effect of mergers, acquisitions, and consolidations, and new entrants in the communications industry, and unexpected announcements or developments from others in our industry;
- our ability to comply with restrictions imposed by the U.S. Government as a condition to our merger with SoftBank;
- the effects of any material impairment of our goodwill or other indefinite-lived intangible assets;
- the impacts of new accounting standards or changes to existing standards that the FASB or other regulatory agencies issue, including the SEC;
- unexpected results of litigation filed against us or our suppliers or vendors;
- the costs or potential customer impact of compliance with regulatory mandates including, but not limited to, compliance with the FCC's Report and Order to reconfigure the 800 MHz band and government regulation regarding "net neutrality";
- equipment failure, natural disasters, terrorist acts or breaches of network or information technology security;
- one or more of the markets in which we compete being impacted by changes in political, economic, or other factors such as monetary policy, legal and regulatory changes, or other external factors over which we have no control;
- the impact of being a "controlled company" exempt from many corporate governance requirements of the NYSE; and
- other risks referenced from time to time in this report and other filings of ours with the SEC.

The words "may," "could," "should," "estimate," "project," "forecast," "intend," "expect," "anticipate," "believe," "target," "plan" and similar expressions are intended to identify forward-looking statements. Forward-looking statements are found throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, and elsewhere in this report. Readers are cautioned that other factors, although not listed above, could also materially affect our future performance and operating results. The reader should not place undue reliance on forward-looking statements, which speak only as of the date of this report. We are not obligated to publicly release any revisions to forward-looking statements to reflect events after the date of this report, including unforeseen events.

Table of Contents**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

We are primarily exposed to the market risk associated with unfavorable movements in interest rates, foreign currencies, and equity prices. The risk inherent in our market risk sensitive instruments and positions is the potential loss arising from adverse changes in those factors.

**Interest Rate Risk**

The communications industry is a capital-intensive, technology-driven business. We are subject to interest rate risk primarily associated with our borrowings. Interest rate risk is the risk that changes in interest rates could adversely affect earnings and cash flows. Specific interest rate risk includes: the risk of increasing interest rates on variable rate debt and the risk of increasing interest rates for planned new fixed rate long-term financings or refinancings. Occasionally we may enter into derivative agreements such as interest rate caps and swaps to manage some of our variable interest rate exposure. As of March 31, 2017, we entered into a five-year fixed-for-floating interest rate swap on a \$2.0 billion notional amount that has been designated as a cash flow hedge and is intended to reduce some of our exposure to rising interest rates by hedging variable interest costs related to 50% of our \$4.0 billion secured term loan.

Approximately 83% of our debt as of March 31, 2017 was fixed-rate debt. While changes in interest rates impact the fair value of this debt, there is no impact to earnings and cash flows because we intend to hold these obligations to maturity unless market and other conditions are favorable.

We perform interest rate sensitivity analyses on our variable-rate debt. These analyses indicate that a one percentage point change in interest rates would have had an annual pre-tax impact of \$62 million on our consolidated statements of operations and cash flows for the year ended March 31, 2017. We also perform a sensitivity analysis on the fair market value of our outstanding debt. A 10% decline in market interest rates is estimated to result in a \$941 million increase in the fair market value of our debt to \$44.2 billion.

**Foreign Currency Risk**

We may enter into forward contracts and options in foreign currencies to reduce the impact of changes in foreign exchange rates. Our foreign exchange risk management program focuses on reducing transaction exposure to optimize consolidated cash flow. We use foreign currency derivatives to hedge our foreign currency exposure related to settlement of international telecommunications access charges and the operation of our international subsidiaries. The dollar equivalent of our net foreign currency payables from international settlements was insignificant and the net foreign currency receivables from international operations was insignificant as of March 31, 2017. The potential immediate pre-tax loss to us that would result from a hypothetical 10% change in foreign currency exchange rates based on these positions would be insignificant.

**Item 8. Financial Statements and Supplementary Data**

The consolidated financial statements required by this item begin on page F-1 of this annual report on Form 10-K and are incorporated herein by reference.

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**Item 9A. Controls and Procedures****Evaluation of Disclosure Controls and Procedures**

Disclosure controls are procedures that are designed with the objective of ensuring that information required to be disclosed in our reports under the Securities Exchange Act of 1934 (Exchange Act), such as this annual report on Form 10-K, is reported in accordance with the SEC's rules. Disclosure controls are also designed with the objective of ensuring that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

In connection with the preparation of this annual report on Form 10-K, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the design and operation of the disclosure controls and procedures were effective as of March 31, 2017 in providing reasonable assurance that information required to be disclosed in reports we file or submit under the Exchange Act is accumulated and communicated to management,

Table of Contents

including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure and in providing reasonable assurance that the information is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms.

**Management's Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control system was designed to provide reasonable assurance to our management and board of directors regarding the reliability of financial reporting and the preparation of financial statements for external purposes.

Our management conducted an assessment of the effectiveness of our internal control over financial reporting as of March 31, 2017. This assessment was based on the criteria set forth by *Internal Control—Integrated Framework*, issued in 2013 by the Committee of Sponsoring Organizations. Management believes that, as of March 31, 2017, our internal control over financial reporting was effective.

Internal controls over our financial reporting continue to be updated as necessary to accommodate modifications to our business processes and accounting procedures. There have been no changes in our internal control over financial reporting that occurred during the quarter ended March 31, 2017 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Our independent registered public accounting firm has issued a report on the effectiveness of our internal control over financial reporting. This report appears on page F-2.

**Item 9B. Other Information*****Disclosure of Iranian Activities under Section 13(r) of the Exchange Act***

Section 219 of the Iran Threat Reduction and Syria Human Rights Act of 2012 added Section 13(r) to the Securities Exchange Act of 1934. Section 13(r) requires an issuer to disclose in its annual or quarterly reports, as applicable, whether it or any of its affiliates knowingly engaged in certain activities, including, among other matters, transactions or dealings relating to the government of Iran. Disclosure is required even where the activities, transactions or dealings are conducted outside the U.S. by non-U.S. affiliates in compliance with applicable law, and whether or not the activities are sanctionable under U.S. law.

After the SoftBank Merger, SoftBank acquired control of Sprint. During the fiscal year ended March 31, 2017, SoftBank, through one of its non-U.S. subsidiaries, provided roaming services in Iran through Telecommunications Services Company (MTN Irancell), which is or may be a government-controlled entity. During the fiscal year ended March 31, 2017, SoftBank had no gross revenues from such services and no net profit was generated. This subsidiary also provided telecommunications services in the ordinary course of business to accounts affiliated with the Embassy of Iran in Japan. During the fiscal year ended March 31, 2017, SoftBank estimates that gross revenues and net profit generated by such services were both under \$9,400. Sprint was not involved in, and did not receive any revenue from, any of these activities. These activities have been conducted in accordance with applicable laws and regulations, and they are not sanctionable under U.S. or Japanese law. Accordingly, with respect to Telecommunications Services Company (MTN Irancell), the relevant SoftBank subsidiary intends to continue such activities. With respect to services provided to accounts affiliated with the Embassy of Iran in Japan, the relevant SoftBank subsidiary is obligated under contract to continue such services.

In addition, during the fiscal year ended March 31, 2017, SoftBank, through one of its non-U.S. indirect subsidiaries, provided office supplies to the Embassy of Iran in Japan. SoftBank estimates that gross revenue and net profit generated by such services were under \$5,300 and \$1,030, respectively. Sprint was not involved in, and did not receive any revenue from any of these activities. Accordingly, the relevant SoftBank subsidiary intends to continue such activities.

Table of Contents**PART III****Item 10. Directors, Executive Officers and Corporate Governance**

The information required by this item regarding our directors is incorporated by reference to the information set forth under the captions "Proposal 1. - Election of Directors" "Board Operations—Board Committees" in our proxy statement relating to our 2017 annual meeting of stockholders, which will be filed with the SEC, and with respect to family relationships, to Part I of this annual report under "Executive Officers of the Registrant." The information required by this item regarding our executive officers is incorporated by reference to Part I of this annual report under the caption titled "Executive Officers of the Registrant." The information required by this item regarding compliance with Section 16(a) of the Exchange Act by our directors, executive officers and holders of ten percent of a registered class of our equity securities is incorporated by reference to the information set forth under the caption "Security Ownership—Section 16(a) Beneficial Ownership Reporting Compliance" in our proxy statement relating to our 2017 annual meeting of stockholders, which will be filed with the SEC.

We have adopted the Sprint Corporation Code of Conduct, which applies to all of our directors, officers and employees. The Code of Conduct is publicly available on our website at <http://www.sprint.com/governance>. If we make any material amendment to our Code of Conduct, or if we grant any waiver from a provision of the Code of Conduct that applies to our principal executive officer, principal financial officer, principal accounting officer or controller, we will disclose the nature of the amendment or waiver on our website at the same location. Also, we may elect to disclose the amendment or waiver in a current report on Form 8-K filed with the SEC.

**Item 11. Executive Compensation**

The information required by this item regarding compensation of executive officers and directors is incorporated by reference to the information set forth under the captions "Director Compensation," "Executive Compensation," and "Board Operations—Compensation Committee Interlocks and Insider Participation" in our proxy statement relating to our 2017 annual meeting of stockholders, which will be filed with the SEC.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The information required by this item, other than the equity compensation plan information presented below, is incorporated by reference to the information set forth under the captions "Security Ownership—Security Ownership of Certain Beneficial Owners" and "Security Ownership—Security Ownership of Directors and Executive Officers" in our proxy statement relating to our 2017 annual meeting of stockholders, which will be filed with the SEC.

**Compensation Plan Information**

Currently we sponsor two active equity incentive plans, the 2015 Amended and Restated Omnibus Incentive Plan (2015 Plan) and our Employee Stock Purchase Plan (ESPP). We also sponsor the 2007 Omnibus Incentive Plan (2007 Plan) and the 1997 Long-Term Incentive Program (1997 Program). All outstanding options under the Nextel Incentive Equity Plan (Nextel Plan) expired in fiscal year 2015. Under the 2015 Plan, we may grant stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units and other equity-based and cash awards to our employees, outside directors and certain other service providers. Our board of directors, or one or more committees, will determine the terms of each award. No new grants can be made under the 2007 Plan or the 1997 Program.

Table of Contents

The following table provides information about the shares of common stock that may be issued upon exercise of awards as of March 31, 2017.

Plan Category	Number of Securities To be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))
	(a)	(b)	(c)
Equity compensation plans approved by stockholders of common stock	120,440,328	\$4.57	211,161,529

- (1) Includes 11,825,982 shares covered by options and 71,761,210 restricted stock units under the 2015 Plan, 25,353,304 shares covered by options and 10,952,022 restricted stock units under the 2007 Plan, and 25,835 restricted stock units outstanding under the 1997 Program. Also includes purchase rights to acquire 521,975 shares of common stock accrued at March 31, 2017 under the ESPP. Under the ESPP, each eligible employee may purchase common stock at quarterly intervals at a purchase price per share equal to 85% of the market value on the last business day of the offering period.
- (2) Included in the total of 120,440,328 shares are 10,952,022 restricted stock units under the 2007 Plan, which will be counted against the 2007 Plan maximum in a 2.5 to 1 ratio.
- (3) The weighted average exercise price does not take into account the shares of common stock issuable upon vesting of restricted stock units issued under the 1997 Program, the 2007 Plan or the 2015 Plan. These restricted stock units have no exercise price. The weighted average purchase price also does not take into account the 521,975 shares of common stock issuable as a result of the purchase rights accrued under the ESPP; the purchase price of these shares was \$7.32 for each share.
- (4) Of these shares, 139,992,111 shares of common stock were available under the 2015 Plan. Through March 31, 2017, 171,358,126 cumulative shares came from the 2007 Plan, the 1997 Program and predecessor plans, including the Nextel Plan.
- (5) Includes 71,169,418 shares of common stock available for issuance under the ESPP after issuance of the 521,975 shares purchased in the quarter ended March 31, 2017 offering. See note 1 above.
- (6) No new awards may be granted under the 2007 Plan or the 1997 Program.

#### Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required by this item is incorporated by reference to the information set forth under the captions "Certain Relationships and Related Party Transactions" and "Board Operations—Independence of Directors" in our proxy statement relating to our 2017 annual meeting of stockholders, which will be filed with the SEC.

#### Item 14. Principal Accounting Fees and Services

The information required by this item is incorporated by reference to the information set forth under the caption "Principal Accounting Fees and Services" in our proxy statement relating to our 2017 annual meeting of stockholders, which will be filed with the SEC.

Table of Contents

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

1. The consolidated financial statements of Sprint Corporation filed as part of this annual report are listed in the Index to Consolidated Financial Statements.
2. The exhibits filed as part of this annual report are listed in the Exhibit Index.

**Item 16. Form 10-K Summary**

None.



Table of Contents**SIGNATURES  
SPRINT CORPORATION  
(Registrant)**

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on the 26<sup>th</sup> day of May, 2017.

/s/ MASAYOSHI SON

Masayoshi Son, Chairman

/s/ MARCELO CLAURE

Marcelo Claure, Director

/s/ RONALD D. FISHER

Ronald D. Fisher, Vice Chairman

/s/ PATRICK T. DOYLE

Patrick T. Doyle, Director

/s/ GORDON M. BETHUNE

Gordon M. Bethune, Director

/s/ JULIUS GENACHOWSKI

Julius Genachowski, Director

/s/ ADMIRAL MICHAEL G. MULLEN

Admiral Michael G. Mullen, Director

/s/ SARA MARTINEZ TUCKER

Sara Martinez Tucker, Director

Table of Contents**Exhibit Index**

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
<b>(2) Plan of Acquisition, Reorganization, Arrangement, Liquidation or Succession</b>						
2.1**	Agreement and Plan of Merger, dated as of October 15, 2012, by and among Sprint Nextel Corporation, SoftBank Corp., Starburst I, Inc., Starburst II, Inc. and Starburst III, Inc.	8-K	001-04721	2.1	10/15/2012	
2.2	First Amendment to Agreement and Plan of Merger, dated November 29, 2012, by and among Sprint Nextel Corporation, SoftBank Corp., Starburst I, Inc., Starburst II, Inc. and Starburst III, Inc.	10-Q	001-04721	2.5	5/6/2013	
2.3	Second Amendment to Agreement and Plan of Merger, dated April 12, 2013, by and among Sprint Nextel Corporation, SoftBank Corp., Starburst I, Inc., Starburst II, Inc. and Starburst III, Inc.	10-Q	001-04721	2.6	5/6/2013	
2.4**	Third Amendment to Agreement and Plan of Merger, dated June 10, 2013, by and among Sprint Nextel Corporation, SoftBank Corp., Starburst I, Inc., Starburst II, Inc. and Starburst III, Inc.	8-K	001-04721	2.1	6/11/2013	
2.5**	Agreement and Plan of Merger, dated as of December 17, 2012, by and among Sprint Nextel Corporation, Collie Acquisition Corp. and Clearwire Corporation	8-K	001-04721	2.1	12/18/2012	
2.6**	First Amendment to Agreement and Plan of Merger, dated as of April 18, 2013, by and among Sprint Nextel Corporation, Collie Acquisition Corp. and Clearwire Corporation (Filed as Annex-2 to Clearwire Corporation's Proxy Statement)	DEFM14A	001-34196		4/23/2013	
2.7**	Second Amendment to Agreement and Plan of Merger, dated as of May 21, 2013, by and among Sprint Nextel Corporation, Collie Acquisition Corp. and Clearwire Corporation	8-K	001-04721	2.1	5/22/2013	
2.8**	Third Amendment to Agreement and Plan of Merger, dated June 20, 2013, by and among Sprint Nextel Corporation, Collie Acquisition Corp. and Clearwire Corporation	8-K	001-04721	2.1	6/21/2013	
<b>(3) Articles of Incorporation and Bylaws</b>						
3.1	Amended and Restated Certificate of Incorporation	8-K	001-04721	3.1	7/11/2013	
3.2	Amended and Restated Bylaws	8-K	001-04721	3.2	8/7/2013	
<b>(4) Instruments Defining the Rights of Security Holders, including Indentures</b>						
4.1	Indenture, dated as of October 1, 1998, by and among	10-Q	001-04721	4(b)	11/2/1998	

Sprint Capital Corporation, Sprint Corporation and The Bank of New York Mellon Trust Company, N.A. (as successor to Bank One, N.A.)

4.2	First Supplemental Indenture, dated as of January 15, 1999, by and among Sprint Capital Corporation, Sprint Corporation and The Bank of New York Mellon Trust Company, N.A. (as successor to Bank One, N.A.)	8-K	001-04721	4(b)	2/3/1999
-----	--	-----	-----------	------	----------

Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
4.3	Second Supplemental Indenture, dated as of October 15, 2001, by and among Sprint Capital Corporation, Sprint Corporation and The Bank of New York Mellon Trust Company, N.A. (as successor to Bank One, N.A.)	8-K	001-04721	99	10/29/2001	
4.4	Third Supplemental Indenture, dated as of September 11, 2013, by and among Sprint Corporation, Sprint Capital Corporation, Sprint Communications, Inc. and The Bank of New York Mellon Trust Company, N.A. (as successor to Bank One, N.A.)	8-K	001-04721	4.5	9/11/2013	
4.5	Indenture, dated as of November 20, 2006, by and between Sprint Nextel Corporation and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.1	11/9/2011	
4.6	First Supplemental Indenture, dated as of November 9, 2011, by and between Sprint Nextel Corporation and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.2	11/9/2011	
4.7	Second Supplemental Indenture, dated as of November 9, 2011, by and among Sprint Nextel Corporation, the Subsidiary Guarantors and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.3	11/9/2011	
4.8	Third Supplemental Indenture, dated as of March 1, 2012, by and between Sprint Nextel Corporation and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.1	3/1/2012	
4.9	Fourth Supplemental Indenture, dated as of March 1, 2012, by and among Sprint Nextel Corporation, the Subsidiary Guarantors and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.2	3/1/2012	
4.10	Fifth Supplemental Indenture, dated as of August 14, 2012, by and between Sprint Nextel Corporation and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.1	8/14/2012	
4.11	Sixth Supplemental Indenture, dated as of November 14, 2012, by and between Sprint Nextel Corporation and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.1	11/14/2012	
4.12	Seventh Supplemental Indenture, dated as of November 20, 2012, by and between Sprint Nextel Corporation and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.1	11/20/2012	
4.13	Eighth Supplemental Indenture, dated as of September 11, 2013, by and among Sprint Corporation, Sprint Communications, Inc. and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.4	9/11/2013	
4.14	Ninth Supplemental Indenture, dated as of June 26, 2014, by and between Bright PCS Holdings, Inc., Bright Personal Communications Services, LLC, Horizon Personal Communications, Inc., iPCS Equipment, Inc., iPCS Wireless, Inc., Pinsight Media+, Inc., OneLouder Apps, Inc., iPCS, Inc., Sprint Communications, Inc. and The Bank of New York Mellon Trust Company, N.A.	10-Q	001-04721	4.1	8/8/2014	



Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
4.15	Tenth Supplemental Indenture, dated as of August 9, 2016, by and among Virgin Mobile USA - Evolution, Inc., as new guarantor, Sprint Communications, Inc., The Bank of New York Mellon Trust Company, N.A., as trustee	8-K	001-04721	4.4	2/6/2017	
4.16	Eleventh Supplemental Indenture, dated as of November 16, 2016, by and among Sprint Communications, Inc., The Bank of New York Mellon Trust Company, N.A., as trustee and certain subsidiaries of Sprint Corporation as new guarantors	8-K	001-04721	4.5	2/6/2017	
4.17	Indenture, dated as of September 11, 2013, by and between Sprint Corporation and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.1	9/11/2013	
4.18	First Supplemental Indenture, dated as of September 11, 2013, by and among Sprint Corporation, Sprint Communications, Inc. and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.2	9/11/2013	
4.19	Second Supplemental Indenture, dated as of September 11, 2013, by and among Sprint Corporation, Sprint Communications, Inc. and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.3	9/11/2013	
4.20	Third Supplemental Indenture, dated as of December 12, 2013, by and among Sprint Corporation, Sprint Communications, Inc. and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.1	12/12/2013	
4.21	Fourth Supplemental Indenture, dated as of February 24, 2015, by and among Sprint Corporation, Sprint Communications, Inc. and The Bank of New York Mellon Trust Company, N.A.	8-K	001-04721	4.1	2/24/2015	
4.22	Indenture, dated as of October 27, 2016, among Sprint Spectrum Co LLC, Sprint Spectrum Co II LLC, Sprint Spectrum Co III LLC and Deutsche Bank Trust Company Americas, as trustee and securities intermediary.	8-K	001-04721	4.1	11/2/2016	
4.23	Series 2016-1 Supplement, dated as of October 27, 2016, among Sprint Spectrum Co LLC, Sprint Spectrum Co II LLC, Sprint Spectrum Co III LLC and Deutsche Bank Trust Company Americas, as trustee and securities intermediary.	8-K	001-04721	4.2	11/2/2016	
4.24	Form of Series 2016-1 3.360% Senior Secured Notes, Class A-1 (included in Exhibit 4.23).	8-K	001-04721	4.3	11/2/2016	
<b>(10) Material Contracts</b>						
10.1	Amended and Restated Receivables Purchase Agreement, dated as of April 24, 2015, among Sprint Spectrum L.P., individually and as Servicer, the Sellers	8-K	001-04721	10.1	4/27/2015	

party thereto, the various Conduit Purchasers, Committed Purchasers, and Purchaser Agents from time to time party thereto, Mizuho Bank Ltd. as Administrative Agent and Collateral Agent and The Bank of Tokyo-Mitsubishi UFJ, Ltd., New York Branch, as Administrative Agent

Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
10.2	Second Amended and Restated Receivables Purchase Agreement, dated as of November 19, 2015, by and among Sprint Spectrum L.P., as servicer, certain Sprint special purpose entities, as sellers, certain commercial paper conduits and financial institutions from time to time party thereto, as purchaser agents, The Bank of Tokyo-Mitsubishi UFJ, Ltd., New York Branch, as administrative agent, SMBC Nikko Securities America, Inc., as administrative agent, and Mizuho Bank, Ltd., as administrative agent and collateral agent	8-K	001-04721	10.6	11/20/2015	
10.3	First Amendment to Second Amended and Restated Receivables Purchase Agreement, dated as of November 18, 2016, by and among Sprint Spectrum L.P., as initial servicer, the Sellers party thereto, the various Conduit Purchasers, Committed Purchasers and Purchaser Agents party thereto, Mizuho Bank, Ltd., as Collateral Agent, The Bank of Tokyo-Mitsubishi UFJ, Ltd., as SCC Administrative Agent, and SMBC Nikko Securities America, Inc. as Lease Administrative Agent	10-Q	001-04721	10.6	2/6/2017	
10.4	Second Amendment to the Second Amended and Restated Receivables Purchase Agreement, dated as of February 3, 2017, by and among Sprint Spectrum L.P., as servicer, certain Sprint Corporation special purpose entities, as sellers, certain commercial paper conduits and financial institutions from time to time party thereto, as purchasers, the entities from time to time party thereto as purchaser agents, The Bank of Tokyo-Mitsubishi UFJ, Ltd., New York Branch, as administrative agent, SMBC Nikko Securities America, Inc., as administrative agent, and Mizuho Bank, Ltd., as administrative agent and collateral agent	8-K	001-04721	10.2	2/6/2017	
10.5	First Amendment to the Second Amended and Restated Receivables Sale and Contribution Agreement, dated as of February 3, 2017, by and among Sprint Spectrum L.P., as servicer, and certain Sprint Corporation subsidiaries, as originators and sellers, and certain special purpose entities, as purchasers	8-K	001-04721	10.3	2/6/2017	
10.6	Amended and Restated Receivables Sale Agreement, dated as of April 24, 2015, between Sprint Spectrum L.P., as an Originator and as Servicer, the other Originators from time to time party thereto and the Buyers from time to time party thereto	8-K	001-04721	10.2	4/27/2015	
10.7	Second Amended and Restated Receivables Sale and Contribution Agreement, dated as of November 19, 2015, by and among certain Sprint subsidiaries as originators and special purpose entities	8-K	001-04721	10.7	11/20/2015	

Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
10.8	Credit Agreement, dated as of February 3, 2017, by and among Sprint Communications, Inc., as Borrower, the guarantors party thereto, JPMorgan Chase Bank, N.A., as Administrative Agent, and the lenders party thereto.	8-K	001-04721	10.1	2/6/2017	
10.9	Amended and Restated First Step Transfer Agreement (Tranche 1), dated as of April 28, 2016, among the originators from time to time party thereto, the lessees from time to time party thereto and Sprint Spectrum L.P	10-K	001-04721	10.10	5/17/2016	
10.10	Amended and Restated Second Step Transfer Agreement (Tranche 1), dated as of April 28, 2016, among the lessees from time to time party thereto and Mobile Leasing Solutions, LLC	10-K	001-04721	10.11	5/17/2016	
10.11	Amended and Restated Master Lease Agreement (Tranche 1), dated as of April 28, 2016, among Mobile Leasing Solutions, LLC, the lessees from time to time party thereto, Sprint Spectrum L.P. and Mizuho Bank, Ltd., as collateral agent	10-K	001-04721	10.12	5/17/2016	
10.12	Amended and Restated Performance Support Agreement (Tranche 1), dated as of April 28, 2016, by Sprint Corporation in favor of Mobile Leasing Solutions, LLC	10-K	001-04721	10.13	5/17/2016	
10.13	Amended and Restated Guaranty (Tranche 1), dated as of April 28, 2016, by Sprint Corporation in favor of Mobile Leasing Solutions, LLC	10-K	001-04721	10.14	5/17/2016	
10.14	Master Lease Agreement, dated as of March 31, 2016 (effective as of April 5, 2016), among the purchasers party thereto and the lessees party thereto	8-K	001-04721	10.2	4/6/2016	
10.15	Form of Sale Agreement, dated as of March 31, 2016 (effective as of April 5, 2016), by and between the lessees party thereto and the purchasers party thereto	8-K	001-04721	10.1	4/6/2016	
10.16	Guaranty, dated as of March 31, 2016 (effective as of April 5, 2016), by Sprint Corporation in favor of the purchasers party thereto	8-K	001-04721	10.3	4/6/2016	
10.17	Amended and Restated First Step Transfer Agreement (Tranche 2), dated as of December 8, 2016, by and among Sprint Spectrum L.P., the Originators from time to time party thereto, and the Lessees from time to time party thereto	10-Q	001-04721	10.7	2/6/2017	
10.18	Amended and Restated Second Step Transfer Agreement (Tranche 2), dated as of December 8, 2016, by and among Mobile Leasing Solutions, LLC acting for itself and on behalf of Series 2 thereof and the Lessees from time to time party thereto	10-Q	001-04721	10.8	2/6/2017	
10.19	Amended and Restated Master Lease Agreement (Tranche 2), dated as of December 8, 2016, by and among Sprint Spectrum L.P., the Lessees from time to time party thereto, Mizuho Bank, Ltd., and Mobile	10-Q	001-04721	10.9	2/6/2017	

Leasing Solutions, LLC acting for itself and on behalf of  
Series 2 thereof

Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
10.20	First Step Transfer Agreement (Tranche 2), dated as of April 28, 2016, among the originators from time to time party thereto, the lessees from time to time party thereto and Sprint Spectrum L.P.	8-K	001-04721	10.1	4/29/2016	
10.21	Second Step Transfer Agreement (Tranche 2), dated as of April 28, 2016, among the lessees from time to time party thereto and Mobile Leasing Solutions, LLC, acting for itself and on behalf of Series 2 thereof	8-K	001-04721	10.2	4/29/2016	
10.22	Master Lease Agreement (Tranche 2), dated as of April 28, 2016, among Mobile Leasing Solutions, LLC, acting for itself and on behalf of Series 2 thereof, the lessees from time to time party thereto, Sprint Spectrum L.P. and Mizuho Bank, Ltd., as Collateral Agent	8-K	001-04721	10.3	4/29/2016	
10.23	Performance Support Agreement (Tranche 2), dated as of April 28, 2016, by Sprint Corporation in favor of Mobile Leasing Solutions, LLC, acting for itself and on behalf of Series 2 thereof	8-K	001-04721	10.4	4/29/2016	
10.24	Guaranty (Tranche 2), dated as of April 28, 2016, by Sprint Corporation in favor of Mobile Leasing Solutions, LLC, acting for itself and on behalf of Series 2 thereof	8-K	001-04721	10.5	4/29/2016	
10.25	Credit Agreement, dated as of April 28, 2016, among Sprint Communications, Inc., as borrower, Sprint Corporation and certain subsidiaries of Sprint Communications, Inc., as guarantors, and Mizuho Bank, Ltd., as administrative agent, arranger and bookrunner	8-K	001-04721	10.6	4/29/2016	
10.26	First Amendment, dated as of June 29, 2016, to the Credit Agreement, dated as of April 28, 2016, by and between Sprint Communications, Inc. and Mizuho Bank, Ltd.	10-Q	001-04721	10.1	11/1/2016	
10.27	Incremental Agreement No. 1, dated as of June 29, 2016, to the Credit Agreement, dated as of April 28, 2016, by and among Sprint Communications, Inc., the Guarantors party thereto, the Lenders parties thereto, and Mizuho Bank, Ltd., as Arranger, Bookrunner, and administrative agent for the Lenders	10-Q	001-04721	10.2	11/1/2016	
10.28	Guarantee and Collateral Agreement, dated October 27, 2016, among Deutsche Bank Trust Company Americas, Sprint Spectrum PledgeCo LLC, Sprint Spectrum PledgeCo II LLC, Sprint Spectrum PledgeCo III LLC, Sprint Spectrum License Holder LLC, Sprint Spectrum License Holder II LLC and Sprint Spectrum License Holder III LLC.	8-K	001-04721	10.1	11/2/2016	
10.29	Intra-Company Spectrum Lease Agreement, dated as of October 27, 2016, among Sprint Spectrum License Holder LLC, Sprint Spectrum License Holder II LLC and Sprint Spectrum License Holder III LLC, Sprint Communications, Inc., Sprint Intermediate Holdco LLC,	8-K	001-04721	10.2	11/2/2016	

Sprint Intermediate Holdco II LLC, Sprint Intermediate  
Holdco III LLC and the guarantors named therein.

Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
10.30	Warrant Agreement for Sprint Corporation Common Stock, dated as of July 10, 2013, by and between Sprint Corporation and Starburst I, Inc.	8-K	001-04721	10.6	7/11/2013	
<b>(10) Executive Compensation Plans and Arrangements</b>						
10.31	Summary of 2014 Long-Term Incentive Plan	8-K	001-04721		10/9/2014	
10.32	STI and LTI Plan Information	10-Q	001-04721	10.4	8/7/2015	
10.33	Form of Evidence of Award Agreement (awarding restricted stock units) under the 2007 Omnibus Incentive Plan to Section 16 officers other than Robert L. Johnson	10-Q	001-04721	10.21	11/6/2013	
10.34	Form of Evidence of Award Agreement (awarding performance-based restricted stock units) under the 2007 Omnibus Incentive Plan to Joseph J. Euteneuer	10-Q	001-04721	10.24	11/6/2013	
10.35	Form of Evidence of Award Agreement (awarding performance-based restricted stock units) under the 2007 Omnibus Incentive Plan to Section 16 officers other than Messrs. Robert L. Johnson and Joseph J. Euteneuer	10-Q	001-04721	10.23	11/6/2013	
10.36	Form of Award Agreement (awarding performance-based restricted stock units) under the 2014 Long-Term Incentive Plan to Joseph J. Euteneuer	10-Q	001-04721	10.4	8/8/2014	
10.37	Form of Award Agreement (awarding performance-based restricted stock units) under the 2014 Long-Term Incentive Plan to executive officers other than Messrs. Euteneuer and Johnson and Section 16 officers	10-Q	001-04721	10.6	8/8/2014	
10.38	Form of Award Agreement (awarding performance-based restricted stock units) under the 2014 Long-Term Incentive Plan to Section 16 officers other than Messrs. Euteneuer and Johnson	10-Q	001-04721	10.7	8/8/2014	
10.39	Form of Award Agreement (awarding restricted stock units) under the 2014 Long-Term Incentive Plan to all executive officers other than Robert L. Johnson	10-Q	001-04721	10.9	8/8/2014	
10.40	Form of Award Agreement (awarding stock options) under the 2014 Long-Term Incentive Plan for executive officers with Sprint employment agreements	10-Q	001-04721	10.11	8/8/2014	
10.41	Form of Award Agreement (awarding stock options) under the 2014 Long-Term Incentive Plan to executive officers other than those with Sprint employment agreements and Robert L. Johnson	10-Q	001-04721	10.12	8/8/2014	
10.42	Form of Turnaround Incentive Award Agreement (awarding restricted stock units) under the 2015 Omnibus Incentive Plan for certain executive officers in exchange for reduced long-term incentive opportunities	10-Q	001-04721	10.6	11/9/2015	
10.43	Form of Turnaround Incentive Award Agreement (awarding restricted stock units) under the 2015 Omnibus	10-Q	001-04721	10.7	11/9/2015	

Incentive Plan for certain executive officers

Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
10.44	Form of Award Agreement (awarding stock options) under the 2015 Omnibus Incentive Plan to executive officers other than those with Sprint employment agreements and Robert L. Johnson	10-Q	001-04721	10.8	11/9/2015	
10.45	Form of Award Agreement (awarding restricted stock units) under the 2015 Omnibus Incentive Plan to executive officers other than Robert L. Johnson	10-Q	001-04721	10.9	11/9/2015	
10.46	Form of Award Agreement (awarding performance-based restricted stock units) under the 2015 Omnibus Incentive Plan to executive officers other than Robert L. Johnson	10-Q	001-04721	10.10	11/9/2015	
10.47	Form of Stock Option Agreement under the Stock Option Exchange Program (for certain Nextel Communication Inc. employees)	Sch. TO-I	005-41991	d(2)	5/17/2010	
10.48	Form of Stock Option Agreement under the Stock Option Exchange Program (for all other employees other than those with Nextel employment agreements)	Sch. TO- IIA	005-41991	d(3)	5/21/2010	
10.49	Amended and Restated Employment Agreement, effective as of August 11, 2015, by and between Sprint Corporation and Raul Marcelo Claire	8-K	001-04721	10.1	8/11/2015	
10.50	Employment Agreement, executed December 20, 2010, effective April 4, 2011, by and between Joseph J. Euteneuer and Sprint Nextel Corporation	8-K	001-04721	10.1	12/21/2010	
10.51	First Amendment to Employment Agreement, dated November 20, 2012, by and between Sprint Nextel Corporation and Joseph J. Euteneuer	8-K	001-04721	10.3	11/20/2012	
10.52	Second Amendment to Employment Agreement, dated November 11, 2013, by and between Joseph J. Euteneuer and Sprint Communications, Inc.	8-K	001-04721	10.1	11/12/2013	
10.53	Third Amendment to Employment Agreement, dated November 14, 2014, between Sprint Communications, Inc. and Joseph J. Euteneuer	10-Q	001-04721	10.4	2/5/2015	
10.54	Fourth Amendment to Employment Agreement, effective November 6, 2015, by and between Sprint Nextel Corporation, now known as Sprint Communications, Inc., and Joseph Euteneuer	8-K	001-04721	10.1	11/12/2015	
10.55	Employment Agreement, effective September 6, 2013 by and between Sprint Corporation and Brandon Dow Draper	10-Q	001-04721	10.25	11/6/2013	
10.56	Brandon Dow Draper Sign-On Award of Restricted Stock Units	10-Q	001-04721	10.26	11/6/2013	
10.57	First Amendment to Employment Agreement, dated February 21, 2014, by and between Sprint Corporation and Brandon Dow Draper	10-KT	001-04721	10.78	5/23/2014	

7/20/2017

Document

10.58

Employment Agreement, dated January 2, 2016, by and  
between Sprint Corporation and Jorge Gracia

10-Q

001-04721

10.12

2/4/2016

68

Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
10.59	Employment Agreement, effective May 20, 2014, by and between Sprint Corporation and John C. Saw	10-Q	001-04721	10.1	8/8/2014	
10.60	First Amendment to Employment Agreement, effective October 20, 2014, by and between Sprint Corporation and John C. Saw	10-Q	001-04721	10.3	11/6/2014	
10.61	Second Amendment to Employment Agreement, effective July 27, 2015, by and between Sprint Corporation and John C. Saw	10-Q	001-04721	10.1	11/9/2015	
10.62	Amended and Restated Employment Agreement, effective December 31, 2008, by and between Sprint Nextel Corporation and Jaime A. Jones	10-K	001-04721	10.68	5/26/2015	
10.63	First Amendment to Amended and Restated Employment Agreement, effective December 13, 2012, by and between Sprint Nextel Corporation and Jaime A. Jones	10-K	001-04721	10.69	5/26/2015	
10.64	Second Amendment to Amended and Restated Employment Agreement, effective December 13, 2012, by and between Sprint Nextel Corporation and Jaime A. Jones	10-K	001-04721	10.76	5/17/2016	
10.65	Employment Agreement, effective August 3, 2015, by and between Sprint Corporation and Guenther Ottendorfer	10-Q	001-04721	10.2	11/9/2015	
10.66	Employment Agreement, dated August 2, 2015, by and between Sprint Corporation and Tarek Robbiati	8-K	001-04721	10.1	8/3/2015	
10.67	Amended and Restated Agreement Regarding Special Compensation and Post Employment Restrictive Covenants, dated December 31, 2008, by and between Sprint Nextel Corporation and Paul W. Schieber	10-K	001-04721	10.80	2/24/2014	
10.68	First Amendment to Amended and Restated Agreement Regarding Special Compensation and Post Employment Restrictive Covenants, dated December 11, 2012, by and between Sprint Nextel Corporation and Paul W. Schieber	10-K	001-04721	10.81	2/24/2014	
10.69	Employment Agreement, dated May 1, 2015, by and between Sprint Corporation and Roger Sole Rafols	10-Q	001-04721	10.11	2/4/2016	
10.70	Employment Agreement, dated May 31, 2015, by and between Sprint Corporation and Kevin Crull	10-Q	001-04721	10.3	8/7/2015	
10.71	Summary of Compensation Committee approval of additional monthly flight hours as provided under the Amended and Restated Employment Agreement, effective as of August 11, 2015, by and between Sprint Corporation and Raul Marcelo Claire	10-Q	001-04721	10.3	8/9/2016	
10.72	Form of Award Agreement (awarding restricted stock units) under the 2015 Omnibus Incentive Plan with covenants and restrictions to executive officers	10-Q	001-04721	10.4	8/9/2016	

10.73

Form of Award Agreement (awarding performance-based restricted stock units) under the 2015 Omnibus Incentive Plan with covenants and restrictions to executive officers

10-Q

001-04721

10.5

8/9/2016

Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
10.74	Form of Turnaround Incentive Award Agreement (awarding performance-based restricted stock units) under the 2015 Omnibus Incentive Plan for certain executive officers with proration after two years	10-Q	001-04721	10.6	8/9/2016	
10.75	Form of Award Agreement (awarding stock options) under the 2015 Omnibus Incentive Plan with covenants and restrictions to executive officers without special compensation arrangements	10-Q	001-04721	10.7	8/9/2016	
10.76	Form of Award Agreement (awarding stock options) under the 2015 Omnibus Incentive Plan to executive officers with special compensation arrangements	10-Q	001-04721	10.8	8/9/2016	
10.77	Form of Turnaround Incentive Award Agreement (awarding performance-based restricted stock units) under the 2015 Omnibus Incentive Plan with proration after two years	10-Q	001-04721	10.1	11/1/2016	
10.78	Employment Agreement, executed as of January 19, 2017, between Nestor Cano and Sprint Corporation	8-K	001-04721	10.1	1/24/2017	
10.79	Retention Award Letter for Roger Sole effective as of January 18, 2017	10-Q	001-04721	10.3	2/6/2017	
10.80	Sprint Corporation 2007 Omnibus Incentive Plan	8-K	001-04721	10.2	9/20/2013	
10.81	Sprint Corporation Amended and Restated 2015 Omnibus Incentive Plan	10-Q	001-04721	10.1	2/6/2017	
10.82	Sprint Corporation Change in Control Severance Plan	10-K	001-04721	10.88	5/17/2016	
10.83	Sprint Corporation Deferred Compensation Plan, as amended and restated effective September 26, 2014	10-Q	001-04721	10.2	11/6/2014	
10.84	Executive Deferred Compensation Plan, as amended and restated effective January 1, 2008	10-K	001-04721	10.35	2/27/2009	
10.85	Summary of Director Compensation Programs	10-Q	001-04721	10.19	11/6/2013	
10.86	Director's Deferred Fee Plan, as amended and restated effective January 1, 2008	10-K	001-04721	10.37	2/27/2009	
10.87	Form of Award Agreement (awarding restricted stock units) under the 2007 Omnibus Incentive Plan for non-employee directors	10-Q	001-04721	10.10	5/9/2007	
10.88	Form of Award Agreement (awarding restricted stock units) under the 2015 Omnibus Incentive Plan for non-employee directors	10-Q	001-04721	10.5	11/9/2015	
10.89	Form of Election to Defer Delivery of Shares Subject to RSUs (Outside Directors)	10-K	001-04721	10.95	5/17/2016	
10.90	Form of Indemnification Agreement to be entered into by and between Sprint Corporation and certain of its directors	8-K	001-04721	10.1	7/11/2013	

10.91 Form of Indemnification Agreement to be entered into by  
and between Sprint Corporation and certain of its officers

8-K 001-04721 10.2 7/11/2013

Table of Contents

Exhibit No.	Exhibit Description	Form	Incorporated by Reference			Filed/Furnished Herewith
			SEC File No.	Exhibit	Filing Date	
10.92	Form of Indemnification Agreement to be entered into by and between Sprint Corporation and certain individuals who serve as both a director and officer of Sprint Corporation	8-K	001-04721	10.3	7/11/2013	
12	Computation of Ratio of Earnings to Fixed Charges					*
<b>(21) Subsidiaries of the Registrant</b>						
21	Subsidiaries of the Registrant					*
<b>(23) Consents of Experts and Counsel</b>						
23.1	Consent of Deloitte & Touche LLP, Independent Registered Public Accounting Firm					*
<b>(31) and (32) Officer Certifications</b>						
31.1	Certification of Chief Executive Officer Pursuant to Securities Exchange Act of 1934 Rule 13a-14(a)					*
31.2	Certification of Chief Financial Officer Pursuant to Securities Exchange Act of 1934 Rule 13a-14(a)					*
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes Oxley Act of 2002					*
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes Oxley Act of 2002					*
<b>(101) Formatted in XBRL (Extensible Business Reporting Language)</b>						
101.INS	XBRL Instance Document					*
101.SCH	XBRL Taxonomy Extension Schema Document					*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document					*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document					*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document					*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document					*

\* Filed or furnished, as required.

\*\* Schedules and/or exhibits not filed will be furnished to the SEC upon request, pursuant to Item 601(b)(2) of Regulation S-K.

Table of Contents

**SPRINT CORPORATION**  
**Index to Consolidated Financial Statements**

	<u>Page Reference</u>
<b><u>Sprint Consolidated Financial Statements</u></b>	
<u>Report of Independent Registered Public Accounting Firm</u>	<u>F-2</u>
<u>Consolidated Balance Sheets as of March 31, 2017 and 2016</u>	<u>F-3</u>
<u>Consolidated Statements of Operations for the years ended March 31, 2017, 2016 and 2015</u>	<u>F-4</u>
<u>Consolidated Statements of Comprehensive Loss for the years ended March 31, 2017, 2016 and 2015</u>	<u>F-5</u>
<u>Consolidated Statements of Cash Flows for the years ended March 31, 2017, 2016 and 2015</u>	<u>F-6</u>
<u>Consolidated Statements of Stockholders' Equity for the years ended March 31, 2017, 2016 and 2015</u>	<u>F-7</u>
<u>Notes to the Consolidated Financial Statements</u>	<u>F-8</u>

Table of ContentsIndex to Consolidated Financial Statements**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Stockholders of  
Sprint Corporation  
Overland Park, Kansas

We have audited the accompanying consolidated balance sheets of Sprint Corporation and subsidiaries (the "Company") as of March 31, 2017 and 2016, and the related consolidated statements of operations, comprehensive loss, cash flows and stockholders' equity for each of the three years in the period ended March 31, 2017. We also have audited the Company's internal control over financial reporting as of March 31, 2017, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sprint Corporation and subsidiaries as of March 31, 2017 and 2016, and the related results of their operations and their cash flows for each of the three years in the period ended March 31, 2017, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of March 31, 2017, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission.

/s/ DELOITTE & TOUCHE LLP

Kansas City, Missouri  
May 26, 2017

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**

	March 31,	
	2017	2016
	(in millions, except share and per share data)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 2,870	\$ 2,641
Short-term investments	5,444	—
Accounts and notes receivable, net	4,138	1,099
Device and accessory inventory	1,064	1,173
Prepaid expenses and other current assets	601	1,920
Total current assets	14,117	6,833
Property, plant and equipment, net	19,209	20,297
Intangible assets		
Goodwill	6,579	6,575
FCC licenses and other	40,585	40,073
Definite-lived intangible assets, net	3,320	4,469
Other assets	1,313	728
Total assets	\$ 85,123	\$ 78,975
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 3,281	\$ 2,899
Accrued expenses and other current liabilities	4,141	4,374
Current portion of long-term debt, financing and capital lease obligations	5,036	4,690
Total current liabilities	12,458	11,963
Long-term debt, financing and capital lease obligations	35,878	29,268
Deferred tax liabilities	14,416	13,959
Other liabilities	3,563	4,002
Total liabilities	66,315	59,192
Commitments and contingencies		
Stockholders' equity:		
Common stock, voting, par value \$0.01 per share, 9.0 billion authorized, 3.989 billion and 3.975 billion issued at March 31, 2017 and 2016	40	40
Paid-in capital	27,756	27,563
Treasury shares, at cost	—	(3)
Accumulated deficit	(8,584)	(7,378)
Accumulated other comprehensive loss	(404)	(439)
Total stockholders' equity	18,808	19,783
Total liabilities and stockholders' equity	\$ 85,123	\$ 78,975

*See Notes to the Consolidated Financial Statements*

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions, except per share amounts)</i>		
Net operating revenues:			
Service	\$ 25,368	\$ 27,174	\$ 29,542
Equipment	7,979	5,006	4,990
	<u>33,347</u>	<u>32,180</u>	<u>34,532</u>
Net operating expenses:			
Cost of services (exclusive of depreciation and amortization below)	7,861	9,439	9,660
Cost of products (exclusive of depreciation and amortization below)	7,077	5,795	9,309
Selling, general and administrative	7,994	8,479	9,563
Impairments	—	—	2,133
Severance and exit costs	66	409	304
Depreciation	7,098	5,794	3,797
Amortization	1,052	1,294	1,552
Other, net	435	660	109
	<u>31,583</u>	<u>31,870</u>	<u>36,427</u>
Operating income (loss)	<u>1,764</u>	<u>310</u>	<u>(1,895)</u>
Other expense:			
Interest expense	(2,495)	(2,182)	(2,051)
Other (expense) income, net	(40)	18	27
	<u>(2,535)</u>	<u>(2,164)</u>	<u>(2,024)</u>
Loss before income taxes	(771)	(1,854)	(3,919)
Income tax (expense) benefit	(435)	(141)	574
Net loss	<u>\$ (1,206)</u>	<u>\$ (1,995)</u>	<u>\$ (3,345)</u>
Basic and diluted net loss per common share	<u>\$ (0.30)</u>	<u>\$ (0.50)</u>	<u>\$ (0.85)</u>
Basic and diluted weighted average common shares outstanding	<u>3,981</u>	<u>3,969</u>	<u>3,953</u>

*See Notes to the Consolidated Financial Statements*

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS**

	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Net loss	\$ (1,206)	\$ (1,995)	\$ (3,345)
Other comprehensive income (loss), net of tax:			
Foreign currency translation adjustment	(1)	(11)	(25)
Net unrealized holding losses on derivatives	(2)	—	—
Net unrealized holding losses on securities	—	(1)	(6)
Unrecognized net periodic pension and other postretirement benefits:			
Net actuarial gain (loss)	35	(38)	(393)
Net prior service credits arising during the period	—	9	—
Less: Amortization of actuarial loss, included in net loss	3	10	—
Less: Settlement event charge, included in net loss	—	—	59
Net unrecognized net periodic pension and other postretirement benefits	38	(19)	(334)
Other comprehensive income (loss)	35	(31)	(365)
Comprehensive loss	<u>\$ (1,171)</u>	<u>\$ (2,026)</u>	<u>\$ (3,710)</u>

*See Notes to the Consolidated Financial Statements*

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Cash flows from operating activities:			
Net loss	\$ (1,206)	\$ (1,995)	\$ (3,345)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Impairments	—	—	2,133
Depreciation and amortization	8,150	7,088	5,349
Provision for losses on accounts receivable	555	455	892
Share-based and long-term incentive compensation expense	93	75	86
Deferred income tax expense (benefit)	433	123	(609)
Gains from asset dispositions and exchanges	(354)	—	—
Amortization of long-term debt premiums, net	(302)	(316)	(303)
Loss on disposal of property, plant and equipment	509	487	—
Litigation and other contingencies	140	193	91
Contract terminations	111	—	—
Other changes in assets and liabilities			
Accounts and notes receivable	(1,017)	(1,663)	(644)
Deferred purchase price from sale of receivables	(289)	2,478	—
Inventories and other current assets	(2,305)	(3,065)	(1,573)
Accounts payable and other current liabilities	(365)	(574)	481
Non-current assets and liabilities, net	(308)	111	(199)
Other, net	323	500	91
Net cash provided by operating activities	<u>4,168</u>	<u>3,897</u>	<u>2,450</u>
Cash flows from investing activities			
Capital expenditures - network and other	(1,950)	(4,680)	(5,422)
Capital expenditures - leased devices	(1,925)	(2,292)	(582)
Expenditures relating to FCC licenses	(83)	(98)	(163)
Reimbursements relating to FCC licenses	—	—	95
Proceeds from sales and maturities of short-term investments	4,621	418	3,131
Purchases of short-term investments	(10,065)	(252)	(2,077)
Proceeds from sales of assets and FCC licenses	219	62	315
Proceeds from sale-leaseback transaction	—	1,136	—
Other, net	(42)	(29)	(11)
Net cash used in investing activities	<u>(9,225)</u>	<u>(5,735)</u>	<u>(4,714)</u>
Cash flows from financing activities:			
Proceeds from debt and financings	10,966	1,355	1,930
Repayments of debt, financing and capital lease obligations	(5,417)	(899)	(574)
Debt financing costs	(358)	(11)	(87)
Other, net	95	24	35

Net cash provided by financing activities	5,286	469	1,304
Net increase (decrease) in cash and cash equivalents	229	(1,369)	(960)
Cash and cash equivalents, beginning of period	2,641	4,010	4,970
Cash and cash equivalents, end of period	<u>\$ 2,870</u>	<u>\$ 2,641</u>	<u>\$ 4,010</u>

*See Notes to the Consolidated Financial Statements*

F-6

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
*(in millions)*

	Common Stock		Paid-in Capital	Treasury Shares		Accumulated Deficit	Accumulated Other Comprehensive Loss	Total
	Shares	Amount		Shares	Amount			
Balance, March 31, 2014	3,941	\$ 39	\$ 27,354	—	\$ —	\$ (2,038)	\$ (43)	\$ 25,312
Net loss						(3,345)		(3,345)
Other comprehensive loss, net of tax							(365)	(365)
Issuance (repurchase) of common stock, net	26	1	41	1	(7)			35
Share-based compensation expense			71					71
Capital contribution by SoftBank			2					2
Balance, March 31, 2015	3,967	\$ 40	\$ 27,468	1	\$ (7)	\$ (5,383)	\$ (408)	\$ 21,710
Net loss						(1,995)		(1,995)
Other comprehensive loss, net of tax							(31)	(31)
Issuance of common stock, net	7		6		4			10
Share-based compensation expense			71					71
Capital contribution by SoftBank			14					14
Other, net			4					4
Balance, March 31, 2016	3,974	\$ 40	\$ 27,563	1	\$ (3)	\$ (7,378)	\$ (439)	\$ 19,783
Net loss						(1,206)		(1,206)
Other comprehensive income, net of tax							35	35
Issuance of common stock, net	15		47	(1)	3			50
Share-based compensation expense			91					91
Capital contribution by SoftBank			6					6
Other, net			49					49
Balance, March 31, 2017	3,989	\$ 40	\$ 27,756	—	\$ —	\$ (8,584)	\$ (404)	\$ 18,808

*See Notes to the Consolidated Financial Statements*

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**INDEX**

	<u>Page Reference</u>
1. <u>Description of Operations</u>	<u>F-9</u>
2. <u>Summary of Significant Accounting Policies and Other Information</u>	<u>F-9</u>
3. <u>Funding Sources</u>	<u>F-18</u>
4. <u>Installment Receivables</u>	<u>F-21</u>
5. <u>Financial Instruments</u>	<u>F-22</u>
6. <u>Property, Plant and Equipment</u>	<u>F-23</u>
7. <u>Intangible Assets</u>	<u>F-25</u>
8. <u>Long-Term Debt, Financing and Capital Lease Obligations</u>	<u>F-27</u>
9. <u>Severance and Exit Costs</u>	<u>F-31</u>
10. <u>Supplemental Financial Information</u>	<u>F-32</u>
11. <u>Income Taxes</u>	<u>F-33</u>
12. <u>Commitments and Contingencies</u>	<u>F-36</u>
13. <u>Stockholders' Equity and Per Share Data</u>	<u>F-39</u>
14. <u>Segments</u>	<u>F-39</u>
15. <u>Quarterly Financial Data</u>	<u>F-43</u>
16. <u>Related-Party Transactions</u>	<u>F-43</u>
17. <u>Guarantor Financial Information</u>	<u>F-45</u>
18. <u>Subsequent Events</u>	<u>F-54</u>

Table of Contents

Index to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1. Description of Operations**

Sprint Corporation, including its consolidated subsidiaries, is a communications company offering a comprehensive range of wireless and wireline communications products and services that are designed to meet the needs of individual consumers, businesses, government subscribers and resellers.

The Wireless segment includes retail, wholesale, and affiliate service revenue from a wide array of wireless voice and data transmission services and equipment revenue from the sale or lease of wireless devices and the sale of accessories in the U.S., Puerto Rico and the U.S. Virgin Islands. The Wireline segment includes revenue from domestic and international wireline data communication services in addition to voice, data and IP communication services provided to our Wireless segment.

On July 10, 2013, SoftBank Corp., which subsequently changed its name to SoftBank Group Corp., and certain of its wholly-owned subsidiaries (together, "SoftBank") completed the merger (SoftBank Merger) with Sprint Nextel as contemplated by the Agreement and Plan of Merger, dated as of October 15, 2012 (as amended, the Merger Agreement) and the Bond Purchase Agreement, dated as of October 15, 2012 (as amended, the Bond Agreement). As a result of the SoftBank Merger, Starburst II, Inc. (Starburst II) became the parent company of Sprint Nextel. Immediately thereafter, Starburst II changed its name to Sprint Corporation and Sprint Nextel changed its name to Sprint Communications, Inc. (Sprint Communications). As a result of the completion of the SoftBank Merger in which SoftBank acquired an approximate 78% interest in Sprint Corporation, and subsequent open market stock purchases, SoftBank owned approximately 83% of the outstanding common stock of Sprint Corporation as of March 31, 2017.

**Note 2. Summary of Significant Accounting Policies and Other Information**

**Basis of Consolidation and Estimates**

The consolidated financial statements include our accounts, those of our 100% owned subsidiaries, and subsidiaries we control or in which we have a controlling financial interest. All intercompany transactions and balances have been eliminated in consolidation.

The consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States (U.S. GAAP). This requires management of the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses and the disclosure of contingent assets and liabilities as of the date of the consolidated financial statements. Significant estimates and assumptions are used for, but are not limited to, allowance for doubtful accounts, estimated economic lives and residual values of property, plant and equipment, fair value of identified purchased tangible and intangible assets in a business combination and fair value assessments for purposes of impairment testing.

Certain prior period amounts have been reclassified to conform to the current period presentation.

***Change in Estimate***

When estimating the value of returned inventory, we evaluate many factors and obtain information to support the estimated value of used devices and their useful lives. During the year ended March 31, 2015, we observed sustained value and extended useful lives for handsets leading to an increase in the estimated value for returned inventory. As a result, we revised our methodology and assumptions used in estimating the value for returned handsets during the year ended March 31, 2015.

The change in estimate was accounted for on a prospective basis. The effect of the change in estimate, which was included in "Cost of products" in our consolidated statements of operations, reduced our operating loss by approximately \$80 million, or \$0.02 per basic and diluted share, for the year ended March 31, 2015.

**Summary of Significant Accounting Policies**

***Cash and Cash Equivalents***

Cash equivalents generally include highly liquid investments with maturities at the time of purchase of three months or less. These investments may include money market funds, certificates of deposit, U.S. government and government-sponsored debt securities, corporate debt securities, municipal securities, bank-related securities, and credit and debit card transactions in process. The carrying amounts approximate fair value.

Table of ContentsIndex to Consolidated Financial Statements**SPRINT CORPORATION  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS*****Short-Term Investments***

Short-term investments generally include time deposits and commercial paper with terms greater than three months but less than one year at the date of purchase. The carrying amounts are recorded at amortized cost and approximate fair value. The interest earned is recognized in the consolidated statements of operations over the contractual term of the short-term investments.

***Installment Receivables***

The carrying value of installment receivables approximates fair value because the receivables are recorded at their present value, net of the deferred interest and allowance for credit losses. At the time of the installment sale, we impute interest on the installment receivable and record it as a reduction to revenue and as a reduction to the face amount of the related receivable. Interest income is recognized over the term of the installment contract in service revenue.

We categorize our installment receivables as prime and subprime based upon subscriber credit profiles and as unbilled, billed-current and billed-past due based upon the age of the receivable. We use proprietary scoring systems that measure the credit quality of our receivables using several factors, such as credit bureau information, subscriber credit risk scores and service plan characteristics. Payment history is subsequently monitored to further evaluate credit profiles. Prime subscriber receivables are those with lower delinquency risk and subprime subscriber receivables are those with higher delinquency risk. Subscribers within the subprime category may be required to make a down payment on their device and accessory purchases. Installment receivables for which invoices have not yet generated for the customer are considered unbilled. Installment receivables for which invoices have been generated but which are not past the contractual due date are considered billed-current. Installment receivables for which invoices have been generated and the payment is approximately ten days past the contractual due date are considered billed-past due. Account balances are written-off if collection efforts are unsuccessful and future collection is unlikely based on the length of time from the day accounts become past due.

***Allowance for Doubtful Accounts***

An allowance for doubtful accounts is established to cover probable and reasonably estimable losses. Because of the number of subscriber accounts, it is not practical to review the collectability of each of those accounts individually to determine the amount of allowance for doubtful accounts each period, although some account level analysis is performed with respect to large wireless and wireline subscribers. The estimate of allowance for doubtful accounts considers a number of factors, including collection experience, aging of the remaining accounts receivable portfolios, credit quality of the subscriber base and other qualitative considerations, including macro-economic factors. Account balances are written off if collection efforts are unsuccessful and future collection is unlikely based on the length of time from the day accounts become past due. Amounts written off against the allowance for doubtful accounts, net of recoveries and other adjustments, were \$371 million, \$612 million, and \$752 million for the years ended March 31, 2017, 2016, and 2015, respectively. See *Note 4. Installment Receivables* for additional information as it relates to the allowance for doubtful accounts specifically attributable to installment receivables.

***Device and Accessory Inventory***

Inventories are stated at the lower of cost or market. Cost is determined by the first-in, first-out (FIFO) method. The Company sells wireless devices separately or in conjunction with a service contract. A device sold with a service contract may be sold below cost, as any promotional discounts on the device are expected to be recovered through the service contract.

The net realizable value of devices and other inventory is analyzed on a regular basis. This analysis includes assessing obsolescence, sales forecasts, product life cycle, marketplace and other considerations. If assessments regarding the above factors adversely change, we may sell devices at higher prices or record a write-down to inventory for obsolete or slow-moving items prior to the point of sale.

***Property, Plant and Equipment***

Property, plant and equipment (PP&E), including improvements that extend useful lives, are recognized at cost. Depreciation on PP&E is generally calculated using the straight-line method based on estimated economic useful lives of 3 to 30 years for buildings and improvements and network equipment, site costs and related software and 3 to 12 years for non-network internal use software, office equipment and other. Leasehold improvements are depreciated over the shorter of the

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

lease term or the estimated useful life of the respective assets. Leased devices are depreciated using the straight-line method to their estimated residual value generally over the term of the lease. We calculate depreciation on certain network assets using the group life method. Accordingly, ordinary asset retirements and disposals on those assets are charged against accumulated depreciation with no gain or loss recognized. Gains or losses associated with all other asset retirements or disposals are recognized in "Other, net" in the consolidated statements of operations. Depreciation rates for assets are revised periodically to account for changes, if any, related to management's strategic objectives, technological changes, changes in estimated residual values, or obsolescence. Changes in our estimates will result in adjustment to depreciation prospectively over the estimated useful lives of our non-leased assets and over the remaining period of benefit for devices leased to our customers. Repair and maintenance costs and research and development costs are expensed as incurred.

We capitalize costs for network and non-network software developed or obtained for internal use during the application development stage. These costs are included in PP&E and, when the software is placed in service, are depreciated over estimated useful lives of three to five years. Costs incurred during the preliminary project and post-implementation stage, as well as maintenance and training costs, are expensed as incurred.

***Long-Lived Asset Impairment***

Sprint evaluates long-lived assets, including intangible assets subject to amortization, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset group may not be recoverable. Asset groups are determined at the lowest level for which identifiable cash flows are largely independent of cash flows of other groups of assets and liabilities. When the carrying amount of a long-lived asset group is not recoverable and exceeds its fair value, an impairment loss is recognized equal to the excess of the asset group's carrying value over the estimated fair value. See *Note 6. Property, Plant and Equipment* for additional information on long-lived asset impairments.

Certain assets that have not yet been deployed in the business, including network equipment, cell site development costs and software in development, are periodically assessed to determine recoverability. Network equipment and cell site development costs are expensed whenever events or changes in circumstances cause the Company to conclude the assets are no longer needed to meet management's strategic network plans and will not be deployed. Software development costs are expensed when it is no longer probable that the software project will be deployed. Network equipment that has been removed from the network is also periodically assessed to determine recoverability. If we experience significant operational challenges, including retaining and attracting subscribers, future cash flows of the Company may not be sufficient to recover the carrying value of our wireless asset group, and we could record asset impairments that are material to Sprint's consolidated results of operations and financial condition.

***Indefinite-Lived Intangible Assets***

Our indefinite-lived intangible assets primarily consist of goodwill, certain of our trademarks and FCC licenses. Goodwill represents the excess of consideration paid over the estimated fair value of the net tangible and identifiable intangible assets acquired in business combinations. In determining whether an intangible asset, other than goodwill, is indefinite-lived, we consider the expected use of the assets, the regulatory and economic environment within which they are being used, and the effects of obsolescence on their use. We assess our indefinite-lived intangible assets, including goodwill, for impairment at least annually or, if necessary, more frequently, whenever events or changes in circumstances indicate the asset may be impaired.

These analyses, which include the determination of fair value, require considerable judgment and are highly sensitive to changes in underlying assumptions. Consequently, there can be no assurance that the estimates and assumptions made for the purposes of estimating the fair values of our indefinite-lived assets, including goodwill, will prove to be an accurate prediction of the future. Sustained declines in the Company's operating results, number of wireless subscribers, forecasted future cash flows, growth rates and other assumptions, as well as significant, sustained declines in the Company's stock price and related market capitalization could impact the underlying key assumptions and our estimated fair values, potentially leading to a future material impairment of goodwill or other indefinite-lived intangible assets. See *Note 7. Intangible Assets* for additional information on indefinite-lived intangible asset impairments.

Table of ContentsIndex to Consolidated Financial Statements**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS*****Derivatives and Hedging***

The Company uses derivative instruments to hedge its exposure to interest rate risks arising from operating and financing activities. In accordance with its risk management policies, the Company does not hold or issue derivative instruments for trading or speculative purposes.

Derivatives are recognized in the consolidated balance sheets at their fair values. When the Company becomes a party to a derivative instrument and intends to apply hedge accounting, it formally documents the hedge relationship and the risk management objective for undertaking the hedge which includes designating the instrument for financial reporting purposes as a fair value hedge, a cash flow hedge, or a net investment hedge. The accounting for changes in fair value of a derivative instrument depends on whether the Company had designated it in a qualifying hedging relationship and further, on the type of hedging relationship. At March 31, 2017, the Company only held and applied hedge accounting for derivatives designated as cash flow hedges.

Changes in the fair value of a derivative not designated in a hedging relationship are recognized in the consolidated statements of operations along with the ineffective portions of changes in the fair value of derivatives designated in hedging relationships.

The effective portion of changes in the fair value of a derivative designated as a cash flow hedge is recorded in "Other comprehensive income (loss)" in the consolidated statements of comprehensive loss and reclassified into earnings in the period or periods during which the hedged item affects earnings.

For derivative instruments designated as hedges, the Company assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. Highly effective means that cumulative changes in the fair value of the derivative are between 80% and 125% of the cumulative changes in the fair value of the hedged item. In addition, when the Company determines that a derivative is not highly effective as a hedge, hedge accounting is discontinued. When it is probable that a hedged forecasted transaction will not occur, the Company discontinues hedge accounting for the affected portion of the forecasted transaction, and reclassifies any gains or losses in "Accumulated other comprehensive loss" to earnings in the consolidated statements of operations. When a derivative in a hedge relationship is terminated or the hedged item is sold, extinguished or terminated, hedge accounting is discontinued prospectively.

***Benefit Plans***

We provide a defined benefit pension plan and other postretirement benefits to certain employees, and we sponsor a defined contribution plan for all employees.

In June 2014, the Company's Board of Directors approved a plan amendment to the Sprint Retirement Pension Plan (the Plan) to offer certain terminated participants, who had not begun to receive Plan benefits, the opportunity to voluntarily elect to receive their benefits as an immediate lump sum distribution. Upon expiration of the election period and completion of cash payments on November 28, 2014, the lump sum distribution, totaling approximately \$560 million, created a settlement event that resulted in a \$59 million charge, which is reflected in "Other, net" in the consolidated statements of operations, and a reduction in the projected benefit obligation of approximately \$300 million, impacted by the settlement as well as a change in the mortality tables and a change in the discount rate used to estimate the projected benefit obligation.

As of March 31, 2017 and 2016, the fair value of our pension plan assets and certain other postretirement benefit plan assets in aggregate was \$1.4 billion and \$1.3 billion, respectively, and the fair value of our projected benefit obligations in aggregate was \$2.2 billion in each period. As a result, the plans were underfunded by approximately \$800 million and \$900 million as of March 31, 2017 and 2016, respectively, and were recorded as a net liability in our consolidated balance sheets. Estimated contributions totaling approximately \$50 million are expected to be paid during the fiscal year 2017.

The offset to the pension liability is recorded in equity as a component of "Accumulated other comprehensive loss," net of tax, including \$35 million, \$29 million, and \$393 million for the years ended March 31, 2017, 2016, and 2015, respectively, which is amortized to "Selling, general and administrative" in our consolidated statements of operations. The change in the net liability of the Plan in the year ended March 31, 2017 was affected by the higher than expected actual rate of return on Plan assets experienced during the year. There was no change in the discount rate used to estimate the projected benefit obligation during the year ended March 31, 2017. The change in the net liability of the Plan in the year ended March 31, 2016 was affected by a change in the discount rate used to estimate the projected benefit obligation, increasing from 4.2%

Table of ContentsIndex to Consolidated Financial Statements**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

for the year ended March 31, 2015 to 4.3% for the year ended March 31, 2016, combined with a \$9 million prior service credit resulting from an amendment to one of the other postretirement benefit plans during 2015. The change in the net liability of the Plan in the year ended March 31, 2015 was affected by the impact of the settlement event on the projected benefit obligation combined with a change in the discount rate used to estimate the projected benefit obligation, decreasing from 4.9% for the three-month transition period ended March 31, 2014 to 4.2% for the year ended March 31, 2015. We intend to make future cash contributions to the Plan in an amount necessary to meet minimum funding requirements according to applicable benefit plan regulations.

As of December 31, 2005, the Plan was amended to freeze benefit plan accruals for participants. The objective for the investment portfolio of the pension plan is to achieve a long-term nominal rate of return, net of fees, which exceeds the plan's long-term expected rate of return on investments for funding purposes which was 7.75% for the years ended March 31, 2017 and 2016. To meet this objective, our investment strategy for the year ended March 31, 2017 was governed by an asset allocation policy, whereby a targeted allocation percentage is assigned to each asset class as follows: 38% to U.S. equities; 16% to international equities; 28% to fixed income investments; 9% to real estate investments; and 9% to other investments including hedge funds. Actual allocations are allowed to deviate from target allocation percentages within a range for each asset class as defined in the investment policy. The long-term expected rate of return on investments for funding purposes is 7.5% for the year ended March 31, 2018.

Investments of the Plan are measured at fair value on a recurring basis which is determined using quoted market prices or estimated fair values. As of March 31, 2017, 34% of the investment portfolio was valued at quoted prices in active markets for identical assets; 48% was valued using quoted prices for similar assets in active or inactive markets, or other observable inputs; and 18% was valued using unobservable inputs that are supported by little or no market activity, the majority of which used the net asset value per share (or its equivalent) as a practical expedient to measure the fair value.

Under our defined contribution plan, participants may contribute a portion of their eligible pay to the plan through payroll withholdings. For the year ended March 31, 2017 and the three-month period ended March 31, 2016, the Company matched 50% of the participants' pre-tax and Roth contribution (in aggregate) on the first 4% of eligible compensation. For the nine-month period ended December 31, 2015 and the year ended March 31, 2015, the Company matched 100% of the participants' pre-tax and Roth contribution (in aggregate) on the first 3% of eligible compensation and 50% of the participants' pre-tax and Roth contribution (in aggregate) on the next 2% of eligible compensation up to a maximum matching contribution of 4%. Fixed matching contributions totaled approximately \$28 million, \$54 million, and \$71 million for the years ended March 31, 2017, 2016, and 2015, respectively.

***Revenue Recognition***

Operating revenues primarily consist of wireless service revenues, revenues generated from device and accessory sales, revenues from leasing a device, revenues from wholesale operators and third-party affiliates, as well as long distance voice, data and Internet revenues. Service revenues consist of fixed monthly recurring charges, variable usage charges and miscellaneous fees such as directory assistance, roaming, equipment protection, late payment and early termination charges, interest, and certain regulatory related fees, net of service credits and other adjustments. We generally recognize service revenues as services are rendered, assuming all other revenue recognition criteria are met. We recognize revenue for access charges and other services charged at fixed amounts ratably over the service period, net of credits and adjustments for service discounts, billing disputes and fraud or unauthorized usage. As a result of the cutoff times of our multiple billing cycles each month, we are required to estimate the amount of subscriber revenues earned but not billed from the end of each billing cycle to the end of each reporting period. These estimates are based primarily on rate plans in effect and our historical usage and billing patterns. Regulatory fees and costs are recorded gross. The largest component of the regulatory fees is the Universal Service Fund, which represented no more than 2% of net operating revenues for all periods presented in the consolidated statements of operations.

We recognize equipment revenue and corresponding costs of equipment when title and risk of loss passes to the indirect dealer or end-use subscriber, assuming all other revenue recognition criteria are met. For arrangements involving multiple deliverables such as equipment and service, revenue is allocated to the deliverables based on their relative selling prices. Equipment revenue is limited to the amount of non-contingent consideration received when the device is sold to a subscriber. Equipment revenue is also reduced by the estimated amount of imputed interest associated with installment receivables for subscribers who elect to finance the purchase of a device for up to a 24-month period. When we subsidize the

Table of ContentsIndex to Consolidated Financial Statements**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

cost of the device as an incentive to retain and acquire subscribers, the cost of these incentives is recorded as a reduction to revenue upon activation of the device and a service contract.

If a multiple-element arrangement includes an option to purchase, on a monthly basis, an annual trade-in right, the amount of the total arrangement consideration is reduced by the estimated fair value of the trade-in right or the guarantee and the remaining proceeds are then allocated amongst the other deliverables in the arrangement.

Qualified subscribers can lease a device for a contractual period of time. At the end of the lease term, subscribers have the option to turn in their device, continue leasing their device or purchase the device. Accounting for device leases involves specific determinations under applicable lease accounting standards, which involve complex and prescriptive provisions. These provisions impact the timing and amount of revenue recognized for our leased devices. The critical elements that are considered with respect to our lease accounting are the economic life of the device and the fair value of the device, including the residual value. We only lease devices to qualifying subscribers that also purchase a service plan. To date, substantially all of our device leases were classified as operating leases. Revenues under these arrangements are allocated amongst the deliverables in the multiple-element arrangement considering the relative fair values of the lease and non-lease elements. The amount allocable to the operating lease element is included within equipment revenue in the consolidated results of operations and is recognized ratably over the lease term, which is typically two years or less.

The accounting estimates related to the recognition of revenue require us to make assumptions about numerous factors such as future billing adjustments for disputes with subscribers, unauthorized usage, future returns, mail-in rebates on device sales, the fair value of a trade-in right and the total arrangement consideration.

***Dealer Commissions***

Cash consideration given by us to a dealer or end-use subscriber is presumed to be a reduction of equipment revenue unless we receive, or will receive, an identifiable benefit in exchange for the consideration, and the fair value of such benefit can be reasonably estimated, in which case the consideration will generally be recorded as a selling expense or a purchase of inventory. We compensate our dealers using specific compensation programs related to the sale of our devices and our subscriber service contracts, or both. When a commission is earned by a dealer solely due to a selling activity relating to wireless service, the cost is recorded as a selling expense. Commissions are generally earned upon sale of device, service, or both, to an end-use subscriber. Incentive payments to dealers for sales associated with devices and service contracts are classified as contra-revenue, to the extent the incentive payment is reimbursement of loss on the device, and selling expense for the amount associated with the selling effort. Incentive payments to certain indirect dealers who purchase devices from other sources, such as the original equipment manufacturer (OEM), are recognized as selling expense when the device is activated with a Sprint service plan because Sprint does not recognize any equipment revenue or cost of products for those transactions.

***Severance and Exit Costs***

Liabilities for severance and exit costs are recognized based upon the nature of the cost to be incurred. For involuntary separation plans that are completed within the guidelines of our written involuntary separation plan, a liability is recognized when it is probable and reasonably estimable. For voluntary separation plans (VSP), a liability is recognized when the VSP is irrevocably accepted by the employee. For one-time termination benefits, such as additional severance pay or benefit payouts, and other exit costs, such as lease termination costs, the liability is measured and recognized initially at fair value in the period in which the liability is incurred, with subsequent changes to the liability recognized as adjustments in the period of change. Severance and exit costs associated with business combinations are recorded in the results of operations when incurred.

***Compensation Plans***

As of March 31, 2017, Sprint sponsored three incentive plans: the 2015 Omnibus Incentive Plan (2015 Plan); the 2007 Omnibus Incentive Plan (2007 Plan); and the 1997 Long-Term Incentive Program (1997 Program)(together, "Compensation Plans"). Sprint also sponsors an Employee Stock Purchase Plan (ESPP). Under the 2015 Plan, we may grant share and non-share based awards, including stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units and other equity-based and cash awards to employees, outside directors and other eligible individuals as defined by the plan. As of March 31, 2017, the number of shares available and reserved for future

Table of ContentsIndex to Consolidated Financial Statements**SPRINT CORPORATION  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

grants under the 2015 Plan and ESPP totaled approximately 211 million common shares. The Compensation Committee of our board of directors, or one or more executive officers should the Compensation Committee so authorize, as provided in the 2015 Plan, will determine the terms of each share and non-share based award. No new grants can be made under the 2007 Plan or the 1997 Program. We use new shares to satisfy share-based awards or treasury shares, if available.

The fair value of each option award is estimated on the grant date using the Black-Scholes option valuation model, based on several assumptions including the risk-free interest rate, volatility, expected dividend yield and expected term. During the year ended March 31, 2017, the Company granted approximately 12 million stock options with a weighted average grant date fair value of \$2.23 per share based upon assumptions of a risk free interest rate from 1.23% to 2.27%, expected volatility from 53.6% to 65.2%, expected dividend yield of 0% and expected term from 5.5 years to 6.5 years. In general, options are granted with an exercise price equal to the market value of the underlying shares on the grant date, vest on an annual basis over three years, and have a contractual term of ten years. As of March 31, 2017, 37 million options were outstanding, of which 17 million options were exercisable.

We generally determine the fair value of each restricted stock unit award based on the closing price of the Company's common stock on the date of grant. Restricted stock units generally have performance and service requirements or service requirements only with vesting periods ranging from one to three years. During the years ended March 31, 2017 and 2016, we also granted performance-based restricted stock units to executive and non-executive employees that are earned (Earned Shares) based upon the achievement of certain market conditions equal to specified volume-weighted average prices of the Company's common stock during regular trading on the New York Stock Exchange over any 150-day calendar period ending May 31, 2019 (Performance Period). Earned Shares will generally vest 50% over four years from the grant date and 50% over five years from the grant date, with continuous service required through each vesting date. As of March 31, 2017, the specified market criteria was achieved at a threshold price target qualifying for a 100% payout, however, the Earned Shares remain subject to the vesting requirements. The fair value of these market-based restricted stock units is estimated at the date of grant using a Monte Carlo valuation methodology, which incorporates into the valuation the possibility that the market condition may not be satisfied. For the year ended March 31, 2017, assumptions used in the Monte Carlo valuation model are consistent with those we use to value stock options and include a risk free interest rate from 1.20% to 1.92%, expected volatility from 53.6% to 70.8%, and expected dividend yield of 0%. The number of restricted stock units that ultimately vest can increase depending upon the future performance of the Company's common stock and the achievement of a higher threshold price target during the Performance Period, with a maximum payout of 120%. Compensation cost related to the share-based awards with market conditions is recognized regardless of the level of threshold price target achievement.

Employees and directors who are granted restricted stock units are not required to pay for the shares but generally must remain employed with us, or continue to serve as a member of our board of directors, until the restrictions lapse, which is typically three years for employees and one year for directors. Certain restricted stock units outstanding as of March 31, 2017, are entitled to dividend equivalents paid in cash, if dividends are declared and paid on common shares, but performance-based restricted stock units are not entitled to dividend equivalent payments until the applicable performance and service criteria have been met. During the year ended March 31, 2017, the Company granted approximately 55 million service only and performance-based restricted stock units, including those with market conditions, with a weighted average grant date fair value of \$5.64 per share. At March 31, 2017, approximately 77 million restricted stock unit awards were outstanding.

*Compensation Costs*

The cost of employee services received in exchange for share-based awards classified as equity is measured using the estimated fair value of the award on the date of the grant, and that cost is recognized over the period that the award recipient is required to provide service in exchange for the award. Awards of instruments classified as liabilities are measured at the estimated fair value at each reporting date through settlement.

Pre-tax share and non-share based compensation charges from our incentive plans included in net loss were \$93 million, \$75 million, and \$86 million for the years ended March 31, 2017, 2016, and 2015, respectively. The net income tax benefit recognized in the consolidated financial statements for share-based compensation awards was \$33 million, \$20 million, and \$34 million for the years ended March 31, 2017, 2016, and 2015, respectively. As of March 31, 2017, there was \$251 million of total unrecognized compensation cost related to non-vested incentive awards that are expected to be recognized over a weighted average period of 3.35 years.

Table of Contents

Index to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

***Advertising Costs***

We recognize advertising expense when incurred as selling, general and administrative expense. Advertising expenses totaled \$1.1 billion, \$1.3 billion, and \$1.5 billion for each of the years ended March 31, 2017, 2016, and 2015, respectively.

***Variable Interest Entities (VIE)***

VIEs are entities which lack sufficient equity to permit the entity to finance its activities without additional subordinated financial support from other parties, have equity investors which do not have the ability to make significant decisions relating to the entity's operations through voting rights, do not have the obligation to absorb the expected losses, or do not have the right to receive the residual returns of the entity. A common type of VIE is a special purposes entity (SPE). SPEs are commonly used in securitization transactions in order to isolate certain assets and distribute the cash flows from those assets to investors. SPEs are generally structured to insulate investors from claims on the SPE's assets by creditors of other entities, including the creditors of the seller of the assets.

We are required to consolidate the assets and liabilities of VIEs when we are deemed to be the primary beneficiary. The primary beneficiary is the party which has the power to make the decisions that most significantly affect the economic performance of the VIE and has the obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE.

**New Accounting Pronouncements**

In May 2014, the FASB issued new authoritative literature, *Revenue from Contracts with Customers*, and has subsequently modified several areas of the standard in order to provide additional clarity and improvements. The issuance is part of a joint effort by the FASB and the International Accounting Standards Board (IASB) to enhance financial reporting by creating common revenue recognition guidance for U.S. GAAP and International Financial Reporting Standards and, thereby, improving the consistency of requirements, comparability of practices and usefulness of disclosures. The new standard will supersede much of the existing authoritative literature for revenue recognition. In July 2015, the FASB deferred the effective date of this standard. As a result, the standard and related amendments will be effective for the Company for its fiscal year beginning April 1, 2018, including interim periods within that fiscal year. Early application is permitted, but not before the original effective date of April 1, 2017.

Two adoption methods are available for implementation of the standard update related to the recognition of revenue from contracts with customers. Under one method, the guidance is applied retrospectively to contracts for each reporting period presented, subject to allowable practical expedients. Under the other method, the guidance is applied only to the most current period presented, recognizing the cumulative effect of the change as an adjustment to the beginning balance of retained earnings, and also requires additional disclosures comparing the results to the previous guidance.

The Company is currently evaluating the guidance, including which implementation approach will be applied. The ultimate impact on revenue resulting from the application of the new standard will be subject to assessments that are dependent on many variables, including, but not limited to, the terms and mix of the contractual arrangements we have with customers. Upon adoption, we expect that the allocation of revenue between equipment and service for our wireless fixed-term service plans will result in more revenue allocated to equipment and recognized earlier as compared with current GAAP. We expect the timing of recognition of our sales commission expenses will also be impacted, as a substantial portion of these costs (which are currently expensed) will be capitalized and amortized consistent with the transfer of the related good or service. We continue to evaluate the available transition methods. Our considerations include, but are not limited to, the comparability of our financial statements and the comparability within our industry from application of the new standard to our contractual arrangements.

We have established a cross-functional team to implement the standard update related to the recognition of revenue from contracts with customers. We have identified and are in the process of implementing changes to our systems, processes and internal controls to meet the updated standard's reporting and disclosure requirements. We expect this guidance to have a material impact on our consolidated financial statements.

In July 2015, the FASB issued authoritative guidance regarding *Inventory*, which simplifies the subsequent measurement of certain inventories by replacing today's lower of cost or market test with a lower of cost and net realizable value test. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

costs of completion, disposal, and transportation. The standard will be effective for the Company's fiscal year beginning April 1, 2017, including interim periods within that fiscal year. The Company does not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

In January 2016, the FASB issued authoritative guidance regarding *Financial Instruments*, which amended guidance on the classification and measurement of financial instruments. Under the new guidance, entities will be required to measure equity investments that are not consolidated or accounted for under the equity method at fair value with any changes in fair value recorded in net income, unless the entity has elected the new practicability exception. For financial liabilities measured using the fair value option, entities will be required to separately present in other comprehensive income the portion of the changes in fair value attributable to instrument-specific credit risk. Additionally, the guidance amends certain disclosure requirements associated with the fair value of financial instruments. The standard will be effective for the Company's fiscal year beginning April 1, 2018, including interim reporting periods within that fiscal year. The Company does not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

In February 2016, the FASB issued authoritative guidance regarding *Leases*. The new standard will supersede much of the existing authoritative literature for leases. This guidance requires lessees, among other things, to recognize right-of-use assets and liabilities on their balance sheet for all leases with lease terms longer than twelve months. The standard will be effective for the Company for its fiscal year beginning April 1, 2019, including interim periods within that fiscal year with early application permitted. Entities are required to use modified retrospective application for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements with the option to elect certain transition reliefs. The Company is currently evaluating the guidance and is still assessing the overall impact. However, we expect it to have a material impact on our consolidated financial statements.

In June 2016, the FASB issued authoritative guidance regarding *Financial Instruments - Credit Losses*, which requires entities to use a Current Expected Credit Loss impairment model based on expected losses rather than incurred losses. Under this model, an entity would recognize an impairment allowance equal to its current estimate of all contractual cash flows that the entity does not expect to collect from financial assets measured at amortized cost. The entity's estimate would consider relevant information about past events, current conditions and reasonable and supportable forecasts, which will result in recognition of lifetime expected credit losses. The standard will be effective for the Company's fiscal year beginning April 1, 2020, including interim reporting periods within that fiscal year, although early adoption is permitted. The Company does not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

In October 2016, the FASB issued authoritative guidance regarding *Income Taxes*, which amended guidance for the income tax consequences of intra-entity transfers of assets other than inventory. Under the new guidance, entities will be required to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs, thereby eliminating the recognition exception within current guidance. The standard will be effective for the Company's fiscal year beginning April 1, 2018, including interim reporting periods within that fiscal year. The Company is currently evaluating the guidance and assessing the impact it will have on our consolidated financial statements.

In November 2016, the FASB issued authoritative guidance regarding *Statement of Cash Flows: Restricted Cash*, requiring that amounts generally described as restricted cash or restricted cash equivalents be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The standard will be effective for the Company's fiscal year beginning April 1, 2018, including interim reporting periods within that fiscal year, with early adoption permitted. The Company does not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

In January 2017, the FASB issued authoritative guidance amending *Business Combinations: Clarifying the Definition of a Business*, to clarify the definition of a business with the objective of providing a more robust framework to assist management when evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The standard will be effective for the Company for its fiscal year beginning April 1, 2018, including interim periods within that fiscal year, with early application permitted. The amendments are to be applied prospectively to business combinations that occur after the effective date.

In January 2017, the FASB issued authoritative guidance regarding *Intangibles - Goodwill and Other: Simplifying the Test for Goodwill Impairment*, which simplifies the goodwill impairment test by eliminating the requirement to calculate the implied fair value of goodwill to measure a goodwill impairment charge (Step 2 of the test), but rather to record an

Table of ContentsIndex to Consolidated Financial Statements**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

impairment charge based on the excess of the carrying value over its fair value. The standard will be effective for the Company's annual goodwill impairment test in the fiscal year beginning April 1, 2020, with early adoption permitted. The Company does not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

**Note 3. Funding Sources**

Our device leasing and installment billing programs require a greater use of operating cash flows in the earlier part of the device contracts as our subscribers will generally pay less upfront than a traditional subsidy program. The Accounts Receivable Facility and the Handset Sale-Leaseback transactions described below were designed in large part to mitigate the significant use of cash from purchasing devices from OEMs to fulfill our installment billing and leasing programs. We entered into the Network Equipment Sale-Leaseback transaction in April 2016 to sell and leaseback certain network equipment to unrelated bankruptcy-remote SPEs that provided \$2.2 billion in cash proceeds. In October 2016, we entered into a spectrum financing transaction whereby a portion of our spectrum holdings was used as collateral to issue \$3.5 billion in senior secured notes. In February 2017, we entered into a new credit agreement for \$6.0 billion, consisting of a \$4.0 billion, seven-year secured term loan that matures in February 2024 and a \$2.0 billion secured revolving bank credit facility that expires in February 2021.

**Accounts Receivable Facility***Transaction Overview*

Our Accounts Receivable Facility (Receivables Facility) provides us the opportunity to sell certain wireless service receivables, installment receivables, and future amounts due from customers who lease certain devices from us to unaffiliated third parties (the Purchasers). The maximum funding limit under the Receivables Facility is \$4.3 billion. While we have the right to decide how much cash to receive from each sale, the maximum amount of cash available to us varies based on a number of factors and currently represents approximately 50% of the total amount of the eligible receivables sold to the Purchasers. As of March 31, 2017, the total amount available to be drawn was \$826 million. The Receivables Facility was amended in November 2016 to, among other things, reallocate the Purchasers' commitments between wireless service, installment and future lease receivables to 33%, 39% and 28%, respectively. The amendment was in response to changing trends in the financing methods selected by customers. In February 2017, the Receivables Facility was amended to extend the maturity date to November 2018. Additionally, Sprint gained effective control over the receivables transferred to the Purchasers by obtaining the right, under certain circumstances, to repurchase them. Subsequent to the February 2017 amendment, all proceeds received from the Purchasers in exchange for the transfer of our wireless service and installment receivables are recorded as borrowings and all cash inflows and outflows under the Receivables Facility are reported as financing activities in the consolidated statements of cash flows. As a result of the amendment, there was a non-cash derecognition of the deferred purchase price receivable (DPP) asset totaling \$1.5 billion, along with corresponding increases to "Accounts and notes receivable, net" of \$2.6 billion, "Other assets" of \$563 million and "Long-term debt, financing and capital lease obligations" of \$1.7 billion. During the year ended March 31, 2017 and subsequent to the February 2017 amendment, we elected to receive \$100 million of cash and also remitted \$161 million of funds to the Purchasers because the amount of cash proceeds received by us under the facility exceeded the maximum funding limit, which were reported as financing activities in the consolidated statements of cash flows.

Prior to the February 2017 amendment, wireless service and installment receivables sold to the Purchasers were treated as a sale of financial assets and we derecognized these receivables, as well as the related allowances, and recognized the net proceeds received in cash provided by operating activities in the consolidated statements of cash flows. The total proceeds from the sale of these receivables were comprised of a combination of cash and a DPP. The DPP was realized by us upon either the ultimate collection of the underlying receivables sold to the Purchasers or upon Sprint's election to receive additional advances in cash from the Purchasers subject to the total availability under the Receivables Facility. The fees associated with these sales were recognized in "Selling, general and administrative" in the consolidated statements of operations through the date of the February 2017 amendment. Subsequent to the February 2017 amendment, the sale of wireless service and installment receivables are reported as financings, which is consistent with our historical treatment for the sale of future lease receivables, and the associated fees are recognized as "Interest expense" in the consolidated statements of operations.

Table of Contents

Index to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

***Transaction Structure***

Sprint contributes certain wireless service, installment and future lease receivables as well as the associated leased devices to Sprint's wholly-owned consolidated bankruptcy-remote SPEs. At Sprint's direction, the SPEs have sold, and will continue to sell, wireless service, installment and future lease receivables to Purchasers or to a bank agent on behalf of the Purchasers. Leased devices will remain with the SPEs, once sales are initiated, and continue to be depreciated over their estimated useful life. At March 31, 2017, wireless service and installment receivables contributed to the SPEs and included in "Accounts and notes receivable, net" in the consolidated balance sheets were \$2.9 billion and the long-term portion of installment receivables included in "Other assets" in the consolidated balance sheets was \$569 million. As of March 31, 2017, the net book value of devices contributed to the SPEs was approximately \$3.1 billion.

Each SPE is a separate legal entity with its own separate creditors who will be entitled, prior to and upon the liquidation of the SPE, to be satisfied out of the SPE's assets prior to any assets in the SPE becoming available to Sprint. Accordingly, the assets of the SPE are not available to pay creditors of Sprint or any of its affiliates (other than any other SPE), although collections from these receivables in excess of amounts required to repay the advances, yield and fees of the Purchasers and other creditors of the SPEs may be remitted to Sprint during and after the term of the Receivables Facility.

Sales of eligible receivables by the SPEs generally occur daily and are settled on a monthly basis. Sprint pays a fee for the drawn and undrawn portions of the Receivables Facility. A subsidiary of Sprint services the receivables in exchange for a monthly servicing fee, and Sprint guarantees the performance of the servicing obligations under the Receivables Facility.

***DPP***

Prior to the February 2017 amendment, the DPP was classified as a trading security within "Prepaid expenses and other current assets" in the consolidated balance sheets and was recorded at its estimated fair value. Subsequent to the February 2017 amendment, the Receivables Facility is accounted for as a financing and therefore the DPP is no longer recorded as a separate asset. The DPP related to our wireless service and installment receivables was \$1.2 billion as of March 31, 2016. The fair value of the DPP was estimated using a discounted cash flow model, which relies principally on unobservable inputs such as the nature and credit class of the sold receivables and subscriber payment history, and, for installment receivables sold, the estimated timing of upgrades and upgrade payment amounts for those with upgrade options. Changes in the fair value of the DPP did not have a material impact on our consolidated statements of operations for the years ended March 31, 2017 and 2016.

During the year ended March 31, 2017, prior to the February 2017 amendment, we remitted \$270 million of funds to the Purchasers because the amount of cash proceeds received by us under the facility exceeded the maximum funding limit, which increased the total amount of the DPP due to Sprint. We also elected to receive \$625 million of cash, which decreased the total amount of the DPP due to Sprint. In addition, during the year ended March 31, 2017, prior to the February 2017 amendment, sales of new receivables exceeded cash collections on previously sold receivables such that the DPP increased by \$644 million.

***Variable Interest Entity***

Sprint determined that certain of the Purchasers, which are multi-seller asset-backed commercial paper conduits (Conduits) are considered variable interest entities because they lack sufficient equity to finance their activities. Sprint's interest in the receivables purchased by the Conduits is not considered a variable interest because it is in assets that represent less than 50% of the total activity of the Conduits.

***Handset Sale-Leasebacks***

In December 2015 and May 2016, we sold certain iPhone® devices being leased by our customers to Mobile Leasing Solutions, LLC (MLS), a company formed by a group of equity investors, including SoftBank Group Corp. (SoftBank), and then subsequently leased the devices back. Under the agreements, Sprint generally maintains the customer leases, continues to collect and record lease revenue from the customer and remits monthly rental payments to MLS during the leaseback periods.

Under the agreements, Sprint contributed the devices and the associated customer leases to wholly-owned consolidated bankruptcy-remote special purpose entities of Sprint (SPE Lessees). The SPE Lessees then sold the devices and

Table of ContentsIndex to Consolidated Financial Statements**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

transferred certain specified customer lease end rights and obligations, such as the right to receive the proceeds from customers who elect to purchase the device at the end of the customer lease term, to MLS in exchange for a combination of cash and DPP. Settlement for the DPP occurs near the end of the agreement and can be reduced to the extent that MLS experiences a loss on the device (either not returned or sold at an amount less than the expected residual value of the device), but only to the extent of the device's DPP balance. In the event that MLS sells the devices returned from our customers at a price greater than the expected device residual value, Sprint has the potential to share some of the excess proceeds.

The SPE Lessees retain all rights to the underlying customer leases, such as the right to receive the rental payments during the device leaseback period, other than the aforementioned certain specified customer lease end rights. Each SPE Lessee is a separate legal entity with its own separate creditors who will be entitled, prior to and upon the liquidation of the SPE Lessee, to be satisfied out of the SPE Lessee's assets prior to any assets in the SPE Lessee becoming available to Sprint. Accordingly, the assets of the SPE Lessee are not available to pay creditors of Sprint or any of its affiliates. The SPE Lessees are obligated to pay the full monthly rental payments under each device lease to MLS regardless of whether our customers make lease payments on the devices leased to them or whether the customer lease is canceled. Sprint has guaranteed to MLS the performance of the agreements and undertakings of the SPE Lessees under the transaction documents.

***Handset Sale-Leaseback Tranche 1 (Tranche 1)***

In December 2015, Sprint transferred devices with a net book value of approximately \$1.3 billion to MLS in exchange for proceeds totaling \$1.1 billion and a DPP of \$126 million. We recorded the sale, removed the device from our balance sheet, and classified the leasebacks as operating leases. The difference between the fair value and the net book value of the devices sold was recognized as a loss on disposal of property, plant and equipment in the amount of \$65 million and was included in "Other, net" in the consolidated statements of operations for the year ended March 31, 2016. The cash proceeds received in the transaction were reflected as cash provided by investing activities in the consolidated statements of cash flows and payments made to MLS under the leaseback are reflected as "Cost of products" in the consolidated statements of operations. Rent expense related to MLS totaled \$494 million and \$277 million during the years ended March 31, 2017 and 2016, respectively, and is reflected within cash flows from operations. In December 2016, Sprint terminated Tranche 1 by repurchasing the devices and related customer lease end rights and obligations from MLS for consideration of \$375 million of net cash payments and the DPP of \$126 million. As a result of the transaction, Sprint recorded \$477 million of property, plant and equipment, \$16 million of other assets, and was released from certain liabilities. Additionally, the leaseback was canceled and there will be no future rental payments owed to MLS related to Tranche 1. The impact to the consolidated statements of operations as a result of the termination was immaterial.

***Handset Sale-Leaseback Tranche 2 (Tranche 2)***

In May 2016, Sprint transferred devices with a net book value of approximately \$1.3 billion to MLS in exchange for cash proceeds totaling \$1.1 billion and a DPP of \$186 million. Unlike Tranche 1, Tranche 2 was accounted for as a financing. Accordingly, the devices remain in "Property, plant and equipment, net" in the consolidated balance sheets and we continue to depreciate the assets to their estimated residual values over the respective customer lease terms. At March 31, 2017, the net book value of devices transferred to MLS was approximately \$575 million.

The proceeds received are reflected as cash provided by financing activities in the consolidated statements of cash flows and payments made to MLS will be reflected as principal repayments and interest expense. We have elected to account for the financing obligation at fair value. Accordingly, changes in the fair value of the financing obligation are recognized in "Other (expense) income, net" in the consolidated statements of operations over the course of the arrangement.

Tranche 2 primarily includes devices from our iPhone Forever Program, whereas these devices were specifically excluded from Tranche 1. The iPhone Forever Program provides our leasing customers the ability to upgrade their devices and to enter into a new lease agreement, subject to certain conditions, upon Apple's release of a next generation device. Upon a customer exercising their iPhone Forever upgrade right, Sprint has the option to terminate the existing leaseback by immediately remitting all unpaid device leaseback payments and returning the device to MLS. Alternatively, Sprint has the option to transfer the title in the new device to MLS in exchange for the title in the original device (Exchange Option). If Sprint elects the Exchange Option, we are required to continue to pay existing device leaseback rental related to the original device, among other requirements.

To address the introduction of the upgrade feature into the sale-leaseback structure, among other factors, numerous contractual terms from Tranche 1 were modified, which shifted certain risks of ownership in the devices away

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

from MLS to Sprint and resulted in Tranche 2 being accounted for as a financing. For instance, the device leaseback periods are generally longer in Tranche 2 as compared to Tranche 1, and the resulting amounts committed to be paid by the Company represent the initial proceeds received from MLS plus interest. This mitigates MLS's exposure to certain risks for non-returned and damaged devices, as well as to declines in device residual values.

**Network Equipment Sale-Leaseback**

In April 2016, Sprint sold and leased back certain network equipment to unrelated bankruptcy-remote special purpose entities (collectively, "Network LeaseCo"). The network equipment was used as collateral to raise approximately \$2.2 billion in borrowings from external investors, including SoftBank. Sprint's payments to Network LeaseCo during the leaseback period are used by Network LeaseCo to service debt.

Network LeaseCo is a variable interest entity for which Sprint is the primary beneficiary. As a result, Sprint is required to consolidate Network LeaseCo and our consolidated financial statements include Network LeaseCo's debt and the related financing cash inflows. The network assets included in the transaction, which had a net book value of approximately \$3.0 billion and consisted primarily of equipment located at cell towers, remain on Sprint's consolidated financial statements and continue to be depreciated over their respective estimated useful lives. At March 31, 2017, these network assets had a net book value of approximately \$2.4 billion.

The proceeds received were reflected as cash provided by financing activities in the consolidated statements of cash flows and payments made by Network LeaseCo are reflected as principal repayments and interest expense over the respective terms. Sprint has the option to purchase the equipment at the end of the leaseback term for a nominal amount. All intercompany transactions between Network LeaseCo and Sprint are eliminated in our consolidated financial statements. Principal and interest payments on the borrowings from the external investors will be repaid in staggered, unequal payments through January 2018. The first principal payment of \$300 million was made in March 2017 with the remaining \$1.9 billion of principal payments due in fiscal year 2017.

**Spectrum Financing**

In October 2016, Sprint transferred certain directly held and third-party leased spectrum licenses (collectively, "Spectrum Portfolio") to wholly-owned bankruptcy-remote special purpose entities (collectively, "Spectrum Financing SPEs"). The Spectrum Portfolio, which represents approximately 14% of Sprint's total spectrum holdings on a MHz-pops basis, was used as collateral to raise an initial \$3.5 billion in senior secured notes at 3.36% per annum from external investors under a \$7.0 billion program. Sprint can utilize this financing structure to potentially raise up to an additional \$3.5 billion, subject to certain conditions. The notes will be repaid over a five-year term, with interest-only payments over the first four quarters and amortizing quarterly principal payments thereafter commencing in December 2017 through September 2021.

Sprint Communications, Inc. simultaneously entered into a long-term lease with the Spectrum Financing SPEs for the ongoing use of the Spectrum Portfolio. Sprint Communications, Inc. is required to make monthly lease payments to the Spectrum Financing SPEs at a market rate. Those lease payments are sufficient to service the senior secured notes. As the Spectrum Financing SPEs are wholly-owned Sprint subsidiaries, these entities are consolidated and all intercompany activity has been eliminated.

**Note 4. Installment Receivables**

Certain subscribers have the option to pay for their devices in installments generally up to a 24-month period. Beginning in October 2015, Sprint sold and derecognized all eligible installment receivables, which were accounted for as sales. As a result of amendment to the Receivable Facility in February 2017, Sprint gained effective control over the sold receivables and all subsequent sales are treated as financings. Accordingly, the installment receivables are recognized in the consolidated balance sheets (*see Note 3. Funding Sources*). Short-term installment receivables are recorded in "Accounts and notes receivable, net" and long-term installment receivables are recorded in "Other assets" in the consolidated balance sheets.

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

The following table summarizes the installment receivables:

	March 31, 2017
	<i>(in millions)</i>
Installment receivables, gross	\$ 2,270
Deferred interest	(207)
Installment receivables, net of deferred interest	2,063
Allowance for credit losses	(299)
Installment receivables, net	<u>\$ 1,764</u>
<b>Classified on the consolidated balance sheets as:</b>	
Accounts and notes receivable, net	\$ 1,195
Other assets	569
Installment receivables, net	<u>\$ 1,764</u>

The balance and aging of installment receivables on a gross basis by credit category were as follows:

	March 31, 2017		
	Prime	Subprime	Total
	<i>(in millions)</i>		
Unbilled	\$ 1,501	\$ 619	\$ 2,120
Billed - current	74	36	110
Billed - past due	20	20	40
Installment receivables, gross	<u>\$ 1,595</u>	<u>\$ 675</u>	<u>\$ 2,270</u>

Activity in the deferred interest and allowance for credit losses for the installment receivables was as follows:

	Year Ended March 31,	
	2017	2016
	<i>(in millions)</i>	
Deferred interest and allowance for credit losses, beginning of period	\$ —	\$ 329
Bad debt expense	61	93
Write-offs, net of recoveries	(28)	(105)
Change in deferred interest on short-term and long-term installment receivables	8	(43)
Recognition (derecognition) of deferred interest and allowance for credit losses	465	(274)
Deferred interest and allowance for credit losses, end of period	<u>\$ 506</u>	<u>\$ —</u>

Total bad debt expense for the years ended March 31, 2017, 2016, and 2015, which includes amounts shown in the above table as well as bad debt expense on sold installment receivables, was \$322 million, \$147 million, and \$398 million, respectively.

**Note 5. Financial Instruments**

The Company carries certain assets and liabilities at fair value. Fair value is defined as an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The three-tier hierarchy for inputs used in measuring fair value, which prioritizes the inputs based on the observability as of the measurement date, is as follows: quoted prices in active markets for identical assets or liabilities; observable inputs other than the quoted prices in active markets for identical assets and liabilities; and unobservable inputs for which there is little or no market data, which require the Company to develop assumptions of what market participants would use in pricing the asset or liability.

The carrying amount of cash equivalents, accounts and notes receivable, and accounts payable approximates fair value. Short-term investments are recorded at amortized cost and the respective carrying amounts approximate fair value primarily using quoted prices in active markets. As of March 31, 2017, short-term investments totaled \$5.4 billion and consisted of approximately \$3.0 billion of time deposits and \$2.4 billion of commercial paper. Sprint did not hold any short-

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

term investments as of March 31, 2016. The fair value of marketable equity securities totaling \$46 million for both periods ended March 31, 2017 and 2016, respectively, are measured on a recurring basis using quoted prices in active markets.

Except for our financing transaction with MLS, current and long-term debt and our other financings are carried at amortized cost. The Company elected to measure the financing obligation with MLS at fair value as a means to better reflect the economic substance of the arrangement. The Tranche 2 financing obligation, which amounted to \$385 million at March 31, 2017 and is reported in "Current portion of long-term debt, financing and capital lease obligations" in our consolidated balance sheets, is the only eligible financial instrument for which we have elected the fair value option.

The fair value of the financing obligation, which was determined at the outset of the arrangement using a discounted cash flow model, was derived by unobservable inputs such as customer churn rates, customer upgrade probabilities, and the likelihood that Sprint will elect the Exchange Option versus the termination option upon a customer upgrade. Any gains or losses resulting from changes in the fair value of the financing obligation are included in "Other (expense) income, net" on the consolidated statements of operations. For the year ended March 31, 2017, the change in fair value of the financing obligation resulted in a loss of approximately \$24 million. For the year ended March 31, 2016, the payments made to MLS totaled \$654 million. In addition to the Tranche 2 financing obligation, the remaining debt for which estimated fair value is determined based on unobservable inputs primarily represents borrowings under our Network Equipment Sale-Leaseback and sales of receivables under our Receivables Facility. The carrying amounts associated with these borrowings approximates fair value.

The estimated fair value of the majority of our current and long-term debt, excluding our credit facilities, sold wireless service, installment billing and future receivables, and borrowings under our Network Equipment Sale-Leaseback and Tranche 2 transactions, is determined based on quoted prices in active markets or by using other observable inputs that are derived principally from, or corroborated by, observable market data.

The following table presents carrying amounts and estimated fair values of current and long-term debt:

	Carrying amount at March 31, 2017	Estimated Fair Value Using Input Type			Total estimated fair value
		Quoted prices in active markets	Observable	Unobservable	
<i>(in millions)</i>					
Current and long-term debt	\$ 40,581	\$ 33,196	\$ 4,352	\$ 5,468	\$ 43,016

	Carrying amount at March 31, 2016	Estimated Fair Value Using Input Type			Total estimated fair value
		Quoted prices in active markets	Observable	Unobservable	
<i>(in millions)</i>					
Current and long-term debt	\$ 33,645	\$ 21,757	\$ 4,474	\$ 2,130	\$ 28,361

**Note 6. Property, Plant and Equipment**

Property, plant and equipment consists primarily of network equipment and other long-lived assets used to provide service to our subscribers. Non-cash accruals included in PP&E totaled \$962 million, \$468 million, and \$1.5 billion for the years ended March 31, 2017, 2016, and 2015, respectively.

The following table presents the components of PP&E, and the related accumulated depreciation:

	March 31,	
	2017	2016
<i>(in millions)</i>		
Land	\$ 260	\$ 260
Network equipment, site costs and related software	21,693	21,500
Buildings and improvements	818	798
Non-network internal use software, office equipment, leased devices and other	8,625	6,182
Construction in progress	2,316	1,249
Less: accumulated depreciation	(14,503)	(9,692)
Property, plant and equipment, net	<u>\$ 19,209</u>	<u>\$ 20,297</u>



Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

Network equipment, site costs and related software includes switching equipment, cell site towers, site development costs, radio frequency equipment, network software, digital fiber optic cable, transport facilities and transmission-related equipment. Buildings and improvements principally consists of owned general office facilities, retail stores and leasehold improvements. Non-network internal use software, office equipment, leased devices and other primarily consists of furniture, information technology systems, equipment and vehicles, and leased devices. Construction in progress, which is not depreciated until placed in service, primarily includes materials, transmission and related equipment, labor, engineering, site development costs, interest and other costs relating to the construction and development of our network.

In September 2014, Sprint introduced a leasing program, whereby qualified subscribers can lease a device for a contractual period of time. At the end of the lease term, the subscriber has the option to turn in the device, continue leasing the device, or purchase the device. As of March 31, 2017 and 2016, substantially all of our device leases were classified as operating leases. At lease inception, the devices leased through Sprint's direct channels are reclassified from inventory to property, plant and equipment. For those devices leased through indirect channels, Sprint purchases the device to be leased from the retailer at lease inception. The devices are then depreciated using the straight-line method to their estimated residual value generally over the term of the lease.

The following table presents leased devices and the related accumulated depreciation:

	March 31,	
	2017	2016
	<i>(in millions)</i>	
Leased devices	\$ 7,276	\$ 4,913
Less: accumulated depreciation	(3,114)	(1,267)
Leased devices, net	<u>\$ 4,162</u>	<u>\$ 3,646</u>

During the years ended March 31, 2017 and 2016, there were non-cash transfers to leased devices of \$2.9 billion and \$3.2 billion, respectively, along with a corresponding decrease in "Device and accessory inventory." In addition, during the year ended March 31, 2017, we repurchased MLS Tranche 1 devices totaling \$477 million, which we had sold for \$1.3 billion during the year ended March 31, 2016 (see Note 3. *Funding Sources*). Non-cash accruals included in leased devices totaled approximately \$158 million, \$159 million, and \$182 million as of March 31, 2017, 2016, and 2015, respectively, for devices purchased from indirect dealers that were leased to our subscribers. Depreciation expense incurred on all leased devices for the years ended March 31, 2017, 2016, and 2015 was \$3.1 billion, \$1.8 billion, and \$206 million, respectively.

As of March 31, 2017, the minimum estimated payments to be received for leased devices were as follows (in millions):

Fiscal year 2017	\$ 2,338
Fiscal year 2018	290
Fiscal year 2019	2
	<u>\$ 2,630</u>

During the year ended March 31, 2017, we recorded \$509 million of loss on disposal of property, plant and equipment, net of recoveries, which is included in "Other, net" in our consolidated statements of operations. Losses totaling \$481 million resulted from the write-off of leased devices associated with lease cancellations prior to the scheduled customer lease terms where customers did not return the devices to us. If customers continue to not return devices, we may have material losses in future periods. In addition, we recorded \$28 million of losses related to cell site construction costs that are no longer recoverable as a result of changes in the Company's network plans.

During the year ended March 31, 2016, we recorded \$487 million of loss on disposal of property, plant and equipment, net of recoveries, which is included in "Other, net" in our consolidated statements of operations. These losses were the result of \$65 million in net losses recognized upon the sale of devices to MLS under the Handset Sale-Leaseback Tranche 1 transaction, which represented the difference between the fair value and net book value of the devices sold and \$256 million in losses from the write-off of leased devices associated with lease cancellations prior to the scheduled customer lease terms where customers did not return the devices to us. In addition, we recorded \$166 million of losses due to cell site construction costs and other network costs that are no longer recoverable as a result of changes in the Company's network



Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

plans. During the year ended March 31, 2015, there were no losses on disposal of property, plant and equipment recorded in our consolidated statements of operations.

**Impairments**

During the year ended March 31, 2015, we recorded an impairment loss of \$233 million, which is included in "Impairments" in our consolidated statements of operations, to reduce the carrying value of the Wireline asset group, which includes the Wireline long-lived assets, to its estimated fair value of \$918 million.

**Note 7. Intangible Assets****Indefinite-Lived Intangible Assets**

Our indefinite-lived intangible assets consists of FCC licenses, which were acquired primarily through FCC auctions and business combinations, certain of our trademarks, and goodwill. At March 31, 2017, we held 800 MHz, 1.9 GHz and 2.5 GHz FCC licenses authorizing the use of radio frequency spectrum to deploy our wireless services. As long as the Company acts within the requirements and constraints of the regulatory authorities, the renewal and extension of these licenses is reasonably certain at minimal cost. Accordingly, we have concluded that FCC licenses are indefinite-lived intangible assets. Our Sprint and Boost Mobile trademarks have also been identified as indefinite-lived intangible assets. Goodwill represents the excess of consideration paid over the estimated fair value of net tangible and identifiable intangible assets acquired in business combinations.

The following provides the activity of indefinite-lived intangible assets within the consolidated balance sheets:

	March 31, 2016	Net Additions	March 31, 2017
	<i>(in millions)</i>		
FCC licenses	\$ 36,038	\$ 512 <sup>(1)</sup>	\$ 36,550
Trademarks	4,035	—	4,035
Goodwill <sup>(2)</sup>	6,575	4	6,579
	<u>\$ 46,648</u>	<u>\$ 516</u>	<u>\$ 47,164</u>
	March 31, 2015	Net Additions	March 31, 2016
	<i>(in millions)</i>		
FCC licenses	\$ 35,952	\$ 86	\$ 36,038
Trademarks	4,035	—	4,035
Goodwill <sup>(2)</sup>	6,575	—	6,575
	<u>\$ 46,562</u>	<u>\$ 86</u>	<u>\$ 46,648</u>

(1) Net additions within FCC licenses includes \$85 million of spectrum acquired from the Shentel transaction (see Note 8. Long-Term Debt, Financing and Capital Lease Obligations) and an increase from spectrum license exchanges described below during the year ended March 31, 2017.

(2) Through March 31, 2017 there is no accumulated impairment losses for goodwill.

**Spectrum License Exchanges**

In the second quarter of fiscal year 2016, we exchanged certain spectrum licenses with other carriers in non-cash transactions. As a result, we recorded a non-cash gain of \$354 million, which represented the difference between the fair value and the net book value of the spectrum transferred to the other carriers. The gain was presented in "Other, net" in the consolidated statements of operations for the year ended March 31, 2017.

**Assessment of Impairment**

Our annual impairment testing date for goodwill and indefinite-lived intangible assets is January 1 of each year; however, we test for impairment between our annual tests if an event occurs or circumstances change that indicate that the asset may be impaired, or in the case of goodwill, that the fair value of the reporting unit is below its carrying amount. We did not record any impairment during the years ended March 31, 2017 and 2016. Since the SoftBank Merger in July 2013, actual



Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

results and expectations of net postpaid handset subscriber additions were lower than the forecasts used to allocate the purchase price to the assets acquired and liabilities assumed. During the year ended March 31, 2015, we determined that recoverability of the carrying amount of goodwill and the Sprint trade name should be evaluated for impairment and it was determined that the carrying value of the Sprint trade name exceeded its estimated fair value of \$3.3 billion. Accordingly, during the year ended March 31, 2015 we recorded an impairment loss of \$1.9 billion, which is included in "Impairments" in our consolidated statements of operations.

The determination of fair value requires considerable judgment and is highly sensitive to changes in underlying assumptions. Consequently, there can be no assurance that the estimates and assumptions made for the purposes of the goodwill, spectrum licenses, and Sprint and Boost Mobile trade names impairment tests will prove to be an accurate prediction of the future. Sustained declines in the Company's operating results, number of wireless subscribers, future forecasted cash flows, growth rates and other assumptions, as well as significant, sustained declines in the Company's stock price and related market capitalization could impact the underlying key assumptions and our estimated fair values, potentially leading to a future material impairment of goodwill or other indefinite-lived intangible assets.

#### Intangible Assets Subject to Amortization

Customer relationships are amortized using the sum-of-the-months' digits method, while all other definite-lived intangible assets are amortized using the straight-line method over the estimated useful lives of the respective assets. We reduce the gross carrying value and associated accumulated amortization when specified intangible assets become fully amortized. Amortization expense related to favorable spectrum and tower leases is recognized in "Cost of services" in our consolidated statements of operations.

	Useful Lives	March 31, 2017			March 31, 2016		
		Gross Carrying Value	Accumulated Amortization	Net Carrying Value	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
<i>(in millions)</i>							
Customer relationships	4 to 8 years	\$ 6,923	\$ (5,053)	\$ 1,870	\$ 6,923	\$ (4,045)	\$ 2,878
Other intangible assets:							
Favorable spectrum leases	23 years	869	(138)	731	881	(110)	771
Favorable tower leases	7 years	589	(386)	203	589	(302)	287
Trademarks	34 years	520	(58)	462	520	(43)	477
Other	10 years	91	(37)	54	83	(27)	56
Total other intangible assets		2,069	(619)	1,450	2,073	(482)	1,591
Total definite-lived intangible assets		\$ 8,992	\$ (5,672)	\$ 3,320	\$ 8,996	\$ (4,527)	\$ 4,469
<i>(in millions)</i>							
Estimated amortization expense		\$ 883	\$ 667	\$ 462	\$ 258	\$ 104	

[Table of Contents](#)[Index to Consolidated Financial Statements](#)

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 8. Long-Term Debt, Financing and Capital Lease Obligations**

	Interest Rates	Maturities	March 31, 2017	March 31, 2016
<i>(in millions)</i>				
<b>Notes</b>				
<b>Senior notes</b>				
Sprint Corporation	7.13 - 7.88%	2021 - 2025	\$ 10,500	\$ 10,500
Sprint Communications, Inc.	6.00 - 11.50%	2017 - 2022	6,280	9,280
Sprint Capital Corporation	6.88 - 8.75%	2019 - 2032	6,204	6,204
<b>Senior secured notes</b>				
Sprint Spectrum Co LLC, Sprint Spectrum CO II LLC, Sprint Spectrum Co III LLC	3.36%	2021	3,500	—
<b>Guaranteed notes</b>				
Sprint Communications, Inc.	7.00 - 9.00%	2018 - 2020	4,000	4,000
<b>Secured notes</b>				
Clearwire Communications LLC <sup>(1)</sup>	14.75%	2016	—	300
<b>Exchangeable notes</b>				
Clearwire Communications LLC <sup>(1)(2)</sup>	8.25%	2017	629	629
<b>Credit facilities</b>				
Revolving bank credit facility	3.50%	2021	—	—
Secured term loan	3.50%	2024	4,000	—
Accounts receivable facility	2.02 - 2.51%	2018	1,964	600
Export Development Canada (EDC)	3.48%	2019	300	550
Secured equipment credit facilities	2.57 - 3.27%	2019 - 2021	431	805
<b>Financing obligations, capital lease and other obligations</b>	2.35 - 10.63%	2017 - 2024	3,016	493
<b>Net premiums and debt financing costs</b>			90	597
			<u>40,914</u>	<u>33,958</u>
<b>Less current portion</b>			(5,036)	(4,690)
<b>Long-term debt, financing and capital lease obligations</b>			<u>\$ 35,878</u>	<u>\$ 29,268</u>

(1) Notes of Clearwire Communications LLC are also direct obligations of Clearwire Finance, Inc. and are guaranteed by certain Clearwire subsidiaries.

(2) The \$629 million Clearwire 8.25% Exchangeable Notes have both a par call and put on December 1, 2017 residing in the balance being classified as a current debt obligation.

As of March 31, 2017, Sprint Corporation, the parent corporation, had \$10.5 billion in aggregate principal amount of senior notes outstanding. In addition, as of March 31, 2017, the outstanding principal amount of senior notes issued by Sprint Communications, Inc. and Sprint Capital Corporation, guaranteed notes issued by Sprint Communications, Inc., exchangeable notes issued by Clearwire Communications LLC, secured term loan and secured revolving bank credit facility issued by Sprint Communications, Inc., the EDC agreement, the secured equipment credit facilities, the installment payment obligations, and the Network Equipment Sale-Leaseback and Handset Sale-Leaseback Tranche 2 financing obligations, collectively totaled \$26.1 billion in principal amount of our long-term debt issued by 100% owned subsidiaries, was fully and unconditionally guaranteed by Sprint Corporation. Although certain financing agreements restrict the ability of Sprint Communications, Inc. and its subsidiaries to distribute cash to Sprint Corporation, the ability of the subsidiaries to distribute cash to their respective parents, including to Sprint Communications, Inc. is generally not restricted.

As of March 31, 2017, approximately \$13.1 billion aggregate principal amount of our outstanding debt, comprised of certain notes, financing and capital lease obligations, was secured by substantially all of the assets of the Company. Cash interest

payments, net of amounts capitalized of \$44 million, \$51 million, and \$56 million, totaled \$2.7 billion, \$2.4 billion, and \$2.3 billion during each of the years ended March 31, 2017, 2016, and 2015, respectively. Our weighted average

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

effective interest rate related to our notes and credit facilities was 6.4% for the years ended March 31, 2017 and 2016, and 6.1% for the year ended March 31, 2015.

**Notes**

As of March 31, 2017, our outstanding notes consisted of senior notes, guaranteed notes, and exchangeable notes, all of which are unsecured, as well as senior secured notes associated with our Spectrum Financing transaction. Cash interest on all of the notes is generally payable semi-annually in arrears with the exception of the Spectrum Financing senior secured notes, which are payable quarterly. As of March 31, 2017, \$30.2 billion aggregate principal amount of the notes was redeemable at the Company's discretion at the then-applicable redemption prices plus accrued interest.

As of March 31, 2017, \$24.1 billion aggregate principal amount of our senior notes and guaranteed notes provided holders with the right to require us to repurchase the notes if a change of control triggering event (as defined in the applicable indentures and supplemental indentures) occurs.

Upon the close of the Clearwire Corporation acquisition on July 9, 2013, the Clearwire Communications, LLC 8.25% Exchangeable Notes due 2040 became exchangeable at any time, at the holder's option, for a fixed amount of cash equal to \$706.21 for each \$1,000 principal amount of notes surrendered. On December 1, 2017 the Exchangeable Notes can be tendered at the holder's option for 100% of the par value plus accrued interest resulting in the entire balance being classified as a current debt obligation.

In October 2016, the Company repaid \$300 million in aggregate principal of its Clearwire Communications LLC 14.75% secured notes. In December 2016, the Company repaid \$2.0 billion aggregate principal upon maturity of its outstanding Sprint Communications, Inc. 6% senior notes. In March 2017, the Company repaid \$1.0 billion aggregate principal upon maturity of its outstanding Sprint Communications, Inc. 9.125% senior notes.

In October 2016, Sprint transferred the Spectrum Portfolio to the Spectrum Financing SPEs. The Spectrum Portfolio, which represents approximately 14% of Sprint's total spectrum holdings on a MHz-pops basis, was used as collateral to raise an initial \$3.5 billion in senior secured notes at 3.36% per annum from external investors under a \$7.0 billion program. Sprint can utilize this financing structure to potentially raise up to an additional \$3.5 billion, subject to certain conditions. The notes will be repaid over a five-year term, with interest-only payments over the first four quarters and amortizing quarterly principal payments thereafter commencing December 2017 through September 2021. As of March 31, 2017, approximately \$438 million of the total principal outstanding was classified as "Current portion of long-term debt, financing and capital lease obligations" in the consolidated balance sheets. Total debt finance costs incurred and capitalized in connection with the issuance of notes were approximately \$95 million.

**Credit Facilities*****Secured Term Loan and Revolving Bank Credit Facility***

On February 3, 2017, we entered into a new credit agreement for \$6.0 billion, consisting of a \$4.0 billion, seven-year secured term loan that matures in February 2024 and a \$2.0 billion secured revolving bank credit facility that expires in February 2021. As of March 31, 2017, approximately \$215 million in letters of credit were outstanding under this credit facility, including the letter of credit required by the Report and Order (*see Note 12. Commitments and Contingencies*). As a result of the outstanding letters of credit, which directly reduce the availability of borrowings, the Company had approximately \$1.8 billion of borrowing capacity available under the secured revolving bank credit facility as of March 31, 2017. The bank credit facility requires a ratio (Leverage Ratio) of total indebtedness to trailing four quarters earnings before interest, taxes, depreciation and amortization and other non-recurring items, as defined by the bank credit facility (adjusted EBITDA), not to exceed 6.0 to 1.0 through the quarter ending December 31, 2017. After December 31, 2017, the Leverage Ratio declines on a scheduled basis until the ratio becomes fixed at 3.5 to 1.0 for the fiscal quarter ended March 31, 2020 and each fiscal quarter ending thereafter through expiration of the facility. The term loan has an interest rate equal to LIBOR plus 250 basis points and the secured revolving bank credit facility has an interest rate equal to LIBOR plus a spread that varies depending on the Leverage Ratio. The secured revolving bank credit facility replaced the \$3.3 billion unsecured revolving bank credit facility that was due to expire in February 2018.

In consideration of the seven-year secured term loan, we entered into a five-year fixed-for-floating interest rate swap on a \$2.0 billion notional amount that has been designated as a cash flow hedge. The effective portion of changes in fair value are recorded in "Other comprehensive income (loss)" in the consolidated statements of comprehensive loss and the

[Table of Contents](#)

[Index to Consolidated Financial Statements](#)

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

ineffective portion, if any, is recorded in current period earnings in the consolidated statements of operations as interest expense. The fair value of the interest rate swap was approximately \$2 million, which was recorded as a liability on the consolidated balance sheets at March 31, 2017.

*Accounts Receivable Facility*

As of March 31, 2017, the total amount of borrowings under our \$4.3 billion Receivable Facility was \$2.0 billion and the total amount available to be drawn was \$826 million. Prior to the February 2017 amendment, wireless service and installment receivables sold to the Purchasers were treated as a sale of financial assets and Sprint derecognized these receivables and recognized the net proceeds received in cash provided by operating activities in the consolidated statements of cash flows. Subsequent to the February 2017 amendment, the sale of wireless service and installment receivables are reported as financings, which is consistent with our historical treatment for the sale of future lease receivables. During the year ended March 31, 2017, we repaid \$416 million to the Purchasers and drew \$100 million.

*EDC agreement*

On February 3, 2017, we amended the EDC agreement to provide for security and covenant terms similar to our secured term loan and revolving bank credit facility. However, under the terms of the EDC agreement repayments of outstanding amounts cannot be redrawn. In March 2017, the Company repaid \$250 million of aggregate principal of its outstanding Tranche 4 secured loan due December 15, 2017. As of March 31, 2017, the total principal amount of our borrowings under the EDC facility was \$300 million.

*Secured equipment credit facilities*

*Eksportkreditinamnden (EKN)*

During the year ended March 31, 2017, we made principal repayments totaling \$254 million on the facility, resulting in the total repayment of the principal amount at March 31, 2017. The facility has expired in accordance with its terms.

*Finnvera plc (Finnvera)*

The Finnvera secured equipment credit facility provides for the ability to borrow up to \$800 million to finance network-related purchases from Nokia Solutions and Networks US LLC, USA. The facility has one tranche remaining and available for borrowing through October 2017. Such borrowings are contingent upon the amount and timing of Sprint's network-related purchases. During the year ended March 31, 2017, we made principal repayments totaling \$56 million, resulting in a total principal amount of \$140 million outstanding at March 31, 2017.

*K-sure*

The K-sure secured equipment credit facility provides for the ability to borrow up to \$750 million to finance network-related purchases from Samsung Telecommunications America, LLC. The facility can be divided in up to three consecutive tranches of varying size with borrowings available until May 2018, contingent upon the amount of network-related purchases made by Sprint. During the year ended March 31, 2017, we made principal repayments totaling \$65 million, resulting in a total principal amount of \$259 million outstanding at March 31, 2017.

*Delcredere | Ducroire (D/D)*

The D/D secured equipment credit facility provides for the ability to borrow up to \$250 million to finance network equipment-related purchases from Alcatel-Lucent USA Inc. The principal balance outstanding at March 31, 2017 was \$32 million.

Borrowings under the Finnvera, K-sure and D/D secured equipment credit facilities are each secured by liens on the respective equipment purchased pursuant to each facility's credit agreement. In addition, repayments of outstanding amounts borrowed under the secured equipment credit facilities cannot be redrawn. Each of these facilities is fully and unconditionally guaranteed by both Sprint Communications, Inc. and Sprint Corporation. The secured equipment credit facilities have certain key covenants similar to those in our secured term loan and revolving bank credit facility.

[Table of Contents](#)

[Index to Consolidated Financial Statements](#)

## SPRINT CORPORATION NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

### Financing Obligations

#### *Network Equipment Sale-Leaseback*

In April 2016, Sprint sold and leased back certain network equipment to Network LeaseCo. The network equipment acquired by Network LeaseCo, which is consolidated by us, was used as collateral to raise approximately \$2.2 billion in borrowings from external investors, including SoftBank. Principal and interest payments on the borrowings from the external investors will be repaid in staggered, unequal payments through January 2018. The first principal payment of \$300 million was made in March 2017 with the remaining \$1.9 billion of principal payments due in fiscal year 2017 (see Note 3. *Funding Sources*).

#### *Handset Sale-Leaseback Tranche 2*

In May 2016, Sprint entered into a second transaction with MLS to sell and leaseback certain iPhone® devices leased by our customers. Upon the transfer of devices with a net book value of approximately \$1.3 billion to MLS, Sprint received cash proceeds of \$1.1 billion. Unlike Tranche 1, the proceeds from Tranche 2 were accounted for as a financing (see Note 3. *Funding Sources*). During the year ended March 31, 2017, we repaid \$654 million to MLS, which reduced the principal amount of the financing obligation to \$385 million as of March 31, 2017.

#### *Tower Financing*

We have approximately 3,000 cell sites that we sold and subsequently leased back during 2008. Terms extend through 2021, with renewal options for an additional 20 years. These cell sites continue to be reported as part of our "Property, plant and equipment, net" in our consolidated balance sheets due to our continued involvement with the property sold and the transaction is accounted for as a financing. The financing obligation as of March 31, 2017 is \$191 million.

### Capital Lease and Other Obligations

On August 10, 2015, Shenandoah Telecommunications Company (Shentel) entered into a definitive agreement to acquire one of our wholesale partners, NTELOS Holdings Corp (nTelos). In connection with this definitive agreement, we entered into a series of agreements with Shentel to, among other things, acquire certain assets such as spectrum, terminate our existing wholesale arrangement with nTelos, and amend our existing affiliate agreement with Shentel to primarily include the subscribers formerly under the wholesale arrangement with nTelos. The agreements also expanded the area in which Shentel provides wireless service to Sprint customers and provided for more favorable economic terms. In April 2016, we received regulatory approval and the transaction closed in May 2016. The total consideration for this transaction included \$181 million, on a net present value basis, of notes payable to Shentel. Sprint will satisfy its obligations under the notes payable over an expected term of five to six years, of which the remaining obligation is \$225 million as of March 31, 2017. FCC licenses acquired from Shentel had a total value of \$85 million. \$96 million of the total purchase was recorded in "Other, net" in the consolidated statements of operations as a contract termination in the quarter ended June 30, 2016, which related to the termination of our pre-existing wholesale arrangement with nTelos. The remainder of our capital lease and other obligations of \$315 million as of March 31, 2017 are primarily for the use of wireless network equipment.

### Covenants

Certain indentures and other agreements also require compliance with various covenants, including covenants that limit the ability of the Company and its subsidiaries to sell all or substantially all of its assets, limit the ability of the Company and its subsidiaries to incur indebtedness and liens, and require that we maintain certain financial ratios, each as defined by the terms of the indentures, supplemental indentures and financing arrangements.

As of March 31, 2017, the Company was in compliance with all restrictive and financial covenants associated with its borrowings. A default under any of our borrowings could trigger defaults under certain of our other debt obligations, which in turn could result in the maturities being accelerated.

Under our secured revolving bank credit facility, we are currently restricted from paying cash dividends because our ratio of total indebtedness to adjusted EBITDA (each as defined in the applicable agreements) exceeds 2.5 to 1.0.

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Future Maturities of Long-Term Debt, Financing and Capital Lease Obligations**

Aggregate amount of maturities for long-term debt, financing and capital lease obligations outstanding as of March 31, 2017, were as follows (in millions):

Fiscal year 2017	\$ 5,039
Fiscal year 2018	6,157
Fiscal year 2019	4,168
Fiscal year 2020	2,596
Fiscal year 2021	3,816
Fiscal year 2022 and thereafter	19,048
	<u>40,824</u>
Net premiums and debt financing costs	90
	<u>\$ 40,914</u>

**Note 9. Severance and Exit Costs**

Severance and exit costs consist of lease exit costs primarily associated with tower and cell sites, access exit costs related to payments that will continue to be made under our backhaul access contracts for which we will no longer be receiving any economic benefit, and severance costs associated with reductions in our work force.

The following provides the activity in the severance and exit costs liability included in "Accounts payable," "Accrued expenses and other current liabilities" and "Other liabilities" within the consolidated balance sheets:

	March 31, 2016	Net Expense	Cash Payments and Other	March 31, 2017
	<i>(in millions)</i>			
Lease exit costs	\$ 338	\$ 17 <sup>(1)</sup>	\$ (106)	\$ 249
Severance costs	150	20 <sup>(2)</sup>	(158)	12
Access exit costs	37	31 <sup>(3)</sup>	(28)	40
	<u>\$ 525</u>	<u>\$ 68</u>	<u>\$ (292)</u>	<u>\$ 301</u>

(1) For the year ended March 31, 2017, we recognized costs of \$17 million (\$14 million Wireless, \$3 million Wireline).

(2) For the year ended March 31, 2017, we recognized costs of \$20 million (\$19 million Wireless, \$1 million Wireline).

(3) For the year ended March 31, 2017, we recognized \$2 million (solely attributable to Wireline) as "Cost of services" and \$29 million (\$12 million Wireless, \$17 million Wireline) as "Severance and exit costs."

	March 31, 2015	Net Expense	Cash Payments and Other	March 31, 2016
	<i>(in millions)</i>			
Lease exit costs	\$ 291	\$ 156 <sup>(4)</sup>	\$ (109)	\$ 338
Severance costs	119	216 <sup>(5)</sup>	(185)	150
Access exit costs	44	19 <sup>(6)</sup>	(26)	37
	<u>\$ 454</u>	<u>\$ 391</u>	<u>\$ (320)</u>	<u>\$ 525</u>

(4) We recognized costs of \$176 million (Wireless only) for the year ended March 31, 2016, which were offset by \$20 million of income (Wireless only) resulting from a revision to our estimate of a previously recorded reserve.

(5) For the year ended March 31, 2016, we recognized costs of \$216 million (\$191 million Wireless, \$25 million Wireline).

(6) For the year ended March 31, 2016, we recognized \$2 million (solely attributable to Wireline) as "Cost of services" and \$17 million (solely attributable to Wireless) as "Severance and exit costs".

We continually refine our network strategy and evaluate other potential network initiatives to improve the overall performance of our network. Additionally, major cost cutting initiatives are expected to continue, which may include headcount reductions, among other actions, to reduce operating expenses and improve our operating cash flows. As a result of these ongoing activities, we may incur future material charges associated with lease and access exit costs, severance, asset impairments, and accelerated depreciation, among others.



Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 10. Supplemental Financial Information**

	March 31,	
	2017	2016
	<i>(in millions)</i>	
<b>Accounts and notes receivable, net</b>		
Trade	\$ 2,947	\$ 899
Unbilled trade installment receivables and other	1,545	239
Less allowances for doubtful accounts and deferred interest	(354)	(39)
	<u>\$ 4,138</u>	<u>\$ 1,099</u>
<b>Prepaid expenses and other current assets</b>		
Prepaid expenses	\$ 298	\$ 366
Deferred purchase price for Receivables Facility	—	1,155
Deferred charges and other	303	399
	<u>\$ 601</u>	<u>\$ 1,920</u>
<b>Other assets</b>		
Unbilled trade installment receivables, net	\$ 569	\$ —
Deferred purchase price for Handset Sale-Leaseback Tranche 1	—	116
Investments	237	187
Other	507	425
	<u>\$ 1,313</u>	<u>\$ 728</u>
<b>Accounts payable<sup>(1)</sup></b>		
Trade	\$ 2,937	\$ 2,567
Accrued interconnection costs	123	142
Capital expenditures and other	221	190
	<u>\$ 3,281</u>	<u>\$ 2,899</u>
<b>Accrued expenses and other current liabilities</b>		
Deferred revenues	\$ 1,445	\$ 1,456
Accrued taxes	435	232
Payroll and related	339	339
Severance, lease and other exit costs	83	288
Accrued interest	511	532
Other	1,328	1,527
	<u>\$ 4,141</u>	<u>\$ 4,374</u>
<b>Other liabilities</b>		
Deferred rental income-communications towers	\$ 207	\$ 218
Deferred rent	554	478
Asset retirement obligations	462	550
Unfavorable lease liabilities	490	658
Postretirement benefits and other non-current employee related liabilities	861	994
Other	989	1,104
	<u>\$ 3,563</u>	<u>\$ 4,002</u>

(1) *includes liabilities in the amounts of \$69 million and \$66 million as of March 31, 2017 and 2016, respectively, for payments issued in excess of associated bank balances but not yet presented for collection.*

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 11. Income Taxes**

Sprint Corporation is the parent corporation of an affiliated group of corporations which join in the filing of a U.S. federal consolidated income tax return. Additionally, we file income tax returns in each state jurisdiction which imposes an income tax. In certain state jurisdictions, Sprint and its subsidiaries filed combined state tax returns with certain other SoftBank affiliates beginning with the year ended March 31, 2016. State tax expense or benefit has been determined utilizing the separate return approach as if Sprint and its subsidiaries file on a stand-alone basis. We also file income tax returns in a number of foreign jurisdictions. However, our foreign income tax activity has been immaterial. Cash paid or received for income tax purposes was insignificant for all periods presented.

Income tax expense consists of the following:

	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Current income tax (expense) benefit			
Federal	\$ 50	\$ 13	\$ 5
State	(50)	(30)	(39)
Total current income tax (expense) benefit	—	(17)	(34)
Deferred income tax (expense) benefit			
Federal	(284)	(206)	491
State	(149)	83	118
Total deferred income tax (expense) benefit	(433)	(123)	609
Foreign income tax expense	(2)	(1)	(1)
Total income tax (expense) benefit	\$ (435)	\$ (141)	\$ 574

The differences that caused our effective income tax rates to differ from the 35% U.S. federal statutory rate for income taxes were as follows:

	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Income tax benefit at the federal statutory rate	\$ 270	\$ 649	\$ 1,372
Effect of:			
State income taxes, net of federal income tax effect	24	38	124
State law changes, net of federal income tax effect	4	20	4
(Increase) reduction in liability for unrecognized tax benefits	(14)	(4)	1
Credit for increasing research activities	15	14	—
Tax (expense) benefit from organizational restructuring	(118)	90	—
Change in federal and state valuation allowance	(615)	(939)	(911)
Other, net	(1)	(9)	(16)
Income tax (expense) benefit	\$ (435)	\$ (141)	\$ 574
Effective income tax rate	(56.4)%	(7.6)%	14.6%

Income tax expense allocated to other items was as follows:

	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Unrecognized net periodic pension and other postretirement benefit cost <sup>(1)</sup>	\$ (24)	\$ —	\$ —

*(1) These amounts have been recognized in accumulated other comprehensive loss.*

F-33

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

Deferred income taxes are recognized for the temporary differences between the carrying amounts of our assets and liabilities for financial statement purposes and their tax bases. Deferred tax assets are also recorded for operating loss, capital loss and tax credit carryforwards. The sources of the differences that give rise to the deferred income tax assets and liabilities as of March 31, 2017 and 2016, along with the income tax effect of each, were as follows:

	March 31,	
	2017	2016
	<i>(in millions)</i>	
<b>Deferred tax assets</b>		
Net operating loss carryforwards	\$ 6,812	\$ 8,057
Tax credit carryforwards	340	384
Capital loss carryforwards	1	83
Property, plant and equipment	2,192	1,230
Debt obligations	205	—
Deferred rent	402	438
Pension and other postretirement benefits	332	378
Accruals and other liabilities	1,454	1,376
	<u>11,738</u>	<u>11,946</u>
<b>Valuation allowance</b>	<u>(10,477)</u>	<u>(9,793)</u>
	<u>1,261</u>	<u>2,153</u>
<b>Deferred tax liabilities</b>		
FCC licenses	12,876	12,738
Trademarks	1,712	1,718
Intangibles	771	1,166
Debt obligations	—	58
Other	318	432
	<u>15,677</u>	<u>16,112</u>
<b>Long-term deferred tax liability</b>	<u>\$ 14,416</u>	<u>\$ 13,959</u>

The realization of deferred tax assets, including net operating loss carryforwards, is dependent on the generation of future taxable income sufficient to realize the tax deductions, carryforwards and credits. However, our history of annual losses reduces our ability to rely on expectations of future income in evaluating the ability to realize our deferred tax assets. Valuation allowances on deferred tax assets are recognized if it is determined that it is more likely than not that the asset will not be realized. As a result, the Company recognized income tax expense to increase the valuation allowance by \$615 million, \$939 million, and \$911 million for the years ended March 31, 2017, 2016, and 2015, respectively. We do not expect to record significant tax benefits on future net operating losses until our circumstances justify the recognition of such benefits.

We believe it is more likely than not that our remaining deferred income tax assets, net of the valuation allowance, will be realized based on current income tax laws and expectations of future taxable income stemming from the reversal of existing deferred tax liabilities. Uncertainties surrounding income tax law changes, shifts in operations between state taxing jurisdictions and future operating income levels may, however, affect the ultimate realization of all or some of these deferred income tax assets.

Income tax expense of \$435 million for the year ended March 31, 2017 was primarily attributable to taxable temporary differences from the tax amortization of FCC licenses and tax expense of \$136 million on pre-tax gains from spectrum license exchanges which increased our deferred tax liability on FCC license temporary differences. In addition, we increased our state income tax valuation allowance by \$89 million as a result of a shift in operations among wholly-owned subsidiaries and an organizational restructuring that occurred during the year.

Income tax expense of \$141 million for the year ended March 31, 2016 was primarily attributable to tax expense resulting from taxable temporary differences from the tax amortization of FCC licenses, partially offset by tax benefits from

F-34

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

the reversal of state income tax valuation allowance on deferred tax assets and changes in state income tax laws enacted during the year. As a result of organizational restructuring, which drove a sustained increase in the profitability of specific legal entities, we revised our estimate regarding the realizability of the involved entities' deferred state tax assets and recorded a state tax benefit of \$90 million.

Income tax benefit of \$574 million for the year ended March 31, 2015 was primarily attributable to recognition of a tax benefit on the \$1.9 billion Sprint trade name impairment loss, partially offset by tax expense on taxable temporary differences from the tax amortization of FCC licenses during the period.

During the years ended March 31, 2017, 2016, and 2015, we generated \$204 million, \$343 million, and \$398 million, respectively, of foreign income, which is included in "Loss before income taxes" on the consolidated statements of operations. We have no material unremitted earnings of foreign subsidiaries.

As of March 31, 2017, we had federal operating loss carryforwards of \$16.4 billion, state operating loss carryforwards of \$17.5 billion and foreign net operating loss carryforwards of \$805 million. Related to these loss carryforwards, we have recorded federal tax benefits of \$5.7 billion, net state tax benefits of \$863 million and foreign tax benefits of \$265 million before consideration of the valuation allowances. Approximately \$620 million of the federal net operating loss carryforwards expire between fiscal years 2017 and 2021. The remaining \$15.8 billion expire in varying amounts between fiscal years 2022 and 2034. The state operating loss carryforwards expire in varying amounts through fiscal year 2035. Foreign operating loss carryforwards of \$446 million do not expire. The remaining foreign operating loss carryforwards expire in varying amounts between fiscal years 2017 and 2035.

We also had available \$429 million of federal and state income tax credit carryforwards as of March 31, 2017. Included in this amount are \$74 million of income tax credits which expire prior to fiscal year 2018 and \$301 million which expire in varying amounts between fiscal years 2018 and 2036. The remaining \$54 million do not expire.

Unrecognized tax benefits are established for uncertain tax positions based upon estimates regarding potential future challenges to those positions at the largest amount that is greater than fifty percent likely of being realized upon ultimate settlement. These estimates are updated at each reporting date based on the facts, circumstances and information available. Interest related to these unrecognized tax benefits is recognized in interest expense. Penalties are recognized as additional income tax expense. The unrecognized tax benefits attributable to uncertain tax positions were \$190 million and \$166 million, as of the March 31, 2017 and 2016, respectively. As of March 31, 2017, the unrecognized tax benefits included items that would favorably affect the income tax provision by \$175 million, if recognized without an offsetting valuation allowance adjustment. The accrued liability for income tax related interest and penalties was insignificant for all periods presented.

A reconciliation of the beginning and ending amount of unrecognized tax benefits was as follows:

	Year Ended March 31,	
	2017	2016
	<i>(in millions)</i>	
<b>Balance at beginning of period</b>	\$ 166	\$ 163
Additions based on current year tax positions	15	—
Additions based on prior year tax positions	10	5
Reductions for lapse of statute of limitations	(1)	(2)
<b>Balance at end of period</b>	<b>\$ 190</b>	<b>\$ 166</b>

As of March 31, 2017, we are under a limited scope federal income tax examination for the tax year ended March 31, 2015 that is being handled by the IRS Exam division. There are not any issues being handled by the IRS Appeals division. We are involved in multiple state income tax examinations related to various years beginning with 1996, which are in various stages of the examination, administrative/judicial review or appellate process. Based on our current knowledge of the examinations, administrative/judicial reviews and appellate processes, we believe it is reasonably possible a number of our uncertain tax positions may be resolved during the next twelve months which could result in a reduction of up to \$42 million in our unrecognized tax benefits.

The federal and state statutes of limitations for assessment of tax liability generally lapse three and four years, respectively, after the date the tax returns are filed. However, income tax attributes that are carried forward, such as net

Table of Contents

Index to Consolidated Financial Statements

## SPRINT CORPORATION NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

operating loss carryforwards, may be challenged and adjusted by taxing authorities at any time prior to the expiration of the statute of limitations for the tax year in which they are utilized.

In March 2016, the FASB issued authoritative guidance on *Compensation - Stock Compensation: Improvements to Employee Share-Based Payment Accounting* which, in part, eliminates the additional paid-in capital pools and requires excess tax benefits and tax deficiencies to be recorded in the income statement when the awards vest or are settled. The Company elected to early adopt this guidance effective April 1, 2016. The early adoption of this guidance did not have a material effect on our consolidated financial statements.

### Note 12. Commitments and Contingencies

#### Litigation, Claims and Assessments

In March 2009, a stockholder brought suit, *Bennett v. Sprint Nextel Corp.*, in the U.S. District Court for the District of Kansas, alleging that Sprint Communications and three of its former officers violated Section 10(b) of the Exchange Act and Rule 10b-5 by failing adequately to disclose certain alleged operational difficulties subsequent to the Sprint-Nextel merger, and by purportedly issuing false and misleading statements regarding the write-down of goodwill. The district court granted final approval of a settlement in August 2015, which did not have a material impact to our financial statements. Five stockholder derivative suits related to this 2009 stockholder suit were filed against Sprint Communications and certain of its present and/or former officers and directors. The first, *Murphy v. Forsee*, was filed in state court in Kansas on April 8, 2009, was removed to federal court, and was stayed by the court pending resolution of the motion to dismiss the *Bennett* case; the second, *Randolph v. Forsee*, was filed on July 15, 2010 in state court in Kansas, was removed to federal court, and was remanded back to state court; the third, *Ross-Williams v. Bennett, et al.*, was filed in state court in Kansas on February 1, 2011; the fourth, *Price v. Forsee, et al.*, was filed in state court in Kansas on April 15, 2011; and the fifth, *Hartleib v. Forsee, et al.*, was filed in federal court in Kansas on July 14, 2011. These cases were essentially stayed while the *Bennett* case was pending, and we have reached an agreement in principle to settle the matters, by agreeing to some governance provisions and by paying plaintiffs' attorneys fees in an immaterial amount. The court approved the settlement but reduced the plaintiffs' attorneys fees; the attorneys fees issue is on appeal.

On April 19, 2012, the New York Attorney General filed a complaint alleging that Sprint Communications has fraudulently failed to collect and pay more than \$100 million in New York sales taxes on receipts from its sale of wireless telephone services since July 2005. The complaint also seeks recovery of triple damages under the State False Claims Act, as well as penalties and interest. Sprint Communications moved to dismiss the complaint on June 14, 2012. On July 1, 2013, the court entered an order denying the motion to dismiss in large part, although it did dismiss certain counts or parts of certain counts. Sprint Communications appealed that order and the intermediate appellate court affirmed the order of the trial court. On October 20, 2015, the Court of Appeals of New York affirmed the decision of the appellate court that the tax statute requires us to collect and remit the disputed taxes. Our petition for certiorari to the U.S. Supreme Court on grounds of federal preemption was denied. Through the year ended March 31, 2017, we have accrued approximately \$200 million associated with this matter. The parties are now engaged in discovery in the trial court. We will continue to defend this matter vigorously and we do not expect the resolution of this matter to have a material adverse effect on our financial position or results of operations.

Eight related stockholder derivative suits have been filed against Sprint Communications and certain of its current and former officers and directors. Each suit alleges generally that the individual defendants breached their fiduciary duties to Sprint Communications and its stockholders by allegedly permitting, and failing to disclose, the actions alleged in the suit filed by the New York Attorney General. One suit, filed by the Louisiana Municipal Police Employees Retirement System, was dismissed by a federal court. Two suits were filed in state court in Johnson County, Kansas and one of those suits was dismissed as premature; and five suits are pending in federal court in Kansas. The remaining Kansas suits have been stayed pending resolution of the Attorney General's suit. We do not expect the resolution of these matters to have a material adverse effect on our financial position or results of operations.

Sprint Communications is also a defendant in a complaint filed by several stockholders of Clearwire Corporation (Clearwire) asserting claims for breach of fiduciary duty by Sprint Communications, and related claims and otherwise challenging the Clearwire acquisition. *ACP Master, LTD, et al. v. Sprint Nextel Corp., et al.*, was filed April 26, 2013, in Chancery Court in Delaware. Plaintiffs in the *ACP Master, LTD* suit have also filed suit requesting an appraisal of the fair

[Table of Contents](#)[Index to Consolidated Financial Statements](#)

## SPRINT CORPORATION NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

value of their Clearwire stock. Trial of those cases took place in October and November 2016; the parties have submitted their post-trial briefing, and oral argument was held on April 25, 2017. We are awaiting a decision. We do not expect the resolution of these matters to have a material adverse effect on our financial position or results of operations.

Sprint is currently involved in numerous court actions alleging that Sprint is infringing various patents. Most of these cases effectively seek only monetary damages. A small number of these cases are brought by companies that sell products and seek injunctive relief as well. These cases have progressed to various degrees and a small number may go to trial if they are not otherwise resolved. Adverse resolution of these cases could require us to pay significant damages, cease certain activities, or cease selling the relevant products and services. In many circumstances, we would be indemnified for monetary losses that we incur with respect to the actions of our suppliers or service providers. We do not expect the resolution of these cases to have a material adverse effect on our financial position or results of operations.

In October 2013, the FCC Enforcement Bureau began to issue notices of apparent liability (NALs) to other Lifeline providers, imposing fines for intracarrier duplicate accounts identified by the government during its audit function. Those audits also identified a small percentage of potentially duplicative intracarrier accounts related to our Assurance Wireless business. No NAL has yet been issued with respect to Sprint and we do not know if one will be issued. Further, we are not able to reasonably estimate the amount of any claim for penalties that might be asserted. However, based on the information currently available, if a claim is asserted by the FCC, Sprint does not believe that any amount ultimately paid would be material to the Company's results of operations or financial position.

Various other suits, inquiries, proceedings and claims, either asserted or unasserted, including purported class actions typical for a large business enterprise and intellectual property matters, are possible or pending against us or our subsidiaries. During the year ended March 31, 2017, we recorded a \$103 million charge associated with a state tax matter which is presented in our consolidated statements of operations within "Other, net". If our interpretation of certain laws or regulations, including those related to various federal or state matters such as sales, use or property taxes, or other charges were found to be mistaken, it could result in payments by us. While it is not possible to determine the ultimate disposition of each of these proceedings and whether they will be resolved consistent with our beliefs, we expect that the outcome of such proceedings, individually or in the aggregate, will not have a material adverse effect on our financial position or results of operations.

### **Spectrum Reconfiguration Obligations**

In 2004, the FCC adopted a Report and Order that included new rules regarding interference in the 800 MHz band and a comprehensive plan to reconfigure the 800 MHz band. The Report and Order provides for the exchange of a portion of our 800 MHz FCC spectrum licenses, and requires us to fund the cost incurred by public safety systems and other incumbent licensees to reconfigure the 800 MHz spectrum band. Also, in exchange, we received licenses for 10 MHz of nationwide spectrum in the 1.9 GHz band.

The minimum cash obligation is \$2.8 billion under the Report and Order. We are, however, obligated to pay the full amount of the costs relating to the reconfiguration plan, even if those costs exceed \$2.8 billion. As required under the terms of the Report and Order, a letter of credit has been secured to provide assurance that funds will be available to pay the relocation costs of the incumbent users of the 800 MHz spectrum. The letter of credit was initially \$2.5 billion, but has been reduced during the course of the proceeding to \$165 million as of March 31, 2017. Since the inception of the program, we have incurred payments of approximately \$3.5 billion directly attributable to our performance under the Report and Order, including approximately \$45 million during the year ended March 31, 2017. When incurred, substantially all costs are accounted for as additions to FCC licenses with the remainder as property, plant and equipment. Although costs incurred through March 31, 2017 have exceeded \$2.8 billion, not all of those costs have been reviewed and accepted as eligible by the transition administrator.

Completion of the 800 MHz band reconfiguration was initially required by June 26, 2008 and public safety reconfiguration is nearly complete across the country with the exception of the States of Washington, Arizona, California, Texas and New Mexico. The FCC continues to grant the remaining 800 MHz public safety licensees additional time to complete their band reconfigurations which, in turn, delays our access to our 800 MHz replacement channels in these areas. In the areas where band reconfiguration is complete, Sprint has received its replacement spectrum in the 800 MHz band and Sprint is deploying 3G CDMA and 4G LTE on this spectrum in combination with its spectrum in the 1.9 GHz and 2.5 GHz bands.

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Future Minimum Commitments**

As of March 31, 2017, the minimum estimated amounts due under operating leases, spectrum leases and service credits, and purchase orders and other commitments were as follows:

Future Minimum Commitments	Total	Fiscal Year 2017	Fiscal Year 2018	Fiscal Year 2019	Fiscal Year 2020	Fiscal Year 2021	Fiscal Year 2022 and thereafter
	<i>(in millions)</i>						
Operating leases	\$ 12,173	\$ 2,147	\$ 2,113	\$ 2,001	\$ 1,885	\$ 1,579	\$ 2,448
Spectrum leases and service credits	6,971	247	244	268	244	263	5,705
Purchase orders and other commitments	10,051	6,361	1,277	652	429	326	1,006
Total	<u>\$ 29,195</u>	<u>\$ 8,755</u>	<u>\$ 3,634</u>	<u>\$ 2,921</u>	<u>\$ 2,558</u>	<u>\$ 2,168</u>	<u>\$ 9,159</u>

***Operating Leases***

We lease various equipment, office facilities, retail outlets and kiosks, switching facilities and cell sites under operating leases. The non-cancelable portion of these leases generally ranges from monthly up to 15 years. These leases, with few exceptions, provide for automatic renewal options and escalations that are either fixed or based on the consumer price index. Any rent abatements, along with rent escalations, are included in the computation of rent expense calculated on a straight-line basis over the lease term. Our lease term for most leases includes the initial non-cancelable term plus at least one renewal period, if the non-cancelable term is less than ten years, as the exercise of the related renewal option or options is reasonably assured. Our cell site leases generally provide for an initial non-cancelable term of five to twelve years with up to 5 renewal options for five years each.

Our rental commitments for operating leases, including lease renewals that are reasonably assured, consisted mainly of leases for cell and switch sites, real estate, information technology and network equipment and office space. Total rental expense was \$3.1 billion, \$2.9 billion, and \$2.6 billion, for the years ended March 31, 2017, 2016, and 2015, respectively.

***Spectrum Leases and Service Credits***

Certain of the spectrum leases provide for minimum lease payments, additional charges, renewal options and escalation clauses. Leased spectrum agreements generally have terms of up to 30 years. We expect that all renewal periods in our spectrum leases will be renewed by us.

We also have commitments to provide services to certain lessors, and to reimburse lessors for certain capital equipment and third-party service expenditures over the term of the lease. We accrue a monthly obligation for the services and equipment based on the total estimated available service credits divided by the term of the lease. The obligation is reduced by services provided and as actual invoices are presented and paid to the lessors. During the period ended March 31, 2017, we satisfied \$3 million related to these commitments. The maximum remaining commitment at March 31, 2017 was \$83 million and is expected to be incurred over the term of the related lease agreements, which generally range from 15 to 30 years.

***Purchase Orders and Other Commitments***

We are a party to other commitments, which includes, among other things, service, spectrum, network equipment, devices, asset retirement obligations and other executory contracts in connection with conducting our business. Amounts actually paid under some of these agreements will likely be higher due to variable components of these agreements. The more significant variable components that determine the ultimate obligation owed include such items as hours contracted, subscribers and other factors. In addition, we are a party to various arrangements that are conditional in nature and obligate us to make payments only upon the occurrence of certain events, such as the delivery of functioning software or a product. Because it is not possible to predict the timing or amounts that may be due under these conditional arrangements, no such amounts have been included in the table above.

[Table of Contents](#)[Index to Consolidated Financial Statements](#)

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 13. Stockholders' Equity and Per Share Data**

Our certificate of incorporation authorizes 10,020,000,000 shares of capital stock as follows:

- 9,000,000,000 shares of common stock, par value \$0.01 per share;
- 1,000,000,000 shares of non-voting common stock, par value \$0.01 per share; and
- 20,000,000 shares of preferred stock, par value \$0.0001 per share.

**Classes of Common Stock***Voting Common Stock*

The holders of our common stock are entitled to one vote per share on all matters submitted for action by the stockholders. There were approximately 4.0 billion shares of common stock outstanding as of March 31, 2017.

*Treasury Shares*

Shares of common stock repurchased by us are recorded at cost as treasury shares and result in a reduction of stockholders' equity. We reissue treasury shares as part of our stockholder approved stock-based compensation programs, as well as upon conversion of outstanding securities that are convertible into common stock. When shares are reissued, we determine the cost using the FIFO method.

**Dividends**

We did not declare any dividends on our common shares for all periods presented in the consolidated financial statements. We are currently restricted from paying cash dividends by the terms of our secured revolving bank credit facility (*see Note 8. Long-Term Debt, Financing and Capital Lease Obligations*).

**Accumulated Other Comprehensive Loss**

The components of accumulated other comprehensive loss, net of tax were as follows:

	March 31,	
	2017	2016
	<i>(in millions)</i>	
Unrecognized net periodic pension and postretirement benefit cost	\$ (369)	\$ (407)
Unrealized net losses on derivatives	(2)	—
Foreign currency translation adjustments	(33)	(32)
Accumulated other comprehensive loss	<u>\$ (404)</u>	<u>\$ (439)</u>

**Per Share Data**

Basic net loss per common share is calculated by dividing net loss by the weighted average number of common shares outstanding during the period. Diluted net loss per common share adjusts basic net loss per common share, computed using the treasury stock method, for the effects of potentially dilutive common shares, if the effect is not antidilutive. Outstanding options and restricted stock units (exclusive of participating securities) that had no effect on our computation of dilutive weighted average number of shares outstanding as their effect would have been antidilutive were approximately 114 million, 73 million, and 56 million as of the years ended March 31, 2017, 2016, and 2015, respectively, in addition to 62 million total shares issuable under warrants, of which 55 million relate to shares issuable under the warrant held by SoftBank. The warrant was issued to SoftBank at the close of the merger with SoftBank and is exercisable at \$5.25 per share at the option of Softbank, in whole or in part, at any time on or prior to July 10, 2018.

**Note 14. Segments**

Sprint operates two reportable segments: Wireless and Wireline.

- Wireless primarily includes retail, wholesale, and affiliate revenue from a wide array of wireless voice and data transmission services and equipment revenue from the sale of wireless devices (handset and tablets) and accessories in the U.S., Puerto Rico and the U.S. Virgin Islands.

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

- Wireline primarily includes revenue from domestic and international wireline voice and data communication services provided to other communications companies and targeted business subscribers, in addition to our Wireless segment.

We define segment earnings as wireless or wireline operating (loss) income before other segment expenses such as depreciation, amortization, severance, exit costs, goodwill impairments, asset impairments, and other items, if any, solely and directly attributable to the segment representing items of a non-recurring or unusual nature. Expense and income items excluded from segment earnings are managed at the corporate level. Transactions between segments are generally accounted for based on market rates, which we believe approximate fair value. The Company generally re-establishes these rates at the beginning of each fiscal year. Over the past several years, there has been an industry-wide trend of lower rates due to increased competition from other wireline and wireless communications companies as well as cable and Internet service providers.

Segment financial information is as follows:

<u>Statement of Operations Information</u>	Wireless	Wireline	Corporate, Other and Eliminations	Consolidated
	<i>(in millions)</i>			
<b>Year Ended March 31, 2017</b>				
Net operating revenues	\$ 31,787	\$ 1,545	\$ 15	\$ 33,347
Inter-segment revenues <sup>(1)</sup>	—	498	(498)	—
Total segment operating expenses	(21,973)	(1,924)	484	(23,413)
Segment earnings	<u>\$ 9,814</u>	<u>\$ 119</u>	<u>\$ 1</u>	9,934
Less:				
Depreciation				(7,098)
Amortization				(1,052)
Other, net <sup>(3)</sup>				(20)
Operating income				1,764
Interest expense				(2,495)
Other expense, net				(40)
Loss before income taxes				<u>\$ (771)</u>

<u>Statement of Operations Information</u>	Wireless	Wireline	Corporate, Other and Eliminations	Consolidated
	<i>(in millions)</i>			
<b>Year Ended March 31, 2016</b>				
Net operating revenues	\$ 30,377	\$ 1,790	\$ 13	\$ 32,180
Inter-segment revenues <sup>(1)</sup>	—	592	(592)	—
Total segment operating expenses	(22,326)	(2,290)	582	(24,034)
Segment earnings	<u>\$ 8,051</u>	<u>\$ 92</u>	<u>\$ 3</u>	8,146
Less:				
Depreciation				(5,794)
Amortization				(1,294)
Other, net <sup>(3)</sup>				(748)
Operating income				310
Interest expense				(2,182)
Other income, net				18
Loss before income taxes				<u>\$ (1,854)</u>



Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

<u>Statement of Operations Information</u>	Wireless	Wireline	Corporate, Other and Eliminations	Consolidated
	(in millions)			
<b>Year Ended March 31, 2015</b>				
Net operating revenues	\$ 32,327	\$ 2,191	\$ 14	\$ 34,532
Inter-segment revenues <sup>(1)</sup>	—	623	(623)	—
Total segment operating expenses	(26,433)	(2,701)	602	(28,532)
Segment earnings	<u>\$ 5,894</u>	<u>\$ 113</u>	<u>\$ (7)</u>	<u>6,000</u>
Less:				
Depreciation				(3,797)
Amortization				(1,552)
Impairments <sup>(2)</sup>				(2,133)
Other, net <sup>(3)</sup>				(413)
Operating loss				(1,895)
Interest expense				(2,051)
Other income, net				27
Loss before income taxes				<u>\$ (3,919)</u>

<u>Other Information</u>	Wireless	Wireline	Corporate and Other	Consolidated
	(in millions)			
<b>As of and for the year ended March 31, 2017</b>				
Capital expenditures	\$ 3,517	\$ 94	\$ 264	\$ 3,875
Total assets	\$ 74,098	\$ 1,168	\$ 9,857	\$ 85,123
<b>As of and for the year ended March 31, 2016</b>				
Capital expenditures	\$ 6,381	\$ 279	\$ 312	\$ 6,972
Total assets	\$ 73,408	\$ 1,255	\$ 4,312	\$ 78,975
<b>As of and for the year ended March 31, 2015</b>				
Capital expenditures	\$ 5,442	\$ 275	\$ 287	\$ 6,004
Total assets	\$ 75,533	\$ 1,262	\$ 6,046	\$ 82,841

(1) Inter-segment revenues consist primarily of wireline services provided to the Wireless segment for resale to or use by wireless subscribers.

(2) Impairments for the year ended March 31, 2015 consist of a \$1.9 billion trade name impairment related to the Wireless segment and a \$233 million impairment related to Wireline long-lived assets.

(3) Other, net for the year ended March 31, 2017 consists of \$66 million of severance and exit costs, a \$140 million charge for a state tax matter combined with legal reserves related to other pending legal suits and proceedings, and a \$28 million loss on disposal of property, plant and equipment related to cell site construction costs that are no longer recoverable as a result of changes in our network plans. In addition, the year ended March 31, 2017 included a \$354 million non-cash gain related to spectrum license exchanges with other carriers and \$140 million of contract termination costs, primarily related to the termination of our pre-existing wholesale arrangement with nTelos, as a result of the Shentel transaction combined with the costs related to the termination of our relationship with General Wireless Operations Inc. (Radio Shack). Losses totaling \$481 million related to the write-off of leased devices associated with lease cancellations were excluded from Other, net and included within Wireless segment earnings. Other, net for the year ended March 31, 2016 consists of \$409 million of severance and exit costs, combined with \$193 million for legal reserves related to various pending legal suits and proceedings and a \$166 million loss on disposal of property, plant and equipment related to cell site construction costs and other network costs that are no longer recoverable as a result of changes in the Company's network plans, partially offset by \$20 million of income resulting from a revision to our estimate of a previously recorded reserve. Losses totaling \$321 million relating to the write-off of leased devices associated with lease cancellations of \$256 million and the loss on sale of devices to MLS under the Handset Sale-Leaseback Tranche 1 transaction for \$65 million was excluded from Other, net and included within Wireless segment earnings. Other, net for the year ended March 31, 2015 consists of \$304 million of severance and exit costs, combined with \$91 million for legal reserves related to various pending legal suits and proceedings and \$59 million for a partial pension settlement, partially offset by \$41 million of income resulting from a revision to our estimate of a previously recorded reserve.



Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

<u>Operating Revenues by Service and Products</u>	Wireless	Wireline	Corporate, Other and Eliminations <sup>(1)</sup>	Consolidated
	<i>(in millions)</i>			
<b>Year Ended March 31, 2017</b>				
Wireless services	\$ 23,115	\$ —	\$ —	\$ 23,115
Wireless equipment	7,979	—	—	7,979
Voice	—	649	(249)	400
Data	—	166	(89)	77
Internet	—	1,147	(157)	990
Other	693	81	12	786
<b>Total net operating revenues</b>	<b>\$ 31,787</b>	<b>\$ 2,043</b>	<b>\$ (483)</b>	<b>\$ 33,347</b>

<u>Operating Revenues by Service and Products</u>	Wireless	Wireline	Corporate, Other and Eliminations <sup>(1)</sup>	Consolidated
	<i>(in millions)</i>			
<b>Year Ended March 31, 2016</b>				
Wireless services	\$ 24,627	\$ —	\$ —	\$ 24,627
Wireless equipment	5,006	—	—	5,006
Voice	—	840	(329)	511
Data	—	171	(69)	102
Internet	—	1,284	(190)	1,094
Other	744	87	9	840
<b>Total net operating revenues</b>	<b>\$ 30,377</b>	<b>\$ 2,382</b>	<b>\$ (579)</b>	<b>\$ 32,180</b>

<u>Operating Revenues by Service and Products</u>	Wireless	Wireline	Corporate, Other and Eliminations <sup>(1)</sup>	Consolidated
	<i>(in millions)</i>			
<b>Year Ended March 31, 2015</b>				
Wireless services	\$ 26,544	\$ —	\$ —	\$ 26,544
Wireless equipment	4,990	—	—	4,990
Voice	—	1,174	(365)	809
Data	—	213	(88)	125
Internet	—	1,353	(165)	1,188
Other	793	74	9	876
<b>Total net operating revenues</b>	<b>\$ 32,327</b>	<b>\$ 2,814</b>	<b>\$ (609)</b>	<b>\$ 34,532</b>

(1) Revenues eliminated in consolidation consist primarily of wireline services provided to the Wireless segment for resale to or use by wireless subscribers.

[Table of Contents](#)[Index to Consolidated Financial Statements](#)

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 15. Quarterly Financial Data (Unaudited)**

	Quarter			
	1st	2nd	3rd	4th
	<i>(in millions, except per share amounts)</i>			
<b>Fiscal year 2016</b>				
Net operating revenues	\$ 8,012	\$ 8,247	\$ 8,549	\$ 8,539
Operating income	\$ 361	\$ 622	\$ 311	\$ 470
Net loss	\$ (302)	\$ (142)	\$ (479)	\$ (283)
Basic and diluted loss per common share <sup>(1)</sup>	\$ (0.08)	\$ (0.04)	\$ (0.12)	\$ (0.07)
<b>Fiscal year 2015</b>				
Net operating revenues	\$ 8,027	\$ 7,975	\$ 8,107	\$ 8,071
Operating income (loss)	\$ 501	\$ (2)	\$ (197)	\$ 8
Net loss	\$ (20)	\$ (585)	\$ (836)	\$ (554)
Basic and diluted loss per common share <sup>(1)</sup>	\$ (0.01)	\$ (0.15)	\$ (0.21)	\$ (0.14)

*(1) The sum of the quarterly earnings per share amounts may not equal the annual amounts because of the changes in the weighted average number of shares outstanding during the year.*

**Note 16. Related-Party Transactions****SoftBank Related-Party Transactions**

In addition to agreements arising out of or relating to the SoftBank Merger, Sprint has entered into various other arrangements with SoftBank or its controlled affiliates (SoftBank Parties) or with third parties to which SoftBank Parties are also parties, including for international wireless roaming, wireless and wireline call termination, real estate, logistical management and other services.

**Brightstar**

We have arrangements with Brightstar US, Inc. (Brightstar), whereby Brightstar provides supply chain and inventory management services to us in our indirect channels and whereby Sprint may sell new and used devices and new accessories to Brightstar for its own purposes. To facilitate certain of these arrangements, we have extended a \$700 million credit line to Brightstar to assist with the purchasing and distribution of devices and accessories. As a result, we shifted our concentration of credit risk away from our indirect channel partners to Brightstar. As Brightstar is a subsidiary of SoftBank, we expect SoftBank will provide the necessary support to ensure that Brightstar will fulfill its obligations to us under these agreements. However, we have no assurance that SoftBank will provide such support.

The supply chain and inventory management arrangement included, among other things, that Brightstar may purchase inventory from the OEMs to sell directly to our indirect dealers. As compensation for these services, we remit per unit fees to Brightstar for each device sold to dealers or retailers in our indirect channels. During the years ended March 31, 2017, 2016, and 2015 we incurred fees under these arrangements totaling \$64 million, \$102 million, and \$66 million, respectively. Additionally, we have an arrangement with Brightstar whereby they perform certain of our reverse logistics including device buyback, trade-in technology and related services. We may also purchase new and used devices and accessories from Brightstar to be sold in our direct channels.

[Table of Contents](#)[Index to Consolidated Financial Statements](#)

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

Amounts included in our consolidated financial statements associated with these arrangements with Brightstar were as follows:

Consolidated balance sheets:	March 31,	
	2017	2016
	<i>(in millions)</i>	
Accounts receivable	\$ 367	\$ 197
Accounts payable	\$ 160	\$ 96

Consolidated statements of operations:	Year Ended March 31,		
	2017	2016	2015
	<i>(in millions)</i>		
Equipment revenues	\$ 1,682	\$ 1,731	\$ 1,818
Cost of products	\$ 1,600	\$ 1,743	\$ 1,887

In addition, Sprint earned fees of approximately \$100 million, \$103 million, and \$13 million from a Brightstar subsidiary, in the years ended March 31, 2017, 2016, and 2015, respectively, for billing and collecting payments from subscribers under certain insurance programs.

**SoftBank**

In November 2015 and April 2016, Sprint entered into Handset Sale-Leaseback transactions with MLS, a company formed by a group of equity investors, including SoftBank, to sell and lease-back certain devices, which are currently being leased by our customers, for total cash proceeds of approximately \$2.2 billion. SoftBank's initial equity investment in MLS totaled \$79 million. Brightstar provides reverse logistics and remarketing services to MLS with respect to the devices.

In December 2016, Handset Sale-Leaseback Tranche I was terminated and the associated devices were repurchased by Sprint from MLS. With the cash proceeds, MLS repurchased the equity units from its investors including SoftBank. As a result, SoftBank's remaining equity investment in MLS totaled \$39 million as of March 31, 2017.

In April 2016, Sprint sold and leased back certain network equipment to Network LeaseCo. The network equipment acquired by Network LeaseCo, which is consolidated by us, was used as collateral to raise approximately \$2.2 billion in borrowings from external investors, including \$250 million from SoftBank. Principal and interest payments on the borrowings from the external investors will be repaid in staggered, unequal payments through January 2018 (See Note 3. *Funding Sources*) with the first principal payment of approximately \$300 million paid in March 2017 followed by the remaining \$1.9 billion of principal payments due in fiscal year 2017.

All other transactions under agreements with SoftBank Parties, in the aggregate, were immaterial through the period ended March 31, 2017.

[Table of Contents](#)

[Index to Consolidated Financial Statements](#)

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 17. Guarantor Financial Information**

On September 11, 2013, Sprint Corporation issued \$2.25 billion aggregate principal amount of 7.250% notes due 2021 and \$4.25 billion aggregate principal amount of 7.875% notes due 2023 in a private placement transaction with registration rights. On December 12, 2013, Sprint Corporation issued \$2.5 billion aggregate principal amount of 7.125% notes due 2024 in a private placement transaction with registration rights. Each of these issuances is fully and unconditionally guaranteed by Sprint Communications, Inc. (Subsidiary Guarantor), which is a 100% owned subsidiary of Sprint Corporation (Parent/Issuer). In connection with the foregoing, the registration rights agreements with respect to the notes required the Company and Sprint Communications, Inc. to use their reasonable best efforts to cause an offer to exchange the notes for a new issue of substantially identical exchange notes registered under the Securities Act of 1933. Accordingly, in November 2014, we completed an exchange offer for these notes in compliance with our registration obligations. We did not receive any proceeds from this exchange offer. In addition, on February 24, 2015, Sprint Corporation issued \$1.5 billion aggregate principal amount of 7.625% notes due 2025, which are fully and unconditionally guaranteed by Sprint Communications, Inc.

During the years ended March 31, 2017 and 2016 there were non-cash equity contributions from the Subsidiary Guarantor to the Non-Guarantor Subsidiaries as a result of organizational restructuring for tax purposes of approximately \$450 million and \$1.5 billion, respectively.

Under the Subsidiary Guarantor's secured revolving bank credit facility, the Subsidiary Guarantor is currently restricted from paying cash dividends to the Parent/Issuer or any Non-Guarantor Subsidiary because the ratio of total indebtedness to adjusted EBITDA (each as defined in the applicable agreement) exceeds 2.5 to 1.0.

Sprint has a Receivables Facility providing for the sale of eligible wireless service, installment and certain future lease receivables. In November 2015, Sprint also entered into the Tranche 1 transaction to sell and lease-back certain leased devices, which was subsequently terminated in December 2016. In April 2016, Sprint entered into the Tranche 2 transaction to sell and leaseback certain leased devices and a Network Equipment Sale-Leaseback to sell and leaseback certain network equipment. In connection with the Receivables Facility, Tranches 1 and 2 and the Network Equipment Sale-Leaseback, Sprint formed certain wholly-owned consolidated bankruptcy-remote SPEs and SPE Lessees that are included in the non-guarantor subsidiaries condensed consolidated financial information. Each SPE and SPE Lessee is a separate legal entity with its own separate creditors who will be entitled, prior to and upon the liquidation of the SPE or SPE Lessee, to be satisfied out of the SPE or SPE Lessee's assets prior to any assets in the SPE and SPE Lessee becoming available to Sprint (*see Note 3. Funding Sources*).

We have accounted for investments in subsidiaries using the equity method. Presented below is the condensed consolidating financial information.

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

## CONDENSED CONSOLIDATING BALANCE SHEET

	As of March 31, 2017				
	<i>Parent/Issuer</i>	<i>Subsidiary Guarantor</i>	<i>Non- Guarantor Subsidiaries</i>	<i>Eliminations</i>	<i>Consolidated</i>
	<i>(in millions)</i>				
<b>ASSETS</b>					
Current assets:					
Cash and cash equivalents	\$ —	\$ 2,461	\$ 409	\$ —	\$ 2,870
Short-term investments	—	5,444	—	—	5,444
Accounts and notes receivable, net	86	1	4,137	(86)	4,138
Device and accessory inventory	—	—	1,064	—	1,064
Prepaid expenses and other current assets	—	11	590	—	601
Total current assets	86	7,917	6,200	(86)	14,117
Investments in subsidiaries	18,800	23,854	—	(42,654)	—
Property, plant and equipment, net	—	—	19,209	—	19,209
Due from consolidated affiliate	25	13,032	—	(13,057)	—
Note receivable from consolidated affiliate	10,394	575	—	(10,969)	—
Intangible assets					
Goodwill	—	—	6,579	—	6,579
PCC licenses and other	—	—	40,585	—	40,585
Definite-lived intangible assets, net	—	—	3,320	—	3,320
Other assets	—	134	1,179	—	1,313
Total assets	<u>\$ 29,305</u>	<u>\$ 45,512</u>	<u>\$ 77,072</u>	<u>\$ (66,766)</u>	<u>\$ 85,123</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>					
Current liabilities:					
Accounts payable	\$ —	\$ —	\$ 3,281	\$ —	\$ 3,281
Accrued expenses and other current liabilities	103	478	3,646	(86)	4,141
Current portion of long-term debt, financing and capital lease obligations	—	1,356	3,680	—	5,036
Total current liabilities	103	1,834	10,607	(86)	12,458
Long-term debt, financing and capital lease obligations	10,394	13,647	11,837	—	35,878
Note payable due to consolidated affiliate	—	10,394	575	(10,969)	—
Deferred tax liabilities	—	—	14,416	—	14,416
Other liabilities	—	837	2,726	—	3,563
Due to consolidated affiliate	—	—	13,057	(13,057)	—
Total liabilities	10,497	26,712	53,218	(24,112)	66,315
Commitments and contingencies					
Total stockholders' equity	18,808	18,800	23,854	(42,654)	18,808
Total liabilities and stockholders' equity	<u>\$ 29,305</u>	<u>\$ 45,512</u>	<u>\$ 77,072</u>	<u>\$ (66,766)</u>	<u>\$ 85,123</u>

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

## CONDENSED CONSOLIDATING BALANCE SHEET

	As of March 31, 2016				
	<i>Parent/Issuer</i>	<i>Subsidiary Guarantor</i>	<i>Non- Guarantor Subsidiaries</i>	<i>Eliminations</i>	<i>Consolidated</i>
	<i>(in millions)</i>				
<b>ASSETS</b>					
Current assets:					
Cash and cash equivalents	\$ —	\$ 2,154	\$ 487	\$ —	\$ 2,641
Accounts and notes receivable, net	87	27	1,099	(114)	1,099
Device and accessory inventory	—	—	1,173	—	1,173
Prepaid expenses and other current assets	—	12	1,908	—	1,920
Total current assets	87	2,193	4,667	(114)	6,833
Investments in subsidiaries	19,783	23,129	—	(42,912)	—
Property, plant and equipment, net	—	—	20,297	—	20,297
Due from consolidated affiliate	50	19,518	—	(19,568)	—
Note receivable from consolidated affiliate	10,377	245	—	(10,622)	—
Intangible assets					
Goodwill	—	—	6,575	—	6,575
FCC licenses and other	—	—	40,073	—	40,073
Definite-lived intangible assets, net	—	—	4,469	—	4,469
Other assets	—	1,127	620	(1,019)	728
Total assets	<u>\$ 30,297</u>	<u>\$ 46,212</u>	<u>\$ 76,701</u>	<u>\$ (74,235)</u>	<u>\$ 78,975</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>					
Current liabilities:					
Accounts payable	\$ —	\$ —	\$ 2,899	\$ —	\$ 2,899
Accrued expenses and other current liabilities	137	531	3,820	(114)	4,374
Current portion of long-term debt, financing and capital lease obligations	—	3,065	1,625	—	4,690
Total current liabilities	137	3,596	8,344	(114)	11,963
Long-term debt, financing and capital lease obligations	10,377	11,495	8,415	(1,019)	29,268
Note payable due to consolidated affiliate	—	10,377	245	(10,622)	—
Deferred tax liabilities	—	—	13,959	—	13,959
Other liabilities	—	961	3,041	—	4,002
Due to consolidated affiliate	—	—	19,568	(19,568)	—
Total liabilities	10,514	26,429	53,572	(31,323)	59,192
Commitments and contingencies					
Total stockholders' equity	19,783	19,783	23,129	(42,912)	19,783
Total liabilities and stockholders' equity	<u>\$ 30,297</u>	<u>\$ 46,212</u>	<u>\$ 76,701</u>	<u>\$ (74,235)</u>	<u>\$ 78,975</u>

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

## CONDENSED CONSOLIDATING STATEMENT OF COMPREHENSIVE LOSS

	Year Ended March 31, 2017				
	Parent/Issuer	Subsidiary Guarantor	Non- Guarantor Subsidiaries	Eliminations	Consolidated
	(in millions)				
Net operating revenues:					
Service	\$ —	\$ —	\$ 25,368	\$ —	\$ 25,368
Equipment	—	—	7,979	—	7,979
	—	—	33,347	—	33,347
Net operating expenses:					
Cost of services (exclusive of depreciation and amortization below)	—	—	7,861	—	7,861
Cost of products (exclusive of depreciation and amortization below)	—	—	7,077	—	7,077
Selling, general and administrative	—	—	7,994	—	7,994
Severance and exit costs	—	—	66	—	66
Depreciation	—	—	7,098	—	7,098
Amortization	—	—	1,052	—	1,052
Other, net	—	—	435	—	435
	—	—	31,583	—	31,583
Operating income	—	—	1,764	—	1,764
Other (expense) income:					
Interest income	790	145	21	(896)	60
Interest expense	(790)	(1,675)	(926)	896	(2,495)
(Losses) earnings of subsidiaries	(1,206)	402	—	804	—
Other expense, net	—	(78)	(22)	—	(100)
	(1,206)	(1,206)	(927)	804	(2,535)
(Loss) income before income taxes	(1,206)	(1,206)	837	804	(771)
Income tax expense	—	—	(435)	—	(435)
Net (loss) income	(1,206)	(1,206)	402	804	(1,206)
Other comprehensive income (loss)	35	35	42	(77)	35
Comprehensive (loss) income	\$ (1,171)	\$ (1,171)	\$ 444	\$ 727	\$ (1,171)

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

## CONDENSED CONSOLIDATING STATEMENT OF COMPREHENSIVE LOSS

	Year Ended March 31, 2016				
	<i>Parent/Issuer</i>	<i>Subsidiary Guarantor</i>	<i>Non- Guarantor Subsidiaries</i>	<i>Eliminations</i>	<i>Consolidated</i>
	<i>(in millions)</i>				
Net operating revenues:					
Service	\$ —	\$ —	\$ 27,174	\$ —	\$ 27,174
Equipment	—	—	5,006	—	5,006
	—	—	32,180	—	32,180
Net operating expenses:					
Cost of services (exclusive of depreciation and amortization below)	—	—	9,439	—	9,439
Cost of products (exclusive of depreciation and amortization below)	—	—	5,795	—	5,795
Selling, general and administrative	—	—	8,479	—	8,479
Severance and exit costs	—	—	409	—	409
Depreciation	—	—	5,794	—	5,794
Amortization	—	—	1,294	—	1,294
Other, net	—	—	660	—	660
	—	—	31,870	—	31,870
Operating income	—	—	310	—	310
Other (expense) income:					
Interest income	790	165	5	(949)	11
Interest expense	(790)	(1,624)	(717)	949	(2,182)
(Losses) earnings of subsidiaries	(1,997)	(538)	—	2,535	—
Other income, net	—	—	7	—	7
	(1,997)	(1,997)	(705)	2,535	(2,164)
(Loss) income before income taxes	(1,997)	(1,997)	(395)	2,535	(1,854)
Income tax benefit (expense)	2	—	(143)	—	(141)
Net (loss) income	(1,995)	(1,997)	(538)	2,535	(1,995)
Other comprehensive (loss) income	(31)	(31)	(21)	52	(31)
Comprehensive (loss) income	\$ (2,026)	\$ (2,028)	\$ (559)	\$ 2,587	\$ (2,026)

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

## CONDENSED CONSOLIDATING STATEMENT OF COMPREHENSIVE LOSS

	Year Ended March 31, 2015				
	<i>Parent/Issuer</i>	<i>Subsidiary Guarantor</i>	<i>Non-Guarantor Subsidiaries</i>	<i>Eliminations</i>	<i>Consolidated</i>
	<i>(in millions)</i>				
Net operating revenues:					
Service	\$ —	\$ —	\$ 29,542	\$ —	\$ 29,542
Equipment	—	—	4,990	—	4,990
	—	—	34,532	—	34,532
Net operating expenses:					
Cost of services (exclusive of depreciation and amortization below)	—	—	9,660	—	9,660
Cost of products (exclusive of depreciation and amortization below)	—	—	9,309	—	9,309
Selling, general and administrative	—	—	9,563	—	9,563
Impairments	—	—	2,133	—	2,133
Severance and exit costs	—	—	304	—	304
Depreciation	—	—	3,797	—	3,797
Amortization	—	—	1,552	—	1,552
Other, net	—	1	108	—	109
	—	1	36,426	—	36,427
Operating loss	—	(1)	(1,894)	—	(1,895)
Other (expense) income:					
Interest income	687	146	3	(824)	12
Interest expense	(687)	(1,521)	(667)	824	(2,051)
(Losses) earnings of subsidiaries	(3,345)	(1,970)	—	5,315	—
Other income, net	—	1	14	—	15
	(3,345)	(3,344)	(650)	5,315	(2,024)
(Loss) income before income taxes	(3,345)	(3,345)	(2,544)	5,315	(3,919)
Income tax benefit	—	—	574	—	574
Net (loss) income	(3,345)	(3,345)	(1,970)	5,315	(3,345)
Other comprehensive (loss) income	(365)	(365)	(355)	720	(365)
Comprehensive (loss) income	\$ (3,710)	\$ (3,710)	\$ (2,325)	\$ 6,035	\$ (3,710)

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

## CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS

Year Ended March 31, 2017

	<i>Parent/Issuer</i>	<i>Subsidiary Guarantor</i>	<i>Non- Guarantor Subsidiaries</i>	<i>Eliminations</i>	<i>Consolidated</i>
	<i>(in millions)</i>				
Cash flows from operating activities					
Net cash (used in) provided by operating activities	\$ —	\$ (1,629)	\$ 5,996	\$ (199)	\$ 4,168
Cash flows from investing activities:					
Capital expenditures - network and other	—	—	(1,950)	—	(1,950)
Capital expenditures - leased devices	—	—	(1,925)	—	(1,925)
Expenditures relating to FCC licenses	—	—	(83)	—	(83)
Proceeds from sales and maturities of short-term investments	—	4,566	55	—	4,621
Purchases of short-term investments	—	(10,010)	(55)	—	(10,065)
Change in amounts due from/due to consolidated affiliates	—	7,097	—	(7,097)	—
Proceeds from sales of assets and FCC licenses	—	—	219	—	219
Intercompany note advance to consolidated affiliate	—	(414)	—	414	—
Proceeds from intercompany note advance to consolidated affiliate	—	84	—	(84)	—
Other, net	—	—	(42)	—	(42)
Net cash provided by (used in) investing activities	—	1,323	(3,781)	(6,767)	(9,225)
Cash flows from financing activities:					
Proceeds from debt and financings	—	4,000	6,966	—	10,966
Repayments of debt, financing and capital lease obligations	—	(3,250)	(2,167)	—	(5,417)
Debt financing costs	—	(187)	(171)	—	(358)
Intercompany dividends paid to consolidated affiliate	—	—	(199)	199	—
Change in amounts due from/due to consolidated affiliates	—	—	(7,097)	7,097	—
Intercompany note advance from parent	—	—	414	(414)	—
Repayments of intercompany note advance from parent	—	—	(84)	84	—
Other, net	—	50	45	—	95
Net cash provided by (used in) financing activities	—	613	(2,293)	6,966	5,286
Net increase (decrease) in cash and cash equivalents	—	307	(78)	—	229
Cash and cash equivalents, beginning of period	—	2,154	487	—	2,641
Cash and cash equivalents, end of period	\$ —	\$ 2,461	\$ 409	\$ —	\$ 2,870

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

## CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS

	Year Ended March 31, 2016				
	<i>Parent/Issuer</i>	<i>Subsidiary Guarantor</i>	<i>Non-Guarantor Subsidiaries</i>	<i>Eliminations</i>	<i>Consolidated</i>
	<i>(in millions)</i>				
Cash flows from operating activities:					
Net cash (used in) provided by operating activities	\$ —	\$ (1,421)	\$ 5,551	\$ (233)	\$ 3,897
Cash flows from investing activities:					
Capital expenditures - network and other	—	—	(4,680)	—	(4,680)
Capital expenditures - leased devices	—	—	(2,292)	—	(2,292)
Expenditures relating to FCC licenses	—	—	(98)	—	(98)
Proceeds from sales and maturities of short-term investments	—	343	75	—	418
Purchases of short-term investments	—	(197)	(55)	—	(252)
Change in amounts due from/due to consolidated affiliates	1	(36)	—	35	—
Proceeds from sales of assets and FCC licenses	—	—	62	—	62
Proceeds from sale-leaseback transaction	—	—	1,136	—	1,136
Intercompany note advance to consolidated affiliate	—	(159)	—	159	—
Proceeds from intercompany note advance to consolidated affiliate	—	372	—	(372)	—
Other, net	—	—	(29)	—	(29)
Net cash provided by (used in) investing activities	1	323	(5,881)	(178)	(5,735)
Cash flows from financing activities:					
Proceeds from debt and financings	—	250	1,105	—	1,355
Repayments of debt, financing and capital lease obligations	—	(500)	(399)	—	(899)
Debt financing costs	(1)	—	(10)	—	(11)
Intercompany dividends paid to consolidated affiliate	—	—	(233)	233	—
Change in amounts due from/due to consolidated affiliates	—	—	35	(35)	—
Intercompany note advance from parent	—	—	159	(159)	—
Repayments of intercompany note advance from parent	—	—	(372)	372	—
Other, net	—	10	14	—	24
Net cash (used in) provided by financing activities	(1)	(240)	299	411	469
Net decrease in cash and cash equivalents	—	(1,338)	(31)	—	(1,369)
Cash and cash equivalents, beginning of period	—	3,492	518	—	4,010
Cash and cash equivalents, end of period	\$ —	\$ 2,154	\$ 487	\$ —	\$ 2,641

Table of ContentsIndex to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

## CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS

	Year Ended March 31, 2015				
	<i>Parent/Issuer</i>	<i>Subsidiary Guarantor</i>	<i>Non-Guarantor Subsidiaries</i>	<i>Eliminations</i>	<i>Consolidated</i>
	<i>(in millions)</i>				
Cash flows from operating activities:					
Net cash (used in) provided by operating activities	\$ —	\$ (750)	\$ 3,700	\$ (500)	\$ 2,450
Cash flows from investing activities:					
Capital expenditures - network and other	—	—	(5,422)	—	(5,422)
Capital expenditures - leased devices	—	—	(582)	—	(582)
Expenditures relating to FCC licenses	—	—	(163)	—	(163)
Reimbursements relating to FCC licenses	—	—	95	—	95
Proceeds from sales and maturities of short-term investments	—	3,061	70	—	3,131
Purchases of short-term investments	—	(1,987)	(90)	—	(2,077)
Change in amounts due from/due to consolidated affiliates	—	(2,425)	—	2,425	—
Proceeds from sales of assets and FCC licenses	—	—	315	—	315
Intercompany note advance to consolidated affiliate	(1,481)	(343)	—	1,824	—
Other, net	—	—	(11)	—	(11)
Net cash (used in) provided by investing activities	(1,481)	(1,694)	(5,788)	4,249	(4,714)
Cash flows from financing activities:					
Proceeds from debt and financings	1,500	300	130	—	1,930
Repayments of debt and capital lease obligations	—	—	(574)	—	(574)
Debt financing costs	(21)	(5)	(61)	—	(87)
Intercompany dividends paid to consolidated affiliate	—	—	(500)	500	—
Change in amounts due from/due to consolidated affiliates	2	—	2,423	(2,425)	—
Intercompany note advance from parent	—	1,481	343	(1,824)	—
Other, net	—	35	—	—	35
Net cash provided by (used in) financing activities	1,481	1,811	1,761	(3,749)	1,304
Net decrease in cash and cash equivalents	—	(633)	(327)	—	(960)
Cash and cash equivalents, beginning of period	—	4,125	845	—	4,970
Cash and cash equivalents, end of period	\$ —	\$ 3,492	\$ 518	\$ —	\$ 4,010

Table of Contents

Index to Consolidated Financial Statements

**SPRINT CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 18. Subsequent Events**

**Cash Tender Offers for Certain Outstanding Debt**

On May 9, 2017, the Company's wholly-owned subsidiary, Sprint Communications, Inc. commenced tender offers to purchase for cash up to an aggregate principal amount of \$1.0 billion of its 9.000% Guaranteed Notes due 2018 and its 8.375% Notes due 2017. The tender offer with respect to the Guaranteed Notes due 2018 is also subject to a maximum principal amount sublimit of \$500 million. On May 23, 2017, the Company subsequently amended the terms of the tender offers to increase the aggregate principal amount of notes subject to the tender offers to \$1.7 billion and increase the maximum principal amount sublimit applicable to the Guaranteed Notes due 2018 to \$1.2 billion. The tender offers are intended to lower the Company's current overall interest expense and decrease current debt levels and will be funded by available cash on hand. The tender offers will each expire on June 6, 2017, unless extended or earlier terminated by the Company in accordance with the terms of the offers.

As of May 23, 2017, the Company had accepted early tenders for approximately \$1.2 billion principal amount of 9.000% Guaranteed Notes due 2018 and approximately \$388 million principal amount of 8.375% Notes due 2017. As a result of the early tenders, approximately \$1.6 billion aggregate principal amount of debt was retired, and the tender offer for 9.000% Guaranteed Notes due 2018 was concluded. The tender offer for 8.375% Notes due 2017 is still in effect until June 6, 2017, although it is now limited to approximately \$112 million principal amount of such notes.

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

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2016  
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: 1-33409

**T-Mobile**

**T-MOBILE US, INC.**

(Exact name of registrant as specified in its charter)

DELAWARE

20-0836269

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

12920 SE 38th Street, Bellevue, Washington

98006-1350

(Address of principal executive offices)

(Zip Code)

(425) 378-4000

(Registrant's telephone number, including area code)

**Securities registered pursuant to Section 12(b) of the Act:**

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, \$0.00001 par value per share	The NASDAQ Stock Market LLC
5.50% Mandatory Convertible Preferred Stock, Series A, \$0.00001 par value per share	The NASDAQ Stock Market LLC

**Securities registered pursuant to Section 12(g) of the Act:**

None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark 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  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of June 30, 2016, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was \$12.4 billion based on the closing sale price as reported on the New York Stock Exchange. As of February 8, 2017, there were 826,525,821 shares of

common stock outstanding.

#### **DOCUMENTS INCORPORATED BY REFERENCE**

Part III of this Annual Report on Form 10-K incorporates by reference certain portions of the definitive Proxy Statement for the registrant's Annual Meeting of Stockholders, which definitive Proxy Statement shall be filed with the Securities and Exchange Commission within 120 days after the end of the fiscal year to which this Report relates.

**T-Mobile US, Inc.**  
**Form 10-K**  
**For the Year Ended December 31, 2016**

**Table of Contents**

**PART I**

<u>Item 1.</u>	<u>Business</u>	<u>3</u>
<u>Item 1A.</u>	<u>Risk Factors</u>	<u>9</u>
<u>Item 1B.</u>	<u>Unresolved Staff Comments</u>	<u>20</u>
<u>Item 2.</u>	<u>Properties</u>	<u>20</u>
<u>Item 3.</u>	<u>Legal Proceedings</u>	<u>20</u>
<u>Item 4.</u>	<u>Mine Safety Disclosures</u>	<u>20</u>

**PART II**

<u>Item 5.</u>	<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>20</u>
<u>Item 6.</u>	<u>Selected Financial Data</u>	<u>22</u>
<u>Item 7.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>23</u>
<u>Item 7A.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>46</u>
<u>Item 8.</u>	<u>Financial Statements and Supplementary Data</u>	<u>48</u>
<u>Item 9.</u>	<u>Changes in and Disagreements With Accountants on Accounting and Financial Disclosure</u>	<u>93</u>
<u>Item 9A.</u>	<u>Controls and Procedures</u>	<u>93</u>
<u>Item 9B.</u>	<u>Other Information</u>	<u>94</u>

**PART III**

<u>Item 10.</u>	<u>Directors, Executive Officers and Corporate Governance</u>	<u>94</u>
<u>Item 11.</u>	<u>Executive Compensation</u>	<u>95</u>
<u>Item 12.</u>	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>95</u>
<u>Item 13.</u>	<u>Certain Relationships and Related Transactions, and Director Independence</u>	<u>95</u>
<u>Item 14.</u>	<u>Principal Accounting Fees and Services</u>	<u>95</u>

**PART IV**

<u>Item 15.</u>	<u>Exhibits and Financial Statement Schedules</u>	<u>95</u>
<u>Item 16.</u>	<u>Form 10-K Summary</u>	<u>95</u>
	<u>SIGNATURES</u>	<u>96</u>
	<u>INDEX TO EXHIBITS</u>	<u>98</u>

## Cautionary Statement Regarding Forward-Looking Statements

This Annual Report on Form 10-K ("Form 10-K") includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical fact, including information concerning our future results of operations, are forward-looking statements. These forward-looking statements are generally identified by the words "anticipate," "believe," "estimate," "expect," "intend," "may," "could" or similar expressions. Forward-looking statements are based on current expectations and assumptions, which are subject to risks and uncertainties and may cause actual results to differ materially from the forward-looking statements. The following important factors, along with the Risk Factors included in Part I, Item 1A of this Form 10-K, could affect future results and cause those results to differ materially from those expressed in the forward-looking statements:

- adverse economic or political conditions in the U.S. and international markets;
- competition in the wireless services market, including new competitors entering the industry as technologies converge;
- the effects any future merger or acquisition involving us, as well as the effects of mergers or acquisitions in the technology, media and telecommunications industry;
- challenges in implementing our business strategies or funding our wireless operations, including payment for additional spectrum or network upgrades;
- the possibility that we may be unable to renew our spectrum licenses on attractive terms or acquire new spectrum licenses at reasonable costs and terms;
- difficulties in managing growth in wireless data services, including network quality;
- material changes in available technology;
- the timing, scope and financial impact of our deployment of advanced network and business technologies;
- the impact on our networks and business from major technology equipment failures;
- breaches of our and/or our third party vendors' networks, information technology ("IT") and data security;
- natural disasters, terrorist attacks or similar incidents;
- existing or future litigation;
- any changes in the regulatory environments in which we operate, including any increase in restrictions on the ability to operate our networks;
- any disruption or failure of our third parties' or key suppliers' provisioning of products or services;
- material adverse changes in labor matters, including labor campaigns, negotiations or additional organizing activity, and any resulting financial, operational and/or reputational impact;
- the ability to make payments on our debt or to repay our existing indebtedness when due;
- adverse change in the ratings of our debt securities or adverse conditions in the credit markets;
- changes in accounting assumptions that regulatory agencies, including the Securities and Exchange Commission ("SEC"), may require, which could result in an impact on earnings; and,
- changes in tax laws, regulations and existing standards and the resolution of disputes with any taxing jurisdictions.

Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements. We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements, except as required by law. In this Form 10-K, unless the context indicates otherwise, references to "T-Mobile," "T-Mobile US," "our Company," "the Company," "we," "our," and "us" refer to T-Mobile US, Inc., a Delaware corporation, and its wholly-owned subsidiaries.

## PART I.

### Item 1. Business

#### Business Overview

We are the Un-carrier<sup>®</sup>. Un-satisfied with the status quo. Un-afraid to innovate. T-Mobile is the fastest growing wireless company in the U.S. based on customer growth in 2016. T-Mobile provides wireless communications services, including voice, messaging and data, to more than 71 million customers in the postpaid, prepaid and wholesale markets. The Un-carrier strategy is an approach that seeks to listen to the customer, address their pain points, bring innovation to the industry and improve the wireless experience for all. In practice, this means offering our customers a great service on a nationwide 4G Long-Term Evolution ("LTE") network, offering devices when and how our customers want them, and providing plans that are simple, affordable and without unnecessary restrictions. Going forward, we will continue to listen and respond to our customers, refine and improve the Un-carrier strategy and deliver the best value experience in the industry.

Table of Contents**History**

T-Mobile USA, Inc. ("T-Mobile USA") was formed in 1994 as VoiceStream Wireless PCS ("VoiceStream"), a subsidiary of Western Wireless Corporation ("Western Wireless"). VoiceStream was spun off from Western Wireless in 1999, acquired by Deutsche Telekom AG ("Deutsche Telekom") in 2001 and renamed T-Mobile USA, Inc. in 2002.

In 2013, T-Mobile US, Inc. was formed through the business combination between T-Mobile USA and MetroPCS Communications, Inc. ("MetroPCS"). The business combination was accounted for as a reverse acquisition with T-Mobile USA as the accounting acquirer. Accordingly, T-Mobile USA's historical financial statements became the historical financial statements of the combined company.

Our common stock and our 5.50% mandatory convertible preferred stock, Series A ("preferred stock") trade on the NASDAQ Global Select Market of The NASDAQ Stock Market LLC ("NASDAQ") under the symbols "TMUS" and "TMUSP," respectively.

**Business Strategy**

We generate revenue by offering affordable wireless communication services to our postpaid, prepaid and wholesale customers, as well as a wide selection of wireless devices and accessories. Our most significant expenses are related to acquiring and retaining high-quality customers, providing a full range of devices, compensating employees, and operating and expanding our network. We provide service, devices and accessories across our flagship brands, T-Mobile and MetroPCS, through our owned and operated retail stores, third party distributors and our websites (www.T-Mobile.com and www.MetroPCS.com). The information on our websites is not part of this Form 10-K.

We continue to aggressively pursue our strategy, which includes the following elements:

*Un-carrier Strategy*

We introduced our Un-carrier strategy in 2013 and continue to aggressively focus on addressing customer pain points with the launch of additional signature moves. Un-carrier initiatives have included, but are not limited to, offering the following to qualifying customers:

- providing customers with affordable rate plans while eliminating annual service contracts;
- allowing customers easier options to upgrade their eligible devices when they want;
- reimbursing qualifying customers' early termination fees and/or remaining phone payments when they switch from other carriers and trade-in their phones;
- allowing customers to stream music without it counting against their high speed data allotment;
- providing Wi-Fi calling and texting for customers with capable smartphones;
- giving qualified customers the ability to roll-over up to 20 GB per year of their unused high-speed data automatically each month;
- providing reduced United States to international calling rates, and providing messaging and data roaming while traveling abroad at no extra charge;
- allowing customers to access coverage and calling, as well as 4G LTE data, across the U.S., Mexico and Canada at no extra charge;
- providing select video streaming services without it counting against their high speed data allotment on qualifying plans;
- offering eligible new (through December 31, 2016) or existing (as of June 6, 2016) customers ownership in the Company with a free share of T-Mobile stock or an additional share of T-Mobile stock for every new active account each customer refers through December 31, 2016, subject to a maximum of 100 shares in a calendar year;
- enabling eligible customers who download the T-Mobile Tuesday app to be informed about and to redeem products and services offered by participating business partners each Tuesday;
- offering eligible customers a full hour of free in-flight Wi-Fi on their smartphone on all Gogo-equipped domestic flights;
- giving our customers one simple rate plan, T-Mobile ONE™, that includes unlimited calls, unlimited text and unlimited high-speed 4G LTE data on their device; and



## Table of Contents

- beginning in 2017, with our introduction of Un-carrier Next, T-Mobile ONE includes:
  - monthly wireless service fees and taxes in the advertised monthly recurring charge;
  - paying participating customers back for data that is not used in a month if they use less than 2GB high-speed data/month; and
  - giving customers the first-ever price guarantee on an unlimited 4G LTE plan and allowing our customers to keep their T-Mobile ONE price until they decide to change it.

### *Customer Experience*

The ongoing success of our Un-carrier strategy and continued transformation of the network has strengthened T-Mobile's position as a provider of dependable high-speed 4G LTE service. Additionally, we have continued to focus on retaining customers by delivering an improved wireless customer experience. Branded postpaid phone churn improved to 1.30% in 2016, compared to 1.39% in 2015 and 1.58% in 2014. On September 1, 2016, we sold our marketing and distribution rights to certain existing T-Mobile co-branded customers to a current Mobile Virtual Network Operators ("MVNO") partner for nominal consideration. The impact of this transaction resulted in improvements to branded postpaid phone churn for the year ended December 31, 2016. See Performance Measures of Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation of this Form 10-K for information regarding this transaction. Our branded postpaid net customer additions remained strong with 4.1 million in 2016, compared to 4.5 million in 2015 and 4.9 million in 2014, primarily driven by strong customer response to our Un-carrier initiatives, ongoing improvements to network quality, and promotions for services and devices. In addition, we continue to buildout our Extended Range LTE, which operates on our low-band 700 MHz A-Block spectrum. These results reinforce our position as an organization with a strong focus and commitment to providing an outstanding customer experience.

### *Aligned Cost Structure*

We continue to pursue a low-cost business operating model to drive cost savings, which can then be reinvested in the business. These cost-reduction programs are on-going as we continue to simplify our business and drive operational efficiencies and cost savings in areas, such as network optimization, customer roaming and customer service. A portion of these savings have been, and will continue to be, reinvested into growth of our business.

### **Customers**

We provide wireless communication services to three primary categories of customers:

- Branded postpaid customers generally include customers that are qualified to pay after using wireless communication services;
- Branded prepaid customers generally include customers who pay for wireless communication services in advance. Our branded prepaid customers include customers of T-Mobile and MetroPCS; and
- Wholesale customers include Machine-to-Machine ("M2M") and MVNO that operate on our network, but are managed by wholesale partners.

We generate the majority of our service revenues by providing wireless communication services to branded postpaid and branded prepaid customers. Our ability to acquire and retain branded postpaid and prepaid customers is important to our business in the generation of service revenues, equipment revenues and other revenues. In 2016, our service revenues generated by providing wireless communication services by customer category were:

- 65% branded postpaid customers;
- 31% branded prepaid customers; and
- 4% wholesale customers, roaming and other services.

### **Services and Products**

We provide wireless communication services through a variety of service plan options. We also offer a wide selection of wireless devices, including smartphones, tablets and other mobile communication devices, which are manufactured by various suppliers. Services, devices and accessories are offered directly to consumers through our owned and operated retail stores, as



## Table of Contents

well as through our websites. In addition, we sell devices to dealers and other third party distributors for resale through independent third-party retail outlets and a variety of third-party websites.

Our service plan offerings, which allow customers to subscribe for wireless services separately from the purchase of a device include:

- Our T-Mobile ONE plan (T-Mobile ONE), which was launched in September 2016 as phase 12.0 of our Un-carrier initiatives. T-Mobile ONE gives our customers unlimited calls, unlimited text and unlimited high-speed 4G LTE data on their device. On T-Mobile ONE, video typically streams at DVD (480p) quality and tethering is at maximum 3G speeds. Customers can choose to add on additional features to T-Mobile ONE for an additional cost. On T-Mobile ONE Plus customers also receive unlimited High Definition Video Day Passes, Voicemail to Text, NameID, unlimited Gogo in-flight internet passes on capable domestic flights and up to two times faster speeds when traveling abroad in 140+ countries and destinations. On T-Mobile ONE Plus International, customers receive the benefits of T-Mobile ONE Plus as well as free and reduced calling from the U.S. to foreign countries and unlimited high-speed 4G LTE mobile hotspot data in the U.S., Mexico and Canada.
- In January 2017, we introduced the latest in our Un-carrier initiatives, Un-carrier Next, where monthly wireless service fees and taxes are included in the advertised monthly recurring charge for T-Mobile ONE. We also unveiled Kickback on T-Mobile ONE, where participating customers who use 2 GB or less of data in a month, will get an up to a \$10 credit on their next month's bill per qualifying line. In addition, we introduced the Un-contract for T-Mobile ONE with the first-ever price guarantee on an unlimited 4G LTE plan, which allows T-Mobile ONE customers to keep their price for service until they decide to change it.
- Simple Choice plans, which were launched in 2013 as part of phase 1.0 of our Un-carrier initiatives, eliminated annual service contracts and simplified the lineup of consumer rate plans to one affordable plan for unlimited voice and messaging services with the option to add data services. On January 25, 2017, we streamlined our Simple Choice plan offerings to new customers into our T-Mobile ONE plan.

Depending on their credit profile, customers are qualified either for postpaid or prepaid service.

Our device options for customers on T-Mobile ONE, and previously on Simple Choice plans, include:

- Depending on their credit profile, qualifying customers who purchase a device from us have the option of financing all or a portion of the purchase price at the time of sale over an installment period of up to 24 months using our Equipment Installment Plan ("EIP").
- In addition, qualifying customers who finance their initial device with an EIP can enroll in our JUMP!<sup>®</sup> program ("JUMP!") to later upgrade their device. Upon a qualifying JUMP! upgrade, the customer's remaining EIP balance is settled provided they trade-in their used device at the time of upgrade in good working condition and purchase a new device from us on a new EIP.
- In 2015, we introduced JUMP! On Demand. With JUMP! On Demand, a low monthly payment covers the cost of leasing a new device and gives qualified customers the freedom to exchange it for a new device up to three times in 12 months for no extra fee. Upon device upgrade or at lease end, customers must return their device in good working condition or purchase their device.

## **Network Transformation Update**

We continue to increase the depth, breadth and functionality of the nation's densest LTE network by adding new spectrum to increase coverage, and re-farming existing spectrum and implementing new technology to augment capacity. Collectively, these network advancements help provide improved network performance and reliability for our customers.

## *Spectrum Growth*

We provide mobile communication services utilizing mid-band spectrum licenses, such as Advanced Wireless Services ("AWS") and Personal Communications Service ("PCS"), and low-band spectrum licenses utilizing our 700 MHz A-Block spectrum.

- We owned or had agreements to own an average of 86 MHz of spectrum across the top 25 markets in the U.S. as of December 31, 2016, comprised of an average of 12 MHz in the 700 MHz band, 30 MHz in the 1900 MHz PCS band and 44 MHz in the AWS band. This is compared to an average of 85 MHz of spectrum across the top 25 markets in the U.S. as of December 31, 2015.



Table of Contents

- Over the last year, we have entered into and closed on various agreements for the acquisition and exchange of 700 MHz A-Block, AWS and PCS spectrum licenses. See Note 5 – Goodwill, Spectrum Licenses and Other Intangible Assets of the Notes to the Consolidated Financial Statements.
- In addition, we intend to opportunistically acquire spectrum licenses in private party transactions and future Federal Communications Commissions (“FCC”) spectrum license auctions, including the broadcast incentive auction of low-band 600 MHz spectrum licenses that is currently in-progress.
- We have continued to build out our network to concentrate our cell sites where our customers need data most. We had approximately 66,000 cell sites, including macro sites and distributed antenna system network nodes as of December 31, 2016, compared to approximately 64,000 cell sites as of December 31, 2015.
- In 2015, we completed the shutdown of the MetroPCS Code Division Multiple Access (“CDMA”) network. The migration of customers from the MetroPCS CDMA network onto T-Mobile’s LTE and Evolved High Speed Packet Access Plus network provides faster network performance for MetroPCS customers with compatible handsets.

*Network Coverage Growth*

- We continue to expand our coverage breadth and currently provide 4G LTE coverage to 314 million people, up from zero 4G LTE coverage four years ago. We are targeting to provide 320 million people with 4G LTE coverage by year-end 2017.
- We own 700 MHz A-Block spectrum covering 272 million people or approximately 84% of the U.S. population. The spectrum covers all of the top 10 market areas and 29 of the top 30 market areas in the U.S.
- We have deployed our 700 MHz A-Block spectrum in over 500 market areas covering more than 252 million people under the name “Extended Range LTE.” We expect to continue to aggressively roll-out new 700 MHz market areas in 2017 including Chicago, Eastern Montana, and substantially all of the remaining population in 700 MHz licensed areas.

*Network Capacity Growth*

We continue to expand our capacity through the re-farming of existing spectrum and implementation of new technologies including Voice over LTE (“VoLTE”), Carrier Aggregation, 4x4 MIMO, and 256 Quadrature Amplitude Modulation (“QAM”).

- At the end of the fourth quarter of 2016, approximately 70% of spectrum was being used for 4G LTE compared to 52% at the end of the fourth quarter of 2015. We expect to continue to re-farm spectrum currently committed to 2G and 3G technologies.
- Re-farmed spectrum enables us to continue expanding Wideband LTE, which currently covers 232 million people. Wideband LTE refers to markets that have bandwidth of at least 15+15 MHz dedicated to 4G LTE.
- VoLTE currently comprises approximately 67% of total voice calls compared to 39% in December 2015. Moving voice traffic to VoLTE frees up spectrum and allows for the transition of spectrum currently used for 2G and 3G to 4G LTE. We are leading the U.S. wireless industry in terms of VoLTE migration.
- Carrier aggregation is live for our customers in 674 cities. This advanced technology delivers superior speed and performance by bonding two or three discrete spectrum channels together.
- 4x4 MIMO is currently available in more than 300 cities. This technology effectively delivers twice the speed, and incremental network capacity, to customers by doubling the number of data paths between the cell site and a customer's device.
- We have rolled out 256 QAM, which increases the number of bits delivered per transmission to enable faster speed.
- Innovative programs like Binge On and T-Mobile ONE also create capacity by optimizing video for mobile viewing. These programs deliver material capacity benefits to both customers and our network. Since the launch of Binge On, our customers have watched more than 4 billion hours of optimized video.

*Network Speed Leadership*

We continue to have the fastest nationwide 4G LTE network in the U.S. based on both download and upload speeds from millions of user-generated tests. This is the twelfth consecutive quarter that we have led the industry in both download and upload speeds.

## Table of Contents

### **Distribution**

We had approximately 52,000 total points of distribution, including approximately 13,000 T-Mobile and MetroPCS branded locations and 39,000 third-party and national retailer locations, as well as distribution through our websites, as of December 31, 2016. Our distribution density in major metropolitan areas provides customers with the convenience of having retail and service locations close to where they live and work.

### **Competition**

The wireless telecommunications industry is highly competitive. We are the third largest provider of postpaid service plans and the largest provider of prepaid service plans in the U.S. as measured by customers. Our competitors include other national carriers, such as AT&T Inc. ("AT&T"), Verizon Communications, Inc. ("Verizon") and Sprint Corporation. AT&T and Verizon are significantly larger than us and may enjoy greater resources and scale advantages as compared to us. In addition, our competitors include numerous smaller regional carriers, existing MVNOs, such as TracFone Wireless, Inc., and future MVNOs, such as Comcast Corporation and Charter Communications, Inc., many of which offer or plan to offer no-contract, prepaid service plans. Competitors also include providers who offer similar communication services, such as voice and messaging, using alternative technologies or services. Competitive factors within the wireless telecommunications industry include pricing, market saturation, service and product offerings, customer experience, network investment and quality, development and deployment of technologies, availability of additional spectrum licenses and regulatory changes. Some competitors have shown a willingness to use aggressive pricing as a source of differentiation. Other competitors have sought to add ancillary services, like mobile video, to enhance their offerings. Taken together, the competitive factors we face continue to put pressure on margins as companies compete to retain the current customer base and continue to add new customers.

### **Employees**

As of December 31, 2016, we employed approximately 50,000 full-time and part-time employees, including network, retail, administrative and customer support functions.

### **Regulation**

The FCC regulates many key aspects of our business, including licensing, construction, the operation and use of our network, modifications of our network, control and ownership of our licenses and authorizations, the sale, transfer and acquisition of certain licenses, domestic roaming arrangements and interconnection agreements, pursuant to its authority under the Communications Act of 1934, as amended ("Communications Act"). The FCC has a number of complex requirements and proceedings that affect our operations and that could increase our costs or diminish our revenues. For example, the FCC has rules regarding provision of 911 and E-911 services, porting telephone numbers, interconnection, roaming, internet openness or net neutrality, disabilities access, privacy and cybersecurity, consumer protection, and the universal service and Lifeline programs. Many of these and other issues are being considered in ongoing proceedings, and we cannot predict whether or how such actions will affect our business, financial condition or results of operations. Our ability to provide services and generate revenues could be harmed by adverse regulatory action or changes to existing laws and regulations. In addition, regulation of companies that offer competing services can impact our business indirectly.

Wireless communications providers must be licensed by the FCC to provide communications services at specified spectrum frequencies within specified geographic areas and must comply with the rules and policies governing the use of the spectrum as adopted by the FCC. The FCC issues each license for a fixed period of time, typically 10 years in the case of cellular, PCS and point-to-point microwave licenses. AWS licenses have an initial term of 15 years, with successive 10-year terms thereafter. While the FCC has generally renewed licenses given to operating companies like us, the FCC has authority to both revoke a license for cause and to deny a license renewal if a renewal is not in the public interest. Furthermore, we could be subject to fines, forfeitures and other penalties for failure to comply with FCC regulations, even if any such non-compliance was unintentional. In extreme cases, penalties can include revocation of our licenses. The loss of any licenses, or any related fines or forfeitures, could adversely affect our business, results of operations and financial condition.

Additionally, Congress' and the FCC's allocation of additional spectrum for broadband commercial mobile radio service ("CMRS"), which includes cellular, PCS and specialized mobile radio, could significantly increase competition. We cannot assess the impact that any developments that may occur in the U.S. economy or any future spectrum allocations by the FCC may have on license values. FCC spectrum auctions and other market developments may adversely affect the market value of our licenses in the future. A significant decline in the value of our licenses could adversely affect our financial condition and results of operations. In addition, the FCC periodically reviews its policies on how to evaluate carriers' spectrum holdings. A change in these policies could affect spectrum resources and competition among us and other carriers.



Table of Contents

Congress and the FCC have imposed limitations on foreign ownership of CMRS licensees that exceed 20% direct ownership or 25% indirect ownership. The FCC has ruled that higher levels of indirect foreign ownership, even up to 100%, are presumptively consistent with the public interest albeit subject to review. Consistent with that established policy, the FCC has issued a declaratory ruling authorizing up to 100% ownership of our company by Deutsche Telekom. This declaratory ruling, and our licenses, are conditioned on Deutsche Telekom's and the Company's compliance with a network security agreement with the Department of Justice, the Federal Bureau of Investigation and the Department of Homeland Security. Failure to comply with the terms of this agreement could result in fines, injunctions and other penalties, including potential revocation of our spectrum licenses.

While the Communications Act generally preempts state and local governments from regulating the entry of, or the rates charged by, wireless communication providers, certain state and local governments regulate other terms and conditions of wireless service, including billing, termination of service arrangements and the imposition of early termination fees, advertising, network outages, the use of devices while driving, zoning and land use. Additionally, the Federal Trade Commission ("FTC") and other federal agencies have asserted that they have jurisdiction over some consumer protection and elimination and prevention of anticompetitive business practices with respect to the provision of non-common carrier services. Further, the FCC and the Federal Aviation Administration regulate the siting, lighting and construction of transmitter towers and antennae. Tower siting and construction are also subject to state and local zoning, as well as federal statutes regarding environmental and historic preservation. The future costs to comply with all relevant regulations are to some extent unknown and changes to regulations, or the applicability of regulations, could result in higher operating and capital expenses, or reduced revenues in the future.

**Available Information**

Our Form 10-K and all other reports and amendments filed with or furnished to the SEC, are publicly available free of charge on the Investor Relations section of our website at investor.t-mobile.com or at www.sec.gov as soon as reasonably practicable after these materials are filed with or furnished to the SEC. Our corporate governance guidelines, code of business conduct, code of ethics for senior financial officers and charters for the audit, compensation, nominating and corporate governance and executive committees of our board of directors are also posted on the Investor Relations section of our website at investor.t-mobile.com. The information on our websites is not part of this or any other report we file with, or furnishes to, the SEC.

Investors and others should note that we announce material financial and operational information to our investors using our investor relations website, press releases, SEC filings and public conference calls and webcasts. We intend to also use the @TMobileIR Twitter account (<https://twitter.com/TMobileIR>) and the @JohnLegere Twitter (<https://twitter.com/JohnLegere>), Facebook and Periscope accounts, which Mr. Legere also uses as means for personal communications and observations, as means of disclosing information about the Company and its services and for complying with its disclosure obligations under Regulation FD. The information we post through these social media channels may be deemed material. Accordingly, investors should monitor these social media channels in addition to following the Company's press releases, SEC filings and public conference calls and webcasts. The social media channels that we intend to use as a means of disclosing the information described above may be updated from time to time as listed on the Company's investor relations website.

**Item 1A. Risk Factors**

In addition to the other information contained in this Form 10-K, the following risk factors should be considered carefully in evaluating T-Mobile. Our business, financial condition, liquidity, or operating results, as well as the price of our common stock and other securities, could be materially adversely affected by any of these risks.

***Risks Related to Our Business and the Wireless Industry***

**The scarcity and cost of additional wireless spectrum, and regulations relating to spectrum use, may adversely affect our business strategy and financial performance.**

We will need to acquire additional spectrum in order to continue our customer growth, expand and deepen our coverage, maintain our quality of service, meet increasing customer demands and deploy new technologies. We will be at a competitive disadvantage and possibly experience erosion in the quality of service in certain markets if we fail to gain access to necessary spectrum before reaching capacity. As a result, we are actively seeking to make additional investment in spectrum, which could be significant.

Table of Contents

The continued interest in, and acquisition of, spectrum by existing carriers and others may reduce our ability to acquire and/or raise the cost of acquiring spectrum in the secondary market or negatively impact our ability to gain access to spectrum through other means, including government auctions. We may need to enter into spectrum sharing or leasing arrangements, which are subject to certain risks and uncertainties and may involve significant expenditures. Although the FCC is conducting an auction for low band spectrum, in which we are participating, gaining access to that spectrum may take up to three years or more. Any material delay could adversely impact our ability to implement our plans and efforts to improve our network. In addition, our return on investment in spectrum depends on our ability to attract additional customers and to provide additional services and usage to existing customers. As a result, the return on any investment in spectrum that we make may not be as much as we anticipate or take longer than expected. Additionally, we may be unable to secure the spectrum we need in any auction we may elect to participate in or in the secondary market, on favorable terms or at all.

The FCC may impose conditions on the use of new wireless broadband mobile spectrum, including new restrictions or rules governing the use or access to current or future spectrum. This could increase pressure on capacity. Additional conditions that may be imposed by the FCC include heightened build-out requirements, limited renewal rights, clearing obligations, or open access or net neutrality requirements that may make it less attractive or less economical to acquire spectrum. In addition, rules may be established for future government spectrum auctions that may negatively impact our ability to obtain spectrum economically or in appropriate configurations or coverage areas.

If we cannot acquire needed spectrum from the government or otherwise, if competitors acquire spectrum that will allow them to provide services competitive with our services, or if we cannot deploy services over acquired spectrum on a timely basis without burdensome conditions, at reasonable cost, and while maintaining network quality levels, then our ability to attract and retain customers and our associated financial performance could be materially adversely affected.

**Competition, industry consolidation, and changes in the market for wireless services could negatively affect our ability to attract and retain customers and adversely affect our business, financial condition, and operating results.**

We have multiple wireless competitors, some of which have greater resources than us and compete for customers based principally on service/device offerings; price; network coverage, speed and quality; and customer service. We expect market saturation to continue to cause the wireless industry's customer growth rate to be moderate in comparison with historical growth rates or possibly negative, leading to ongoing competition for customers. Customer churn may increase as the wireless industry shifts away from service contracts. We also expect that our customers' appetite for data services will place increasing demands on our network capacity. This competition and our capacity will continue to put pressure on pricing and margins as companies compete for potential customers. Our ability to compete will depend on, among other things, continued absolute and relative improvement in network quality and customer services, effective marketing and selling of products and services, attractive pricing, and cost management, all of which will involve significant expenses.

Joint ventures, mergers, acquisitions and strategic alliances in the wireless sector have resulted in and are expected to result in larger competitors competing for a limited number of customers. The two largest national wireless communication providers currently serve a significant percentage of all wireless customers and hold significant spectrum and other resources. Our largest competitors may be able to enter into exclusive handset, device, or content arrangements, execute pervasive advertising and marketing campaigns, or otherwise improve their cost position relative to ours. In addition, refusal of our large competitors to provide critical access to resources and inputs, such as roaming services on reasonable terms, could improve their position within the wireless broadband mobile services industry.

We are also facing competition from other service providers as industry sectors converge, such as telecom services and content; satellite, wireless, and fiber; and other service providers. Companies like Comcast and AT&T/DirecTV (and AT&T's proposed acquisition of Time Warner) will have the scale and assets to aggressively compete in a converging industry. Verizon is also a significant competitor focusing on premium content offerings as well as acquisitions and proposed acquisitions like AOL and Yahoo to diversify outside of core wireless. Further, some of our competitors now provide content services in addition to voice and broadband services, and consumers are increasingly accessing video content from Internet-based providers and applications, all of which create increased competition in this area. These factors, together with the effects of the increasing aggregate penetration of wireless services in all metropolitan areas and the ability of our larger competitors to use resources to build out their networks and to quickly deploy advanced technologies, could make it more difficult for us to continue to attract and retain customers, and may adversely affect our competitive position and ability to grow, which would have a material adverse effect on our business, financial condition and operating results.

Table of Contents

**If we are unable to take advantage of technological developments on a timely basis, we may experience a decline in demand for our services or face challenges in implementing or evolving our business strategy.**

Significant technological changes continue to impact the communications industry. In general, these technological changes enhance communications and enable a broader array of companies to offer services competitive with ours. In order to grow and remain competitive with new and evolving technologies in our industry, we will need to adapt to future changes in technology, continually invest in our network, enhance our existing offerings, and introduce new offerings to address our current and potential customers' changing demands. Enhancing our network, such as deploying 5G, is subject to risk from equipment changes and migration of customers from existing spectrum bands and the potential inability to secure spectrum necessary to deploy advanced technologies. Adopting new and sophisticated technologies may result in implementation issues such as scheduling and supplier delays, unexpected or increased costs, technological constraints, regulatory permitting issues, customer dissatisfaction, and other issues that could cause delays in launching new technological capabilities, which in turn could result in significant costs or reduce the anticipated benefits of the upgrades. In general, the development of new services in the wireless telecommunications industry will require us to anticipate and respond to the continuously changing demands of our customers, which we may not be able to do accurately or timely. We could experience a material adverse effect on our business, operations, financial condition and operating results if our new services fail to retain or gain acceptance in the marketplace or if costs associated with these services are higher than anticipated.

**We could be harmed by data loss or other security breaches, whether directly or by way of third parties.**

Our business, like that of most retailers and wireless companies, involves the receipt, storage, and transmission of confidential information, including sensitive personal information and payment card information, confidential information about our employees and suppliers, and other sensitive information about our company, such as our business plans, transactions and intellectual property ("confidential information"). Unauthorized access may be difficult to anticipate, detect, or prevent, particularly given that the methods of unauthorized access constantly change and evolve. We may experience unauthorized access or distribution of confidential information by third parties or employees, errors or breaches by third party suppliers, or other breaches of security that compromise the integrity of confidential information, and such breaches can have a materially adverse effect on our business or damage our reputation.

In addition, cyber-attacks, such as denial of service and other malicious attacks, could disrupt our internal systems and applications, impair our ability to provide services to our customers, and have other adverse effects on our business and that of others who depend on our services. As a telecommunications carrier, we are considered a critical infrastructure provider and therefore may be more likely to be the target of such attacks. Such attacks against companies may be perpetrated by a variety of groups or persons, including those in jurisdictions where U.S. law enforcement is or has been unable to effectively address such attacks.

In addition, we provide confidential, proprietary and personal information to third-party service providers when it is necessary to pursue business objectives. We and our third-party service providers have been subject to unauthorized access to confidential information in the past, including a breach at one of our credit check providers in September 2015 in which a subset of records containing current and potential customer information was compromised by an external party.

Although we regularly review our procedures and safeguards to prevent unauthorized access to sensitive data and to defend against attacks seeking to disrupt our services, the ever-evolving threat landscape requires us to continually evaluate and adapt our systems and processes. We cannot assure you that the preventive actions we take will be adequate to repel a significant attack or prevent information security breaches or the misuses of data, unauthorized access by third parties or employees, or exploits against third-party supplier environments. If we are subject to such attacks or compromise, we may incur significant costs, be subject to regulatory investigations, sanctions and private litigation, experience disruptions to our operations or suffer damage to our reputation. Although the cyber-attacks that we and our third-party service providers have been subjected to in the past have not caused significant harm to our company, future cyber-attacks may materially adversely affect our business, financial condition, and operating results.

**System failures and business disruptions may allow unauthorized use of or interference with our network and other systems which could be materially adversely affect our reputation and financial condition.**

To be successful, we must provide our customers with reliable, trustworthy service and protect the communications, location, and personal information shared or generated by our customers. We rely upon both our systems and networks and the systems and networks of other providers and suppliers to provide and support our services and, in some cases, protect our customers' and our information. Failure of our or others' systems, networks, or infrastructure may prevent us from providing reliable service or may allow for the unauthorized use of or interference with our networks and other systems or for the compromise of

Table of Contents

customer information. Examples of these risks include:

- human error such as responding to deceptive communications or unintentionally executing malicious code;
- physical damage, power surges or outages, or equipment failure, including those as a result of severe weather, natural disasters, terrorist attacks, and acts of war;
- theft of customer and/or proprietary information offered for sale for competitive advantage or corporate extortion;
- unauthorized access to our IT and business systems or to our network and critical infrastructure and those of our suppliers and other providers;
- supplier failures or delays; and
- system failures or outages of our business systems or communications network.

Such events could cause us to lose customers, lose revenue, incur expenses, suffer reputational and goodwill damages, and subject us to litigation or governmental investigation. Remediation costs could include liability for information loss, repairing infrastructure and systems, and/or costs of incentives offered to customers. Our insurance may not cover, or be adequate to fully reimburse us for, costs and losses associated with such events.

**We are in the process of implementing a new billing system, which will support a portion of our subscribers, while maintaining our legacy billing system. Any unanticipated difficulties, disruption, or significant delays could have adverse operational, financial, and reputational effects on our business.**

We are currently implementing a new customer billing system, which involves a new third-party supported platform and utilization of a phased deployment approach. Post implementation, we plan to operate both the existing and new billing systems in parallel to aid in the transition to the new system until all phases of the conversion are complete.

The implementation may cause major system or business disruptions, or we may fail to implement the new billing system in a timely or effective manner. In addition, the third-party billing services supporting vendor may experience errors, cyber-attacks, or other operational disruptions that could negatively impact us and over which we may have limited control. Interruptions and/or failure of this new billing services system could disrupt our operations and impact our ability to provide or bill for our services, retain customers, attract new customers, or negatively impact overall customer experience. Any occurrence of the foregoing could cause material adverse effects on our operations and financial condition, material weaknesses in our internal control over financial reporting, and reputational damage.

**We rely on third parties to provide products or services for the operation of our business, and a failure or inability by such parties to provide these products or services could adversely affect our business, financial condition, and operating results.**

We depend heavily on suppliers, their subcontractors, and other third parties in order for us to efficiently operate our business. Our business is complex, and it is not unusual for multiple vendors located in multiple locations to help us to develop, maintain, and troubleshoot products and services, such as network components, software development services, and billing and customer service support. Our suppliers may provide services outside of the United States, which carries associated additional regulatory and legal obligations. We generally rely upon the suppliers to provide contractual assurances and accurate information regarding risks associated with their provision of products or services in accordance with our expectations and standards such as our supplier code of conduct and our third party-risk management standard, and they may fail to do so.

Generally, there are multiple sources for the types of products and services we purchase or use. However, we currently rely on a limited number of suppliers for billing services, voice and data communications transport services, network infrastructure, equipment, handsets, other devices, and payment processing services, among other products and services. Disruptions or failure of such suppliers to adequately perform could have a material adverse effect on our business, operations, and financial performance.

In the past, our suppliers, contractors and third-party retailers may not have always performed at the levels we expected or at the levels required by their contracts. Our business could be severely disrupted if key suppliers, contractors, service providers, or third-party retailers fail to comply with their contracts or become unable to continue the supply due to patent or other intellectual property infringement actions or other disruptions. Our business could also be disrupted if we experience delays or service degradation during any transition to a new outsourcing provider or other supplier or we were required to replace the supplied products or services with those from another source, especially if the replacement became necessary on short notice. Any such disruptions could have a material adverse effect on our business, financial condition, and operating results.



Table of Contents**Economic, political, and market conditions may adversely affect our business and financial performance, as well as our access to financing on favorable terms or at all.**

Our business and financial performance are sensitive to changes in general economic conditions, including interest rates, consumer credit conditions, consumer debt levels, consumer confidence, rates of inflation (or concerns about deflation), unemployment rates, economic growth, energy costs, and other macro-economic factors. Difficult, or worsening, general economic conditions could have a material adverse effect on our business, financial condition, and operating results.

Market volatility, political and economic uncertainty, and weak economic conditions may materially adversely affect our business and financial performance in a number of ways. Our services are available to a broad customer base, a significant segment of which may be more vulnerable to weak economic conditions. We may have greater difficulty in gaining new customers within this segment, and existing customers may be more likely to terminate service due to an inability to pay.

Weak economic conditions and credit conditions may also adversely impact our suppliers and dealers, some of which have filed for or may be considering bankruptcy, or may experience cash flow or liquidity problems, or are unable to obtain or refinance credit such that they may no longer be able to operate. Any of these could adversely impact our ability to distribute, market, or sell our products and services.

In addition, instability in the global financial markets could lead to periodic volatility in the credit, equity, and fixed income markets. This volatility could limit our access to the credit markets, leading to higher borrowing costs or, in some cases, the inability to obtain financing on terms that are acceptable to us or at all.

**The agreements governing our indebtedness and other financing arrangements include restrictive covenants that limit our operating flexibility.**

The agreements governing our indebtedness impose significant operating and financial restrictions on us. These restrictions, subject in certain cases to customary baskets, exceptions, and incurrence-based ratio tests, may limit our or our subsidiaries' ability to engage in some transactions, including the following:

- incurring additional indebtedness and issuing preferred stock;
- paying dividends, redeeming capital stock, or making other restricted payments or investments;
- selling or buying assets, properties, or licenses, including participating in future FCC auctions of spectrum or private sales of spectrum;
- developing assets, properties, or licenses that we have or in the future may procure;
- creating liens on assets;
- engaging in mergers, acquisitions, business combinations, or other transactions;
- entering into transactions with affiliates; and
- placing restrictions on the ability of subsidiaries to pay dividends or make other payments.

These restrictions could limit our ability to react to changes in our operating environment or the economy. Any future indebtedness that we incur may contain similar or more restrictive covenants. Any failure to comply with the restrictions of our debt agreements may result in an event of default under these agreements, which in turn may result in defaults or acceleration of obligations under these agreements and other agreements, giving our lenders the right to terminate any commitments they had made to provide us with further funds and to require us to repay all amounts then outstanding. Any of these events would have a material adverse effect on our business, financial condition, and operating results.

**Our significant indebtedness could adversely affect our business, financial condition and operating results.**

Our ability to make payments on our debt, to repay our existing indebtedness when due, and to fund our capital intensive business and operations, and significant planned capital expenditures will depend on our ability to generate cash in the future, which is in turn subject to the operational risks described elsewhere in this report. Our debt service obligations could have material adverse effects on our business, financial condition, and operating results, including by:

- limiting our flexibility in planning for, or reacting to, changes in our business or the communications industry or pursuing

growth opportunities;

- reducing the amount of cash available for other operational or strategic needs; and

Table of Contents

- placing us at a competitive disadvantage to competitors who are less leveraged than we are.

Some of our debt also has a floating rate of interest linked to various indices. If the resets or the change in indices result in interest rate increases, debt service requirements will increase, which could adversely affect our cash flow and operating results. While we have and may enter into agreements limiting our exposure to higher interest rates in the future, any such agreements may not offer complete protection from this risk, and any portion not subject to such agreements would have full exposure to higher interest rates. Any of these risks could have a material adverse effect on our business, financial condition and operating results.

**Failure to maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act could result in a loss of investor confidence regarding our financial statements or may have a material adverse effect on our business.**

Under Section 404 of the Sarbanes-Oxley Act of 2002, we along with our independently registered public accounting firm are required to report on the effectiveness of our internal controls over financial reporting. We rely heavily on IT systems as an important part of our internal controls in order to operate, transact, and otherwise manage our business, as well as provide effective and timely reporting of our financial results. Failure to design and maintain effective internal controls, including those over our IT systems, could constitute a material weakness that could result in inaccurate financial statements, inaccurate disclosures, or failure to prevent fraud. If we or our independent registered public accounting firm were unable to conclude that we have effective internal controls, investor confidence regarding our financial statements and our business could be materially adversely affected.

**Our financial performance will be impaired if we experience high fraud rates related to device financing, credit cards, dealers, or subscriptions.**

Our operating costs could increase substantially as a result of fraud, including device financing, customer credit card, subscription, or dealer fraud. If our fraud detection strategies and processes are not successful in detecting and controlling fraud, whether directly or by way of the systems, processes, and operations of third parties such as national retailers, dealers, and others, the resulting loss of revenue or increased expenses could have a materially adverse impact on our financial condition and operating results.

**We rely on highly-skilled personnel throughout all levels of our business. Our business could be harmed if we are unable to retain or motivate key personnel, hire qualified personnel or maintain our corporate culture.**

The market for highly skilled workers and leaders in our industry is extremely competitive. We believe that our future success depends in substantial part on our ability to recruit, hire, motivate, develop, and retain talented and highly-skilled personnel for all areas of our organization. Doing so may be difficult due to many factors, including fluctuations in economic and industry conditions, changes to U.S. immigration policy, competitors' hiring practices, employee tolerance for the significant amount of change within and demands on our company and our industry, and the effectiveness of our compensation programs. Our continued ability to compete effectively depends on our ability to retain and motivate our existing employees and to attract new employees. If we do not succeed in retaining and motivating our existing key employees and attracting new key personnel, we may not be able to meet our business plan and, as a result, our revenue growth and profitability may be materially adversely affected.

**Any acquisition, investment, or merger may subject us to significant risks, any of which may harm our business.**

We may pursue acquisitions of, investments in or mergers with businesses, technologies, services and/or products that complement or expand our business. Some of these potential transactions could be significant relative to the size of our business and operations. Any such transaction would involve a number of risks and could present financial, managerial and operational challenges, including:

- diversion of management attention from running our existing business;
- increased costs to integrate the networks, spectrum, technology, personnel, customer base and business practices of the business involved in any such transaction with our business;
- difficulties in effectively integrating the financial and operational reporting systems of the business involved in any such transaction into (or supplanting such systems with) our financial and operational reporting infrastructure and internal control framework in an effective and timely manner;
- potential exposure to material liabilities not discovered in the due diligence process or as a result of any litigation arising in connection with any such transaction;
- significant transaction expenses in connection with any such transaction, whether consummated or not;

Table of Contents

- risks related to our ability to obtain any required regulatory approvals necessary to consummate any such transaction;
- acquisition financing may not be available on reasonable terms or at all and any such financing could significantly increase our outstanding indebtedness or otherwise affect our capital structure or credit ratings; and
- any business, technology, service, or product involved in any such transaction may significantly under-perform relative to our expectations, and we may not achieve the benefits we expect from our transaction, which could, among other things, also result in a write-down of goodwill and other intangible assets associated with such transaction.

For any or all of these reasons, our pursuit of an acquisition, investment, or merger may have a material adverse effect on our business, financial condition, and operating results.

***Risks related to Legal and Regulatory Matters*****Changes in regulations or in the regulatory framework under which we operate could adversely affect our business prospects or operating results.**

The FCC regulates the licensing, construction, modification, operation, ownership, sale, and interconnection of wireless communications systems, as do some state and local regulatory agencies. In particular, the FCC imposes significant regulation on licensees of wireless spectrum with respect to how radio spectrum is used by licensees, the nature of the services that licensees may offer and how the services may be offered, and resolution of issues of interference between spectrum bands. Additionally, the FTC and other federal agencies have asserted that they have jurisdiction over some consumer protection, and elimination and prevention of anticompetitive business practices with respect to the provision of wireless products and services. We are subject to regulatory oversight by various federal, state and local agencies, as well as judicial review and actions, on issues related to the wireless industry that include, but are not limited to: roaming, spectrum allocation and licensing, facilities siting, pole attachments, intercarrier compensation, Universal Service Fund ("USF"), net neutrality, special access, 911 services, consumer protection, consumer privacy, and cybersecurity. We are also subject to regulations in connection with other aspects of our business, including handset financing and insurance activities.

We cannot assure you that the FCC or any other federal, state or local agencies will not adopt regulations or take other enforcement or other actions that would adversely affect our business, impose new costs, or require changes in current or planned operations. For example, in June 2015, the FCC's new net neutrality rules became effective, with the exception of enhanced transparency requirements, a portion of which became effective January 2017. In 2016, the FCC also adopted a new broadband privacy regime that applies to our operations. Both sets of rules potentially subject some of our initiatives and practices to more burdensome requirements and heightened scrutiny by federal and state regulators, the public, edge providers, and private litigants regarding whether such initiatives or practices are compliant.

In addition, states are increasingly focused on the quality of service and support that wireless communication providers provide to their customers and several states have proposed or enacted new and potentially burdensome regulations in this area. We also face potential investigations by, and inquiries from or actions by state Public Utility Commissions. We also cannot assure you that Congress will not amend the Communications Act, from which the FCC obtains its authority and which serves to limit state authority, or enact other legislation in a manner that could be adverse to our business.

Failure to comply with applicable regulations could have a material adverse effect on our business, financial condition and operating results. We could be subject to fines, forfeitures, and other penalties (including, in extreme cases, revocation of our spectrum licenses) for failure to comply with FCC or other governmental regulations, even if any such non-compliance was unintentional. The loss of any licenses, or any related fines or forfeitures, could adversely affect our business, financial condition, and operating results.

**Unfavorable outcomes of legal proceedings may adversely affect our business and financial condition.**

We are regularly involved in a number of legal proceedings before various state and federal courts, the FCC, the FTC, other federal agencies, and state and local regulatory agencies, including state attorneys general. Such legal proceedings can be complex, costly, and highly disruptive to business operations by diverting the attention and energies of management and other key personnel. The assessment of the outcome of legal proceedings, including our potential liability, if any, is a highly subjective process that requires judgments about future events that are not within our control. The amounts ultimately received or paid upon settlement or pursuant to final judgment, order or decree may differ materially from amounts accrued in our financial statements. In addition, litigation or similar proceedings could impose restraints on our current or future manner of doing business. Such potential outcomes including judgments, awards, settlements or orders could have a material adverse effect on our business, financial condition, operating results or ability to do business.



Table of Contents**We offer highly regulated financial services products. These products expose us to a wide variety of state and federal regulations.**

The financing of devices, including through our EIP and JUMP! On Demand programs, has expanded our regulatory compliance obligations. If we fail to remain compliant with any of these regulations, then we face the risk of:

- increased consumer complaints and potential examinations or enforcement actions by federal and state regulatory agencies, including but not limited to the Consumer Financial Protection Board, the FCC and the FTC;
- violation of financial services and consumer protections regulations may result in regulatory fines, penalties, enforcement actions, civil litigation, and/or class action lawsuits.

Failure to comply with applicable regulations and the realization of any of these risks could have a material adverse effect on our business, financial condition, and operating results.

**We may not be able to adequately protect our intellectual property rights or may be accused of infringing intellectual property rights of third parties.**

We rely on a combination of patent, service mark, trademark, and trade secret laws and contractual restrictions to establish and protect our proprietary rights, all of which offer only limited protection. The steps we have taken to protect our intellectual property may not prevent the misappropriation of our proprietary rights. We may not have the ability in certain jurisdictions to adequately protect intellectual property rights. Moreover, others may independently develop processes and technologies that are competitive to ours. Also, we may not be able to discover or determine the extent of any unauthorized use of our proprietary rights. Unauthorized use of our intellectual property rights may increase the cost of protecting these rights or reduce our revenues. We cannot be sure that any legal actions against such infringers will be successful, even when our rights have been infringed. We cannot assure you that our pending or future patent applications will be granted or enforceable, or that the rights granted under any patent that may be issued will provide us with any competitive advantages. In addition, we cannot assure you that any trademark or service mark registrations will be issued with respect to pending or future applications or will provide adequate protection of our brands. We do not have insurance coverage for intellectual property losses, and as such, a charge for an anticipated settlement or an adverse ruling awarding damages represents unplanned loss events. Any of these factors could have material adverse effects on our business, financial condition, and operating results.

Third parties may claim we infringe their intellectual property rights. We are a defendant in numerous intellectual property lawsuits, including patent infringement lawsuits, which exposes us to the risk of adverse financial impact either by way of significant settlement amounts or damage awards. As we adopt new technologies and new business systems, and provide customers with new products and/or services, we may face additional infringement claims. These claims could require us to cease certain activities or to cease selling relevant products and services. These claims can be time-consuming and costly to defend, and divert management resources, and expose us to significant damages awards or settlements, any or all of which could have a material adverse effect on our operations and financial condition. In addition to litigation directly involving our company, our vendors and suppliers can be threatened with patent litigation and/or subjected to the threat of disruption or blockage of sale, use, or importation of products, posing the risk of supply chain interruption to particular products and associated services exposing us to material adverse operational and financial impacts.

**Our business may be impacted by new or changing tax laws or regulations and actions by federal, state, and/or local agencies, or how judicial authorities apply tax laws.**

In connection with the products and services we sell, we calculate, collect, and remit various federal, state, and local taxes, surcharges and regulatory fees ("tax" or "taxes") to numerous federal, state and local governmental authorities, including federal USF contributions and common carrier regulatory fees. In addition, we incur and pay state and local taxes and fees on purchases of goods and services used in our business.

Tax laws are dynamic and subject to change as new laws are passed and new interpretations of the law are issued or applied. In many cases, the application of tax laws are uncertain and subject to differing interpretations, especially when evaluated against new technologies and telecommunications services, such as broadband internet access and cloud related services. Changes in tax laws could impact revenue on tax inclusive plans.

In the event that we have incorrectly described, disclosed, calculated, assessed, or remitted amounts that were due to governmental authorities, we could be subject to additional taxes, fines, penalties, or other adverse actions, which could materially impact our operations or financial condition. In the event that federal, state, and/or local municipalities were to



## Table of Contents

significantly increase taxes on our network, operations, or services, or seek to impose new taxes, it could have a material adverse effect on our margins and financial and operational results.

### **Our wireless licenses are subject to renewal and may be revoked in the event that we violate applicable laws.**

Our existing wireless licenses are subject to renewal upon the expiration of the 10-year or 15-year period for which they are granted. Historically, the FCC has approved our license renewal applications. However, the Communications Act provides that licenses may be revoked for cause and license renewal applications denied if the FCC determines that a renewal would not serve the public interest. In addition, our licenses are subject to our compliance with the terms set forth in the agreement pertaining to national security among Deutsche Telekom, the Federal Bureau of Investigation, the Department of Justice, the Department of Homeland Security and the Company. The failure of Deutsche Telekom or the Company to comply with the terms of this agreement could result in fines, injunctions and other penalties, including potential revocation or non-renewal of our spectrum licenses. If we fail to timely file to renew any wireless license or fail to meet any regulatory requirements for renewal, including construction and substantial service requirements, we could be denied a license renewal. Many of our wireless licenses are subject to interim or final construction requirements and there is no guarantee that the FCC will find our construction, or the construction of prior licensees, sufficient to meet the build-out or renewal requirements. The FCC has pending a rulemaking proceeding to reevaluate, among other things, its wireless license renewal showings and standards and may in this or other proceedings promulgate changes or additional substantial requirements or conditions to its renewal rules, including revising license build out requirements. Accordingly, we cannot assure you that the FCC will renew our wireless licenses upon their expiration. If any of our wireless licenses were to be revoked or not renewed upon expiration, we would not be permitted to provide services under that license, which could have a material adverse effect on our business, financial condition, and operating results.

### **Our business could be adversely affected by findings of product liability for health/safety risks from wireless devices and transmission equipment, as well as by changes to regulations/radio frequency emission standards.**

We do not manufacture the devices or other equipment that we sell, and we depend on our suppliers to provide defect-free and safe equipment. Suppliers are required by applicable law to manufacture their devices to meet certain governmentally imposed safety criteria. However, even if the devices we sell meet the regulatory safety criteria, we could be held liable with the equipment manufacturers and suppliers for any harm caused by products we sell if such products are later found to have design or manufacturing defects. We generally seek to enter into indemnification agreements with the manufacturers who supply us with devices to protect us from losses associated with product liability, but we cannot guarantee that we will be fully protected against all losses associated with a product that is found to be defective.

Allegations have been made that the use of wireless handsets and wireless transmission equipment, such as cell towers, may be linked to various health concerns, including cancer and brain tumors. Lawsuits have been filed against manufacturers and carriers in the industry claiming damages for alleged health problems arising from the use of wireless handsets. In addition, the FCC has from time to time gathered data regarding wireless handset emissions and its assessment of this issue may evolve based on its findings. The media has also reported incidents of handset battery malfunction, including reports of batteries that have overheated. These allegations may lead to changes in regulatory standards. There have also been other allegations regarding wireless technology, including allegations that wireless handset emissions may interfere with various electronic medical devices (including hearing aids and pacemakers), airbags and anti-lock brakes. Defects in the products of our suppliers, such the recent recalls by a handset Original Equipment Manufacturer ("OEM") on one of its smartphone devices, could have an adverse impact on our operating results.

Additionally, there are safety risks associated with the use of wireless devices while operating vehicles or equipment. Concerns over any of these risks and the effect of any legislation, rules or regulations that have been and may be adopted in response to these risks could limit our ability to sell our wireless services.

### ***Related to Ownership of our Common Stock***

#### **We are controlled by Deutsche Telekom, whose interests may differ from the interests of our other stockholders.**

Deutsche Telekom beneficially owns and possesses majority voting power of the fully diluted shares of our common stock.

Through its control of the voting power of our common stock and the rights granted to Deutsche Telekom in our certificate of incorporation and the Stockholder's Agreement, Deutsche Telekom controls the election of our directors and all other matters requiring the approval of our stockholders. By virtue of Deutsche Telekom's voting control, we are a "controlled company," as defined in the NASDAQ listing rules, and are not subject to NASDAQ requirements that would otherwise require us to have a



Table of Contents

majority of independent directors, a nominating committee composed solely of independent directors or a compensation committee composed solely of independent directors. Accordingly, our stockholders will not be afforded the same protections generally as stockholders of other NASDAQ-listed companies with respect to corporate governance for so long as we rely on these exemptions from the corporate governance requirements.

In addition, our certificate of incorporation and the Stockholder's Agreement restrict us from taking certain actions without Deutsche Telekom's prior written consent as long as Deutsche Telekom beneficially owns 30% or more of the outstanding shares of our common stock, including:

- the incurrence of debt (excluding certain permitted debt) if our consolidated ratio of debt to cash flow for the most recently ended four full fiscal quarters for which financial statements are available would exceed 5.25 to 1.0 on a pro forma basis;
- the acquisition of any business, debt or equity interests, operations or assets of any person for consideration in excess of \$1 billion;
- the sale of any of our or our subsidiaries' divisions, businesses, operations or equity interests for consideration in excess of \$1 billion;
- any change in the size of our board of directors;
- the issuances of equity securities in excess of 10% of our outstanding shares or to repurchase debt held by Deutsche Telekom;
- the repurchase or redemption of equity securities or the declaration of extraordinary or in-kind dividends or distributions other than on a pro rata basis; or
- the termination or hiring of our chief executive officer.

These restrictions could prevent us from taking actions that our board of directors may otherwise determine are in the best interests of the Company and our stockholders or that may be in the best interests of our other stockholders.

Deutsche Telekom effectively has control over all matters submitted to our stockholders for approval, including the election or removal of directors, changes to our certificate of incorporation, a sale or merger of our company and other transactions requiring stockholder approval under Delaware law. Deutsche Telekom's controlling interest may have the effect of making it more difficult for a third party to acquire, or discouraging a third party from seeking to acquire, the Company. Deutsche Telekom may have strategic, financial, or other interests different from our other stockholders, including as the holder of a substantial amount of our indebtedness and as the counter-party in a number of commercial arrangements, and may make decisions adverse to the interests of our other stakeholders.

**Future sales or issuances of our common stock, including sales by Deutsche Telekom, could have a negative impact on our stock price.**

We cannot predict the effect, if any, that market sales of shares or the availability of shares of our common stock will have on the prevailing trading price of our common stock from time to time. Sales of a substantial number of shares of our common stock could cause our stock price to decline and could result in dilution of your shares.

We and Deutsche Telekom are parties to the Stockholder's Agreement pursuant to which Deutsche Telekom is free to transfer its shares in public sales without notice, as long as such transactions would not result in the transferee owning 30% or more of the outstanding shares of our common stock. If a transfer would exceed the 30% threshold, it is prohibited unless the transferee makes a binding offer to purchase all of the other outstanding shares on the same price and terms. The Stockholder's Agreement does not otherwise impose any other restrictions on the sales of common stock by Deutsche Telekom. Moreover, we have filed a shelf registration statement with respect to the common stock and certain debt securities held by Deutsche Telekom, which would facilitate the resale by Deutsche Telekom of all or any portion of the shares of our common stock it holds. The sale of shares of our common stock by Deutsche Telekom (other than in transactions involving the purchase of all of our outstanding shares) could significantly increase the number of shares available in the market, which could cause a decrease in our stock price. In addition, even if Deutsche Telekom does not sell a large number of its shares into the market, its right to transfer a large number of shares into the market may depress our stock price.

In addition, we have reserved up to 38.684 million shares of common stock for issuance upon conversion of our preferred stock, subject to certain anti-dilution adjustments. The dividends on the preferred stock may also be paid in cash or, subject to certain limitations, shares of common stock or any combination of cash and shares of common stock. The issuance of additional shares of common stock upon conversion of, or in connection with the payment of dividends upon, the mandatory

Table of Contents

convertible preferred stock may depress our stock price.

**Our stock price may be volatile, and may fluctuate based upon factors that have little or nothing to do with our business, financial condition and operating results.**

The trading prices of the securities of communications companies historically have been highly volatile, and the trading price of our common stock may be subject to wide fluctuations. Our stock price may fluctuate in reaction to a number of events and factors that may include, among other things:

- our or our competitors' actual or anticipated operating and financial results; introduction of new products and services by us or our competitors or changes in service plans or pricing by us or our competitors;
- analyst projections, predictions and forecasts, analyst target prices for our securities and changes in, or our failure to meet, securities analysts' expectations;
- transaction in our common stock by major investors;
- Deutsche Telekom's financial performance, results of operation, or actions implied or taken by Deutsche Telekom;
- entry of new competitors into our markets or perceptions of increased price competition, including a price war;
- our performance, including subscriber growth, and our financial and operational metric performance;
- market perceptions relating to our services, network, handsets, and deployment of our LTE platform and our access to iconic handsets, services, applications, or content;
- market perceptions of the wireless communications industry and valuation models for us and the industry;
- conditions or trends in the Internet and the industry sectors we operate in;
- changes in our credit rating or future prospects;
- changes in interest rates;
- changes in our capital structure, including issuance of additional debt or equity to the public;
- the availability or perceived availability of additional capital in general and our access to such capital;
- actual or anticipated consolidation, or other strategic mergers or acquisition activities involving us or our competitors, or other participants in related or adjacent industries, or market speculations regarding such activities;
- disruptions of our operations or service providers or other vendors necessary to our network operations;
- the general state of the U.S. and world politics and economies, including changes in interest rates; and
- availability of additional spectrum, whether by the announcement, commencement, bidding and closing of auctions for new spectrum or the acquisition of companies that own spectrum, and the extent to which we or our competitors succeed in acquiring additional spectrum.

In addition, the stock market has been volatile in the recent past and has experienced significant price and volume fluctuations, which may continue for the foreseeable future. This volatility has had a significant impact on the trading price of securities issued by many companies, including companies in the communications industry. These changes frequently occur irrespective of the operating performance of the affected companies. Hence, the trading price of our common stock could fluctuate based upon factors that have little or nothing to do with our business, financial condition and operating results.

**We have never paid or declared any cash dividends on our common stock, and we do not intend to declare or pay any cash dividends on our common stock in the foreseeable future.**

We have never paid or declared any cash dividends on our common stock, and we do not intend to declare or pay any cash dividends on our common stock in the foreseeable future. Our credit facilities and the indentures and supplemental indentures governing our long-term debt to affiliates and third parties contain covenants that, among other things, restrict our ability to declare or pay dividends on our common stock. In addition, no dividend may be declared or paid on our common stock, other than dividends payable solely in Shares of our common stock, unless all accrued dividends for all completed dividend periods have been declared and paid on our preferred stock. Other than to pay dividends on our preferred stock, we currently intend to retain future earnings, if any, to invest in our business.

**Our stockholder rights plan could prevent a change in control of our Company in instances in which some stockholders may believe a change in control is in their best interests.**

We have a stockholder rights plan ("Rights Plan") in effect that will expire in March 2017, unless renewed. The Rights Plan will cause substantial dilution to a person or group that attempts to acquire our company on terms that our board of directors

Table of Contents

does not believe are in our and our stockholders' best interest. The Rights Plan is intended to protect stockholders in the event of an unfair or coercive offer to acquire the Company and to provide our board of directors with adequate time to evaluate unsolicited offers. The Rights Plan may prevent or make takeovers or unsolicited corporate transactions with respect to our company more difficult, even if stockholders may consider such transactions favorable, possibly including transactions in which stockholders might otherwise receive a premium for their shares.

**Item 1B. Unresolved Staff Comments**

None.

**Item 2. Properties**

As of December 31, 2016, our significant properties used in connection with switching centers, data centers, call centers and warehouses were as follows:

	Approximate Number	Approximate Size in Square Feet
Switching centers	57	1,400,000
Data centers	8	600,000
Call center	16	1,300,000
Warehouses	16	500,000

As of December 31, 2016, we leased approximately 60,000 cell sites.

As of December 31, 2016, we leased approximately 2,000 T-Mobile and MetroPCS retail locations, including stores and kiosks ranging in size from approximately 100 square feet to 17,000 square feet.

We currently lease office space totaling approximately 950,000 square feet for our corporate headquarters in Bellevue, Washington. We use these offices for engineering and administrative purposes. We also lease space throughout the U.S., totaling approximately 1,200,000 square feet as of December 31, 2016, for use by our regional offices primarily for administrative, engineering and sales purposes.

**Item 3. Legal Proceedings**

See Note 12 – Commitments and Contingencies of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for information regarding certain legal proceedings in which we are involved.

**Item 4. Mine Safety Disclosures**

None.

**PART II.****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities****Market Information**

Our common stock is traded on the NASDAQ Global Select Market of The NASDAQ Stock Market LLC ("NASDAQ") under the symbol "TMUS." As of December 31, 2016, there were 309 registered stockholders of record of our common stock, but we estimate the total number of stockholders to be much higher as a number of our shares are held by brokers or dealers for their customers in street name.

Table of Contents

The high and low common stock sales prices per share were as follows:

	High		Low
<b>Year Ended December 31, 2016</b>			
First Quarter	\$ 41.23	\$	33.23
Second Quarter	44.13		37.93
Third Quarter	48.11		42.71
Fourth Quarter	59.19		44.91
<b>Year Ended December 31, 2015</b>			
First Quarter	\$ 33.48	\$	26.46
Second Quarter	40.77		31.19
Third Quarter	43.43		36.33
Fourth Quarter	42.06		34.24

We have never paid or declared any cash dividends on our common stock, and we do not intend to declare or pay any cash dividends on our common stock in the foreseeable future. Our credit facilities and the indentures and supplemental indentures governing our long-term debt to affiliates and third parties, excluding capital leases, contain covenants that, among other things, restrict our ability to declare or pay dividends on our common stock. In addition, no dividend may be declared or paid on our common stock, other than dividends payable solely in shares of our common stock, unless all accrued dividends for all completed dividend periods have been declared and paid on our preferred stock. Other than to pay dividends on our preferred stock, we currently intend to retain future earnings, if any, to invest in our business. Subject to Delaware law, our board of directors will determine the payment of future dividends on our common stock, if any, and the amount of any dividends in light of:

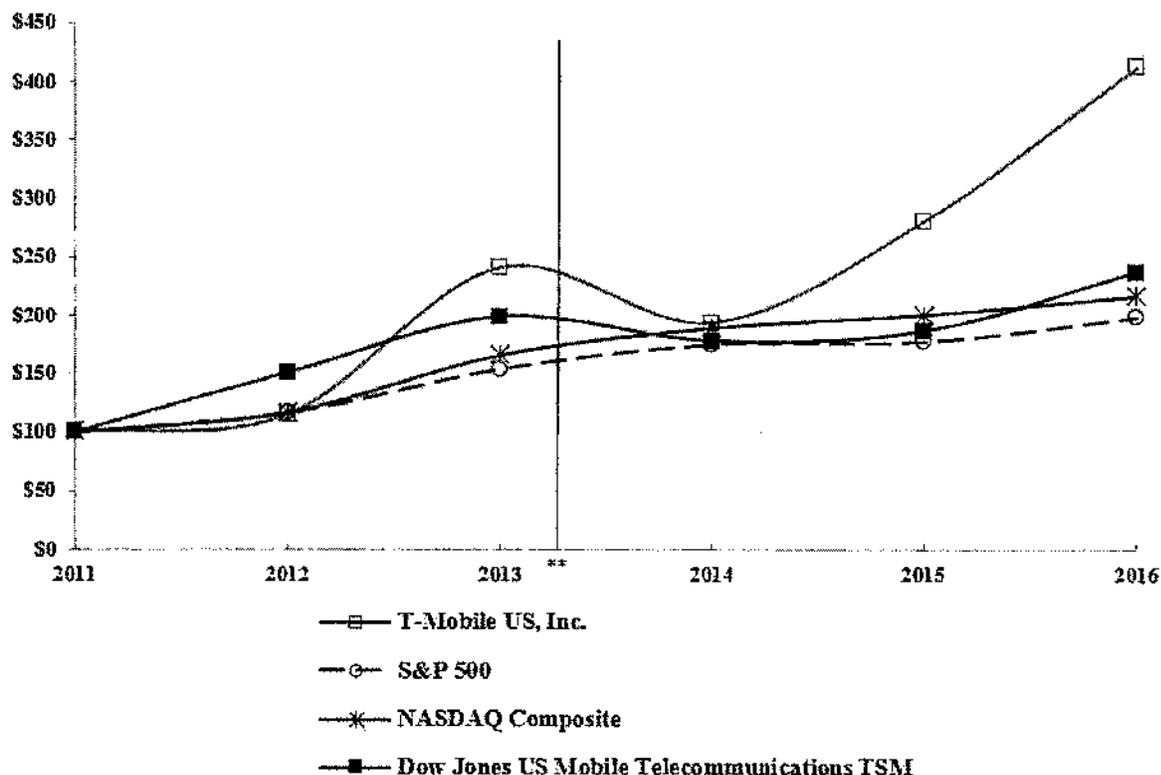
- any applicable contractual or charter restrictions limiting our ability to pay dividends;
- our earnings and cash flows;
- our capital requirements;
- our future needs for cash;
- our financial condition; and
- other factors our board of directors deems relevant.

### Performance Graph

The graph below compares the five-year cumulative total returns of T-Mobile, the NASDAQ Composite index, the S&P 500 index and the Dow Jones US Mobile Telecommunications TSM index. The graph tracks the performance of a \$100 investment, with the reinvestment of all dividends, from December 31, 2011 to December 31, 2016. For periods prior to the closing of the business combination with MetroPCS, our stock price performance represents the stock price of MetroPCS, adjusted to reflect the 1-for-2 reverse stock split effected on April 30, 2013.

Table of Contents**COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN\***

Among T-Mobile US, Inc., the S&P 500 Index, the NASDAQ Composite Index  
and the Dow Jones US Mobile Telecommunications TSM Index



\*\$100 invested on 12/31/11 in stock or index, including reinvestment of dividends.

Fiscal year ending December 31.

\*\*Vertical line represents the first trading day (May 1, 2013) of T-Mobile US, Inc., which was formed through the business combination of T-Mobile USA, Inc. and MetroPCS Communications, Inc.

Copyright© 2017 Standard & Poor's, a division of S&P Global. All rights reserved.

Copyright© 2017 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved.

	At December 31,					
	2011	2012	2013	2014	2015	2016
T-Mobile US, Inc.	\$ 100.00	\$ 114.52	\$ 294.49	\$ 235.83	\$ 342.46	\$ 503.44
S&P 500	100.00	116.00	153.58	174.60	177.01	198.18
NASDAQ Composite	100.00	116.41	165.47	188.69	200.32	216.54
Dow Jones US Mobile Telecommunications TSM	100.00	150.31	198.58	177.40	186.04	237.09

*The stock price performance included in this graph is not necessarily indicative of future stock price performance.*

#### Item 6. Selected Financial Data

The following selected financial data are derived from our consolidated financial statements. In connection with the business combination with MetroPCS, the selected financial data prior to May 1, 2013 represents T-Mobile USA's historical financial data. The data below should be read together with Risk Factors included in Part 1, Item 1A, Management's Discussion and Analysis of Financial Condition and Results of Operations included in Part II, Item 7 and Financial Statements and Supplementary Data included in Part II, Item 8 of this Form 10-K.



Table of Contents**Selected Financial Data**

(in millions, except per share and customer amounts)	As of and for the Year Ended December 31,				
	2016	2015	2014	2013	2012
<b>Statement of Operations Data</b>					
Total service revenues	\$ 27,844	\$ 24,821	\$ 22,375	\$ 19,068	\$ 17,213
Total revenues	37,242	32,053	29,564	24,420	19,719
Operating income (loss)	3,802	2,065	1,416	996	(6,397)
Total other expense, net	(1,475)	(1,087)	(1,003)	(945)	(589)
Income tax (expense) benefit	(867)	(245)	(166)	16	350
Net income (loss)	1,460	733	247	35	(7,336)
Net income (loss) attributable to common stockholders	1,405	678	247	35	(7,336)
Earnings (loss) per share:					
Basic	1.71	0.83	0.31	0.05	(13.70)
Diluted	1.69	0.82	0.30	0.05	(13.70)
<b>Balance Sheet Data</b>					
Cash and cash equivalents	\$ 5,500	\$ 4,582	\$ 5,315	\$ 5,891	\$ 394
Property and equipment, net	20,943	20,000	16,245	15,349	12,807
Spectrum licenses	27,014	23,955	21,955	18,122	14,550
Total assets	65,891	62,413	56,639	49,946	33,622
Total debt, excluding tower obligations	27,786	26,243	21,946	20,182	14,945
Stockholders' equity	18,236	16,557	15,663	14,245	6,115
<b>Other Financial and Operational Data</b>					
Net cash provided by operating activities	\$ 6,135	\$ 5,414	\$ 4,146	\$ 3,545	\$ 3,862
Purchases of property and equipment	(4,702)	(4,724)	(4,317)	(4,025)	(2,901)
Purchases of spectrum licenses and other intangible assets, including deposits	(3,968)	(1,935)	(2,900)	(381)	(387)
Net cash provided by financing activities	463	3,413	2,524	4,044	57
Total customers (in thousands)	71,455	63,282	55,018	46,684	33,389

**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations****Overview**

The objectives of our Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") are to provide users of our consolidated financial statements with the following:

- A narrative explanation from the perspective of management of our financial condition, results of operations, cash flows, liquidity and certain other factors that may affect future results;
- Context to the financial statements; and
- Information that allows assessment of the likelihood that past performance is indicative of future performance.

Our MD&A is provided as a supplement to, and should be read together with, our audited consolidated financial statements for the three years ended December 31, 2016 included in Part II, Item 8 of this Form 10-K. Except as expressly stated, the financial condition and results of operations discussed throughout our MD&A are those of T-Mobile US, Inc. and its consolidated subsidiaries.

**Business Overview**

We introduced our Un-carrier strategy in 2013 with the objective of eliminating customer pain points from the unnecessary complexity of the wireless communication industry. Since that time, we have continued our efforts with the launch of additional initiatives of our Un-carrier strategy. During 2016, we launched the following Un-carrier initiatives:

- In June 2016, we introduced #GetThanked, a history-making move dedicated exclusively to saying “thank you” to our customers. This program, offered to our customers as part of their T-Mobile service: (i) offers eligible new (through December 31, 2016) or existing (as of June 6, 2016) customers ownership in the Company with a free share of T-

Table of Contents

Mobile stock or an additional share of T-Mobile stock for every new active account each customer refers through December 31, 2016, subject to a maximum of 100 shares in a calendar year, (ii) enables eligible customers who download the T-Mobile Tuesday app to be informed about and to redeem products and services offered by participating business partners each Tuesday and (iii) offers eligible customers a full hour of free in-flight Wi-Fi on their smartphone on all Gogo-equipped domestic flights.

- In September 2016, we introduced our T-Mobile ONE plan, a move that gives our customers unlimited calls, unlimited text and unlimited high-speed 4G Long Term Evolution (LTE) data. On T-Mobile ONE, video typically streams at DVD (480p) quality and tethering is at maximum 3G speeds. Customers can choose to add on additional features to T-Mobile ONE for an additional cost. On T-Mobile ONE Plus customers also receive unlimited High Definition Video Day Passes, Voicemail to Text, NameID, unlimited Gogo in-flight internet passes on capable domestic flights and up to two times faster speeds when traveling abroad in 140+ countries and destinations. On T-Mobile ONE Plus International, customers receive the benefits of T-Mobile ONE Plus as well as free and reduced calling from the U.S. to foreign countries and unlimited high-speed 4G LTE mobile hotspot data.
- In January 2017, we introduced, Un-carrier Next, where monthly wireless service fees and all taxes are included in the advertised monthly recurring charge for T-Mobile ONE. We also unveiled Kickback on T-Mobile ONE, where participating customers who use 2 GB or less of data in a month, will get up to a \$10 credit on their next month's bill per qualifying line. In addition, we introduced the Un-contract for T-Mobile ONE with the first-ever price guarantee on an unlimited 4G LTE plan which allows T-Mobile ONE customers to keep their price for service until they decide to change it.

Our ability to acquire and retain branded customers is important to our business in the generation of revenues and we believe our Un-carrier strategy, along with ongoing network improvements, has been successful in attracting and retaining customers as evidenced by continued branded customer growth and improved branded postpaid phone and branded prepaid customer churn.

(in thousands)	Year Ended December 31,			2016 Versus 2015		2015 Versus 2014	
	2016	2015	2014	% Change	% Change	% Change	% Change
<b>Net customer additions</b>							
Branded postpaid customers	4,097	4,510	4,886	(413)	(9)%	(376)	(8)%
Branded prepaid customers	2,508	1,315	1,244	1,193	91 %	71	6 %
Total branded customers	6,605	5,825	6,130	780	13 %	(305)	(5)%

	Year Ended December 31			Bps Change	
	2016	2015	2014	2016 Versus 2015	2015 Versus 2014
Branded postpaid phone churn	1.30%	1.39%	1.58%	-9 bps	-19 bps
Branded prepaid churn	3.88%	4.45%	4.76%	-57 bps	-31 bps

On September 1, 2016, we sold our marketing and distribution rights to certain existing T-Mobile co-branded customers to a current MVNO partner for nominal consideration (the "MVNO Transaction"). Upon the sale, the MVNO Transaction resulted in a transfer of 1,365,000 branded postpaid phone customers and 326,000 branded prepaid customers to wholesale customers. Prospectively from September 1, 2016, revenue for these customers is recorded within wholesale revenues in our Consolidated Statements of Comprehensive Income. Additionally, the impact of the MVNO Transaction resulted in improvements to branded postpaid phone churn for year ended December 31, 2016.

During the year ended December 31, 2016, a handset OEM announced recalls on certain of its smartphone devices. As a result, we recorded no revenue associated with the device sales to customers and impaired the devices to their net realizable value. The OEM has agreed to reimburse T-Mobile for direct and indirect costs associated with the recall, as such, we have recorded an amount due from the OEM as an offset to the loss recorded in Cost of equipment sales and the costs incurred within Selling, general and administrative in our Consolidated Statements of Comprehensive Income and a reduction to Accounts payable and accrued liabilities in our Consolidated Balance Sheets.

Table of Contents**Results of Operations****2016 Highlights**

- Total revenues increased \$5.2 billion, or 16%, to \$37.2 billion in 2016 primarily driven by growth in service and equipment revenues as further discussed below. The MVNO Transaction shifted Branded postpaid revenues to Wholesale revenues, but did not materially impact total revenues.
- Service revenues increased \$3.0 billion, or 12%, to \$27.8 billion in 2016 primarily due to growth in our average branded customer base as a result of strong customer response to our Un-carrier initiatives and the success of our MetroPCS brand and continued growth in new markets.
- Equipment revenues increased \$2.0 billion, or 30%, to \$8.7 billion in 2016 primarily as a result of higher lease revenues, which are recognized over the lease term, resulting from the launch of our JUMP! On Demand program at the end of the second quarter of 2015, an increase in the number of devices sold and a higher average revenue per device sold.
- Operating income increased \$1.7 billion, or 84%, to \$3.8 billion in 2016 primarily due to higher total revenues as well as increased gains on disposals of spectrum licenses, partially offset by higher depreciation and amortization from an increase in the number of devices leased under our JUMP! On Demand Program, higher costs of equipment sales primarily from an increase in the number of devices sold and a higher average cost per device and higher Selling, general and administrative expenses to support customer growth and retention.
- Net income increased \$727 million, or 99%, to \$1.5 billion in 2016 primarily due to higher operating income driven by the factors described above, partially offset by higher interest expense related to higher average debt and higher income tax expense. Additionally, 2016 included \$509 million of net, after-tax gains on disposal of spectrum licenses compared to \$100 million in 2015.
- Adjusted EBITDA increased \$3.0 billion, or 41%, to \$10.4 billion in 2016 primarily from higher service revenues and gains on disposal of spectrum licenses, partially offset by increases in selling, general and administrative expenses to support customer growth. Lower losses on equipment in 2016 primarily due to an increase in lease revenues resulting from the launch of our JUMP! On Demand program at the end of the second quarter of 2015. Revenues associated with leased devices are recognized over the lease term.
- Net cash provided by operating activities increased \$721 million, or 13%, to \$6.1 billion in 2016. The increase was primarily due to an increase in net non-cash income and expenses included in Net income primarily due to changes in Depreciation and Amortization, Deferred income tax expense and Gains on disposal of spectrum licenses expense, as well as an increase in Net income. The increase was partially offset by an increase in net cash outflows from changes in working capital.
- Free Cash Flow increased \$743 million, or 108%, to \$1.4 billion in 2016. The increase was primarily from higher net cash provided by operating activities as discussed above. Cash purchases of property and equipment includes capitalized interest of \$142 million and \$246 million in 2016 and 2015, respectively.

Table of Contents

Set forth below is a summary of our consolidated results:

(in millions)	Year Ended December 31,			2016 Versus 2015		2015 Versus 2014	
	2016	2015	2014	\$ Change	% Change	\$ Change	% Change
<b>Revenues</b>							
Branded postpaid revenues	\$ 18,138	\$ 16,383	\$ 14,392	\$ 1,755	11 %	\$ 1,991	14 %
Branded prepaid revenues	8,553	7,553	6,986	1,000	13 %	567	8 %
Wholesale revenues	903	692	731	211	30 %	(39)	(5)%
Roaming and other service revenues	250	193	266	57	30 %	(73)	(27)%
Total service revenues	27,844	24,821	22,375	3,023	12 %	2,446	11 %
Equipment revenues	8,727	6,718	6,789	2,009	30 %	(71)	(1)%
Other revenues	671	514	400	157	31 %	114	29 %
Total revenues	37,242	32,053	29,564	5,189	16 %	2,489	8 %
<b>Operating expenses</b>							
Cost of services, exclusive of depreciation and amortization shown separately below	5,731	5,554	5,788	177	3 %	(234)	(4)%
Cost of equipment sales	10,819	9,344	9,621	1,475	16 %	(277)	(3)%
Selling, general and administrative	11,378	10,189	8,863	1,189	12 %	1,326	15 %
Depreciation and amortization	6,243	4,688	4,412	1,555	33 %	276	6 %
Cost of MetroPCS business combination	104	376	299	(272)	(72)%	77	26 %
Gains on disposal of spectrum licenses	(835)	(163)	(840)	(672)	NM	677	(81)%
Other, net	—	—	5	—	NM	(5)	NM
Total operating expenses	33,440	29,988	28,148	3,452	12 %	1,840	7 %
Operating income	3,802	2,065	1,416	1,737	84 %	649	46 %
<b>Other income (expense)</b>							
Interest expense	(1,418)	(1,085)	(1,073)	(333)	31 %	(12)	1 %
Interest expense to affiliates	(312)	(411)	(278)	99	(24)%	(133)	48 %
Interest income	261	420	359	(159)	(38)%	61	17 %
Other expense, net	(6)	(11)	(11)	5	(45)%	—	— %
Total other expense, net	(1,475)	(1,087)	(1,003)	(388)	36 %	(84)	8 %
Income before income taxes	2,327	978	413	1,349	138 %	565	137 %
Income tax expense	(867)	(245)	(166)	(622)	254 %	(79)	48 %
Net income	\$ 1,460	\$ 733	\$ 247	\$ 727	99 %	\$ 486	197 %
Net cash provided by operating activities	\$ 6,135	\$ 5,414	\$ 4,146	\$ 721	13 %	\$ 1,268	31 %
Net cash used in investing activities	(5,680)	(9,560)	(7,246)	3,880	(41)%	(2,314)	32 %
Net cash provided by financing activities	463	3,413	2,524	(2,950)	(86)%	889	35 %
<b>Non-GAAP Financial Measures</b>							
Adjusted EBITDA	\$ 10,391	\$ 7,393	\$ 5,636	\$ 2,998	41 %	\$ 1,757	31 %
Free Cash Flow	1,433	690	(171)	743	108 %	861	(504)%
NM - Not Meaningful							

**Comparing 2016 Results with 2015 Results**

**Total revenues** increased \$5.2 billion or 16% primarily due to:

**Branded postpaid revenues** increased \$1.8 billion or 11% primarily from:

- A 13% increase in the number of average branded postpaid phone and mobile broadband customers, driven by strong

customer response to our Un-carrier initiatives and promotions for services and devices;

- Higher device insurance program revenues primarily from customer growth; and
- Higher regulatory program revenues; partially offset by
- An increase in the non-cash net revenue deferral for Data Stash; and
- The impact of reduced Branded postpaid revenues resulting from the MVNO Transaction.

Table of Contents

**Branded prepaid revenues** increased \$1.0 billion or 13% primarily from:

- A 13% increase in the number of average branded prepaid customers driven by the success of our MetroPCS brand; and
- Continued growth in new markets.

**Wholesale revenues** increased \$211 million or 30% primarily from:

- The impact of the increased Wholesale revenues resulting from the MVNO Transaction;
- Growth in customers of certain MVNO partners; and
- An increase in data usage per customer.

**Roaming and other service revenues** increased \$57 million or 30% primarily due to higher international roaming revenues driven by an increase in inbound roaming volumes.

**Equipment revenues** increased \$2.0 billion or 30% primarily from:

- An increase of \$1.2 billion in lease revenues resulting from the launch of our JUMP! On Demand program at the end of the second quarter of 2015. Revenues associated with leased devices are recognized over the lease term.
- An increase of \$570 million in device sales revenues, primarily due to a 9% increase in the number of devices sold. Device sales revenue is recognized at the time of sale.

Gross EIP device financing to our customers increased by \$923 million to \$6.1 billion primarily due to an increase in devices financed due to our focus on EIP sales in 2016, compared to focus on devices financed on JUMP! On Demand after the launch of the program at the end of the second quarter of 2015.

**Other revenues** increased \$157 million or 31% primarily from:

- Higher revenue from revenue share agreements with third parties; and
- An increase in co-location rental income from leasing space on wireless communication towers to third parties.

Our operating expenses consist of the following categories:

- **Cost of services** consists primarily of costs directly attributable to providing wireless service through the operation of our network, including direct switch and cell site costs, such as rent, network access and transport costs, utilities, maintenance, associated labor costs, long distance costs, regulatory program costs, roaming fees paid to other carriers and data content costs.
- **Cost of equipment sales** consists primarily of costs of devices and accessories sold to customers and dealers, device costs to fulfill insurance and warranty claims, costs related to returned and purchased leased devices, write-downs of inventory related to shrinkage and obsolescence, and shipping and handling costs.
- **Selling, general and administrative** consists of costs not directly attributable to providing wireless service for the operation of sales, customer care and corporate activities. These include commissions paid to dealers and retail employees for activations and upgrades, labor and facilities costs associated with retail sales force and administrative space, marketing and promotional costs, customer support and billing, bad debt expense, losses from sales of receivables and back office administrative support activities.

**Operating expenses** increased \$3.5 billion or 12% primarily due to:

**Cost of services** increased \$177 million or 3% primarily from:

- Higher regulatory program costs and expenses associated with network expansion and the build-out of our network to utilize our 700 MHz A-Block spectrum licenses, including higher employee-related costs; partially offset by
- Lower long distance and toll costs; and

- Synergies realized from the decommissioning of the MetroPCS CDMA network.

Table of Contents

**Cost of equipment sales** increased \$1.5 billion or 16% primarily from:

- A 9% increase in the number of devices sold; and
- An increase in the impact from returned and purchased leased devices.

Under our JUMP! On Demand program, the cost of the leased wireless device is capitalized and recognized as depreciation expense over the term of the lease rather than recognized as cost of equipment sales when the device is delivered to the customer. Additionally, upon device upgrade or at lease end, customers must return or purchase their device. Returned devices transferred from Property and equipment, net are recorded as inventory and are valued at the lower of cost or market with any write-down to market recognized as Cost of equipment sales.

**Selling, general and administrative** increased \$1.2 billion or 12% primarily from strategic investments to support our growing customer base including higher:

- Employee-related costs;
- Commissions driven by an increase in branded customer additions; and
- Promotional costs.

**Depreciation and amortization** increased \$1.6 billion or 33% primarily from:

- \$1.5 billion in depreciation expense related to devices leased under our JUMP! On Demand program launched at the end of the second quarter of 2015. Under our JUMP! On Demand program, the cost of a leased wireless device is depreciated over the lease term to its estimated residual value. The total number of devices under lease was higher year-over-year, resulting in higher depreciation expense; and
- The continued build-out of our 4G LTE network.

**Cost of MetroPCS business combination** decreased \$272 million or 72% primarily from lower network decommissioning costs. In 2014, we began decommissioning the MetroPCS CDMA network and certain other redundant network cell sites as part of the business combination. On July 1, 2015, we officially completed the shutdown of the MetroPCS CDMA network. Network decommissioning costs, which are excluded from Adjusted EBITDA, primarily relate to the acceleration of lease costs for cell sites that would have otherwise been recognized as cost of services over the remaining lease term had we not decommissioned the cell sites. Although we expect to incur additional network decommissioning costs in 2017, these costs are not expected to be significant.

**Gains on disposal of spectrum licenses** increased \$672 million primarily from a \$636 million gain from a spectrum license transaction with AT&T recorded in the first quarter of 2016 and \$199 million from other transactions in 2016, compared to \$163 million in 2015. See Note 5 – Goodwill, Spectrum Licenses and Other Intangible Assets of the Notes to the Consolidated Financial Statements.

**Net income** increased \$727 million or 99% primarily from:

- **Operating income**, the components of which are discussed above, increased \$1.7 billion or 84% and
- **Interest expense to affiliates** decreased \$99 million or 24% primarily from:
  - Changes in the fair value of embedded derivative instruments associated with our Senior Reset Notes issued to Deutsch Telekom in 2015; partially offset by
  - Higher interest rates on certain Senior Reset Notes issued to Deutsch Telekom, which were adjusted at reset dates in the second quarter of 2016 and in 2015. Partially offset by:
- **Income tax expense** increased \$622 million or 254% primarily from:
  - Higher income before income taxes; and
  - A higher effective tax rate. The effective tax rate was 37.3% in 2016, compared to 25.1% in 2015. The increase in the effective income tax rate was primarily due to income tax benefits for discrete income tax items recognized in 2015 that did not impact 2016; partially offset by the recognition of \$58 million of excess



Table of Contents

tax benefits related to share-based payments following the adoption of ASU 2016-09 as of January 1, 2016. See Note 1 – Summary of Significant Accounting Policies of the Notes to the Consolidated Financial Statements. Based on recent earnings in certain jurisdictions, sufficient positive evidence may exist within the next twelve months such that we may release a portion of our valuation allowance.

- **Interest expense** increased \$333 million or 31% primarily from:
  - Higher average debt balances with third parties; and
  - Lower capitalized interest costs of \$83 million primarily due to a higher level of build out of our network to utilize our 700 MHz A-Block spectrum licenses in 2015, compared to 2016.
- **Interest income** decreased \$159 million or 38% primarily due to \$166 million lower imputed interest income associated with devices financed through EIP resulting from:
  - An increase in sales of certain EIP receivables pursuant to our EIP receivables sales arrangement resulting from an increase in the maximum funding commitment in June 2016. Interest associated with EIP receivables is imputed at the time of a device sale and then recognized over the financed installment term. See Note 2 – Equipment Installment Plan Receivables of the Notes to the Consolidated Financial Statements; and
  - Focus on devices financed on JUMP! On Demand in the third and fourth quarters of 2015 following the launch of the program of at the end of the second quarter 2015.

We are making an accounting change in 2017 to include imputed interest associated with EIP receivables in Other revenues in our Consolidated Statements of Comprehensive Income. The impact from this accounting change is expected to be approximately \$0.2 to \$0.3 billion in 2017.

Net income during 2016 and 2015 included net, after-tax gains on disposal of spectrum licenses of \$509 million and \$100 million, respectively.

**Guarantor Subsidiaries**

The financial condition and results of operations of the Parent, Issuer and Guarantor Subsidiaries is substantially similar to our consolidated financial condition.

The most significant components of the financial condition of our Non-Guarantor Subsidiaries were as follows:

(in millions)	December 31,		Change	
	2016	2015	\$	%
Other current assets	\$ 565	\$ 400	\$ 165	41 %
Property and equipment, net	375	454	(79)	(17)%
Tower obligations	2,221	2,247	(26)	(1)%
Total stockholders' deficit	(1,374)	(1,359)	(15)	(1)%

The most significant components of the results of operations of our Non-Guarantor Subsidiaries were as follows:

(in millions)	Year Ended December 31,		Change	
	2016	2015	\$	%
Service revenues	\$ 2,023	\$ 1,669	\$ 354	21 %
Cost of equipment sales	1,027	720	307	43 %
Selling, general and administrative	868	733	135	18 %
Total comprehensive income	24	60	(36)	(60)%

The increases in Service revenues, Cost of equipment sales and Selling, general and administrative were primarily the result of an increase in activity of the non-guarantor subsidiary that provides device insurance, primarily driven by growth in our customer base. All other results of operations of the Parent, Issuer and Guarantor Subsidiaries are substantially similar to the Company's consolidated results of operations. See Note 15 – Guarantor Financial Information of the Notes to the Consolidated Financial Statements.



Table of Contents**Comparing 2015 Results with 2014 Results**

**Total Revenues** increased \$2.5 billion or 8% primarily due to:

**Branded postpaid revenues** increased \$2.0 billion or 14% primarily from:

- Growth in the number of average branded postpaid and mobile broadband customers, driven by strong customer response to our Un-carrier initiatives and promotions for services and devices;
- Increased customer adoption of upgrade and insurance programs; and
- Increased regulatory program revenues; partially offset by
- Lower branded postpaid phone ARPU.

**Branded prepaid revenues** increased \$567 million or 8% primarily from:

- Growth in the number of average branded prepaid customers driven by the success of our MetroPCS brand promotional activities; and
- Continued growth in expansion markets.

**Wholesale revenues** decreased \$39 million or 5% primarily from:

- Revised agreements with certain MVNO partners in 2015; partially offset by
- Growth in customers of certain MVNO partners.

**Roaming and other service revenues** decreased \$73 million or 27% primarily from:

- Lower international roaming revenues driven by changes in contractual arrangements with certain roaming partners; and
- A reduction in early termination fees.

**Equipment revenues** decreased \$71 million or 1% primarily from:

- Lower average revenue per device sold, due in part to the impact of customers shifting to leasing higher-end devices under our JUMP! On Demand program; partially offset by
- Growth in the number of devices and accessories sold.

With JUMP! On Demand, revenues associated with leased wireless devices are recognized over the term of the lease rather than when the device is delivered to the customer. Despite the increase in the number of devices leased in 2015 following the launch of JUMP! On Demand, the unit volume of device sales increased 5% in 2015, compared to 2014.

We financed \$5.2 billion of devices through EIP during 2015, a decrease from \$5.8 billion in 2014, primarily due to a decline in devices financed through EIP as customers increasingly shifted to leasing devices with JUMP! On Demand.

**Other revenues** increased \$114 million or 29% primarily attributable to higher non-service revenues from revenue share agreements with third parties.

**Operating expenses** increased \$1.8 billion or 7% primarily due to:

**Cost of services** decreased \$234 million or 4% primarily from:

- Synergies realized from the decommissioning of the MetroPCS CDMA network;
- Lower lease expense associated with spectrum license lease agreements; and
- A reduction in certain regulatory program costs; partially offset by
- Increases related to our network expansion and build-out of our 700 MHz A-Block spectrum.



Table of Contents

**Cost of equipment sales** decreased \$277 million or 3% primarily from:

- Lower average cost per device sold, mainly due to the impact of customers shifting to leasing higher-end devices with JUMP! On Demand; partially offset by
- Growth in the number of devices and accessories sold.

With JUMP! On Demand, the cost of the leased wireless device is capitalized and recognized as depreciation expense over the term of the lease rather than recognized as cost of equipment sales when the device is delivered to the customer. Despite the increase in the number of devices leased in 2015 following the launch of JUMP! On Demand, the unit volume of device sales increased 5% in 2015, compared to 2014.

**Selling, general and administrative** increased \$1.3 billion or 15% primarily from supporting the growing customer base, which also increased 15% and reflects increases in:

- Employee-related costs;
- Promotional costs;
- Commissions; and
- Bad debt expense and losses from sales of receivables primarily resulting from growth in the customer base and in the EIP program.

**Depreciation and amortization** increased \$276 million or 6% primarily from \$312 million in depreciation expense related to devices leased under our JUMP! On Demand program launched at the end of the second quarter of 2015. Under our JUMP! On Demand program, the cost of a leased wireless device is depreciated over the lease term to its estimated residual value. The total number of devices under lease was higher year-over-year, resulting in higher depreciation expense.

**Cost of MetroPCS business combination** increased \$77 million or 26% primarily from higher network decommissioning costs associated with the business combination. In 2014, we began decommissioning the MetroPCS CDMA network and certain other redundant network cell sites. On July 1, 2015, T-Mobile officially completed the shutdown of the MetroPCS CDMA network. Network decommissioning costs, which are excluded from Adjusted EBITDA, primarily relate to the acceleration of lease costs for cell sites that would have otherwise been recognized as cost of services over the remaining lease term had we not decommissioned the cell sites.

**Gains on disposal of spectrum licenses** decreased \$677 million or 81% primarily from:

- \$163 million in 2015 which primarily consisted of a non-cash gain of \$139 million from spectrum license transactions with Verizon recorded in the fourth quarter of 2015; as compared to
- \$840 million in 2014 which primarily consisted of non-cash gains from spectrum license transactions with Verizon, and to a lesser extent, a non-cash gain from a spectrum license transaction with AT&T during the fourth quarter of 2014.

See Note 5 – Goodwill, Spectrum Licenses and Other Intangible Assets of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for further information.

**Net income** increased \$486 million or 197% primarily from:

- **Operating income**, the components of which are discussed above, increased \$649 million or 46% and
- **Interest income** increased \$61 million or 17% primarily attributable to higher interest income from devices financed through EIP. Interest associated with EIP receivables is imputed at the time of sale and then recognized over the financed installment term. Partially offset by:
- **Interest expense to affiliates** increased \$133 million or 48% primarily from:
  - Changes in the fair value of embedded derivative instruments associated with the Senior Reset Notes issued to Deutsche Telekom; partially offset by
  - Lower capitalized interest costs associated with the build out of our network to utilize our 700 MHz A-Block spectrum licenses.



Table of Contents

- **Income tax expense** increased \$79 million or 48% primarily from:
  - Higher income before income taxes; partially offset by
  - A lower effective tax rate. The effective tax rate was 25.1% in 2015, compared to 40.2% in 2014. The decrease in the effective income tax rate was primarily due to the impact of discrete income tax items recognized in 2015, including changes in state and local income tax laws and the recognition of foreign tax credits.
- **Interest expense** increased \$12 million or 1% primarily from:
  - Higher debt balances with third parties; partially offset by
  - Lower capitalized interest costs associated with the build out of our network to utilize our 700 MHz A-Block spectrum licenses.

Net income during 2015 and 2014 included net, after-tax gains on disposal of spectrum licenses of \$100 million and \$515 million, respectively.

**Guarantor Subsidiaries**

The financial condition and results of operations of the Parent, Issuer and Guarantor Subsidiaries is substantially similar to the Company's consolidated financial condition.

The most significant components of the financial condition of our Non-Guarantor Subsidiaries were as follows:

(in millions)	December 31,		Change	
	2015	2014	\$	%
Other current assets	\$ 400	\$ 249	\$ 151	61%
Property and equipment, net	454	537	(83)	(15)%
Tower obligations	2,247	2,250	(3)	—%
Total stockholders' deficit	(1,359)	(1,451)	92	(6)%

The most significant components of the results of operations of our Non-Guarantor Subsidiaries were as follows:

(in millions)	Year Ended December 31,		Change	
	2015	2014	\$	%
Service revenues	\$ 1,669	\$ 1,302	\$ 367	28%
Cost of equipment sales	720	702	18	3%
Selling, general and administrative	733	518	215	42%
Total comprehensive income (loss)	60	(38)	98	258%

The increases in Service revenues, Cost of equipment sales and Selling, general and administrative were primarily the result of an increase in activity of the non-guarantor subsidiary that provides device insurance, primarily driven by growth in our customer base. All other results of operations of the Parent, Issuer and Guarantor Subsidiaries are substantially similar to our consolidated results of operations. See Note 15 – Guarantor Financial Information of the Notes to the Consolidated Financial Statements.

**Performance Measures**

In managing our business and assessing financial performance, we supplement the information provided by our financial statements with other operating or statistical data and non-GAAP financial measures. These operating and financial measures are utilized by our management to evaluate our operating performance and, in certain cases, our ability to meet liquidity requirements. Although companies in the wireless industry may not define each of these measures in precisely the same way, we believe that these measures facilitate comparisons with other companies in the wireless industry on key operating and financial measures.

Table of Contents**Total Customers**

A customer is generally defined as a SIM card with a unique T-Mobile identity number which is associated with an account that generates revenue. Branded customers generally include customers that are qualified either for postpaid service utilizing phones or mobile broadband devices (including tablets), where they generally pay after receiving service, or prepaid service, where they generally pay in advance. Wholesale customers include M2M and MVNO customers that operate on our network, but are managed by wholesale partners.

The following table sets forth the number of ending customers:

(in thousands)	December 31, 2016	December 31, 2015	December 31, 2014	% Change 2016 Versus 2015	% Change 2016 Versus 2014
<b>Customers, end of period</b>					
Branded postpaid phone customers	31,297	29,355	25,844	7%	14%
Branded postpaid mobile broadband customers	3,130	2,340	1,341	34%	74%
Total branded postpaid customers	34,427	31,695	27,185	9%	17%
Branded prepaid customers	19,813	17,631	16,316	12%	8%
Total branded customers	54,240	49,326	43,501	10%	13%
Wholesale customers	17,215	13,956	11,517	23%	21%
Total customers, end of period	71,455	63,282	55,018	13%	15%

The following table sets forth the number of net customer additions:

(in thousands)	Year Ended December 31,			2016 Versus 2015		2016 Versus 2014	
	2016	2015	2014	% Change	% Change	% Change	% Change
<b>Net customer additions</b>							
Branded postpaid phone customers	3,307	3,511	4,047	(204)	(6)%	(536)	(13)%
Branded postpaid mobile broadband customers	790	999	839	(209)	(21)%	160	19%
Total branded postpaid customers	4,097	4,510	4,886	(413)	(9)%	(376)	(8)%
Branded prepaid customers	2,508	1,315	1,244	1,193	91%	71	6%
Total branded customers	6,605	5,825	6,130	780	13%	(305)	(5)%
Wholesale customers	1,568	2,439	2,204	(871)	(36)%	235	11%
Total net customer additions	8,173	8,264	8,334	(91)	(1)%	(70)	(1)%
Transfer from branded postpaid phone customers	(1,365)	—	—	(1,365)	100%	—	—%
Transfer from branded prepaid customers	(326)	—	—	(326)	100%	—	—%
Transfer to wholesale customers	1,691	—	—	1,691	100%	—	—%

The MVNO Transaction resulted in a transfer of 1,365,000 branded postpaid phone customers and 326,000 branded prepaid customers to wholesale customers on September 1, 2016. Prospectively from September 1, 2016, net customer additions for these customers are included within Wholesale customers. Ending customers as of December 31, 2016 reflect the transfers in connection with the MVNO Transaction.

**Branded Customers**

Total branded net customer additions increased 780,000, or 13%, in 2016 primarily from:

- Higher branded prepaid net customer additions primarily due to the success of our MetroPCS brand, continued growth in new markets and distribution expansion, partially offset by an increase in the number of qualified branded prepaid customers migrating to branded postpaid plans; partially offset by
- Lower branded postpaid mobile broadband net customer additions primarily due to higher deactivations resulting from churn on a growing branded postpaid mobile broadband customer base, partially offset by higher gross customer additions; and
- Lower branded postpaid phone net customer additions primarily due to lower gross customer additions from higher

deactivations on a growing customer base, partially offset by lower churn as well as an increase in the number of qualified branded prepaid customers migrating to branded postpaid plans as well as the optimization of our third-party distribution channels.

Table of Contents

Total branded net customer additions decreased 305,000, or 5%, in 2015 primarily from:

- Lower branded postpaid phone net customer additions primarily due to lower gross customer additions in 2015, compared to 2014, which included the introduction of Un-carrier 4.0 Contract Freedom and certain attractive family rate plan promotions, partially offset by approximately 765,000 qualified branded prepaid customers upgrading to branded postpaid plans in 2015, compared to approximately 420,000 in 2014; partially offset by
- Higher branded postpaid mobile broadband net customer additions primarily due to higher gross customer additions driven by promotions for mobile broadband devices, partially offset by higher deactivations resulting from the discontinuation of certain promotional pricing for mobile broadband services and ongoing competitive activity in the marketplace; and
- Higher branded prepaid net customer additions primarily due to higher gross customer additions driven by the success of our MetroPCS brand promotional activities and continued growth in new markets, partially offset by approximately 765,000 qualified branded prepaid customers upgrading to branded postpaid plans in 2015, compared to approximately 420,000 in 2014.

**Wholesale**

Wholesale net customer additions decreased 871,000, or 36%, in 2016 primarily due to higher MVNO deactivations from certain MVNO partners. Going forward, we expect wholesale net customer additions to be significantly lower in 2017, as our MVNO partners deemphasize Lifeline in favor of higher ARPU customer categories.

Wholesale net customer additions increased 235,000, or 11%, in 2015 primarily due to higher MVNO gross customer additions, partially offset by higher MVNO deactivations.

**Customers Per Account**

Customers per account is calculated by dividing the number of branded postpaid customers as of the end of the period by the number of branded postpaid accounts as of the end of the period. An account may include branded postpaid phone and mobile broadband customers. We believe branded postpaid customers per account provides management, investors and analysts with useful information to evaluate our branded postpaid customer base on a per account basis.

	December 31, 2016	December 31, 2015	December 31, 2014	2016 Versus 2015		2015 Versus 2014	
				% Change	% Change	% Change	% Change
Branded postpaid customers per account	2.86	2.54	2.36	0.32	13%	0.18	8%

Branded postpaid customers per account increased in 2016 and 2015 primarily due growth of customers on promotions targeting families and increased penetration of mobile broadband devices. In addition, the increase in 2016 was impact by the MVNO Transaction.

**Churn**

Churn represents the number of customers whose service was disconnected as a percentage of the average number of customers during the specified period. The number of customers whose service was disconnected is presented net of customers that subsequently have their service restored within a certain period of time. We believe that churn provides management, investors and analysts with useful information to evaluate customer retention and loyalty.

	Year Ended December 31,			Bps Change 2016 Versus 2015	Bps Change 2015 Versus 2014
	2016	2015	2014		
Branded postpaid phone churn	1.30%	1.39%	1.58%	-9 bps	-19 bps
Branded prepaid churn	3.88%	4.45%	4.76%	-57 bps	-31 bps

Branded postpaid phone churn decreased 9 basis points in 2016 primarily from:

- The MVNO Transaction as the customers transferred had a higher rate of churn; and
- Increased customer satisfaction and loyalty from ongoing improvements to network quality, customer service and the overall value of our offerings in the marketplace.



Table of Contents

Branded postpaid phone churn decreased 19 basis points in 2015 primarily from ongoing improvements to network quality, customer service and the overall value of our offerings in the marketplace, resulting in increased customer satisfaction and loyalty.

Branded prepaid churn decreased 57 basis points in 2016 primarily from:

- A decrease in certain customers, which have a higher rate of branded prepaid churn;
- Strong performance of the MetroPCS brand; and
- A methodology change in the third quarter of 2015 as discussed below.

Branded prepaid churn decreased 31 basis points in 2015 primarily from a methodology change during 2015 that had no impact on our reported branded prepaid ending customers or net customer additions, but resulted in computationally lower gross customer additions and deactivations. Revision of prior periods was not practicable because certain historical data was no longer available.

*Average Revenue Per User, Average Billings Per User*

ARPU represents the average monthly service revenue earned from customers. We believe ARPU provides management, investors and analysts with useful information to assess and evaluate our service revenue realization per customer and assist in forecasting our future service revenues generated from our customer base. Branded postpaid phone ARPU excludes mobile broadband customers and related revenues.

Average Billings Per User ("ABPU") represents the average monthly customer billings, including monthly lease revenues and EIP billings before securitization, per customer. We believe branded postpaid ABPU provides management, investors and analysts with useful information to evaluate average branded postpaid customer billings as it is indicative of estimated cash collections, including device financing payments, from our customers each month.

The following tables illustrate the calculation of our operating measures ARPU and ABPU and reconcile these measures to the related service revenues:

(in millions, except average number of customers, ARPU and ABPU)	Year Ended December 31,			2016 Versus 2015		2015 Versus 2014	
	2016	2015	2014	\$ Change	% Change	\$ Change	% Change
<b>Calculation of Branded Postpaid Phone ARPU</b>							
Branded postpaid service revenues	\$ 18,138	\$ 16,383	\$ 14,392	\$ 1,755	11 %	\$ 1,991	14 %
Less: Branded postpaid mobile broadband revenues	(773)	(588)	(261)	(185)	31 %	(327)	125 %
Branded postpaid phone service revenues	\$ 17,365	\$ 15,795	\$ 14,131	\$ 1,570	10 %	\$ 1,664	12 %
Divided by: Average number of branded postpaid phone customers (in thousands) and number of months in period	30,484	27,604	23,817	2,880	10 %	3,787	16 %
Branded postpaid phone ARPU	\$ 47.47	\$ 47.68	\$ 49.44	\$ (0.21)	NM	\$ (1.76)	(4)%
<b>Calculation of Branded Postpaid ABPU</b>							
Branded postpaid service revenues	\$ 18,138	\$ 16,383	\$ 14,392	\$ 1,755	11 %	\$ 1,991	14 %
EIP billings	5,432	5,494	3,596	(62)	(1)%	1,898	53 %
Lease revenues	1,416	224	—	1,192	532 %	224	100 %
Total billings for branded postpaid customers	\$ 24,986	\$ 22,101	\$ 17,988	\$ 2,885	13 %	\$ 4,113	23 %
Divided by: Average number of branded postpaid customers (in thousands) and number of months in period	33,184	29,341	24,683	3,843	13 %	4,658	19 %
Branded postpaid ABPU	\$ 62.75	\$ 62.77	\$ 60.73	\$ (0.02)	NM	\$ 2.04	3 %
<b>Calculation of Branded Prepaid ARPU</b>							
Branded prepaid service revenues	\$ 8,553	\$ 7,553	\$ 6,986	\$ 1,000	13 %	\$ 567	8 %
Divided by: Average number of branded prepaid customers (in thousands) and number of months in period	18,797	16,704	15,691	2,093	13 %	1,013	6 %
Branded prepaid ARPU	\$ 37.92	\$ 37.68	\$ 37.10	\$ 0.24	1 %	\$ 0.58	2 %

NM - Not Meaningful

Table of Contents**Branded Postpaid Phone ARPU:**

Branded postpaid phone ARPU decreased \$0.21, in 2016 primarily from:

- Decreases due to an increase in the non-cash net revenue deferral for Data Stash;
- Dilution from promotional activities; partially offset by
- Higher data attach rates;
- The positive impact from our T-Mobile ONE rate plans;
- The transfer of customers as part of the MVNO transaction as those customers had lower ARPU;
- Continued growth of our insurance programs; and
- Higher regulatory program revenues.

We are making an accounting change in 2017 to include imputed interest associated with EIP receivables in Other revenues in our Consolidated Statements of Comprehensive Income, which will be excluded from branded postpaid phone ARPU.

Branded postpaid phone ARPU decreased \$1.76, or 4%, in 2015 primarily from:

- Dilution from the continued growth of customers on Simple Choice plans and promotions targeting families; partially offset by
- An increase in regulatory program revenues.

**Branded Postpaid ABPU:**

Branded postpaid ABPU decreased \$0.02 in 2016 primarily from:

- Lower EIP billings due to the impact of our JUMP! On Demand program launched at the end of the second quarter of 2015;
- Lower branded postpaid phone ARPU, as described above;
- Dilution from increased penetration of mobile broadband devices; partially offset by
- An increase in lease revenues.

Branded postpaid ABPU increased \$2.04, or 3%, in 2015 primarily from:

- Growth in devices financed by customers through the EIP and JUMP! on Demand programs; partially offset by
- Lower branded postpaid phone ARPU, as described above.

**Branded Prepaid ARPU:**

Branded prepaid ARPU increased \$0.24, or 1%, in 2016 primarily from:

- A decrease in certain customers that had lower average branded prepaid ARPU, as well as higher data attach rates; partially offset by
- Dilution from growth of customers on rate plan promotions.

Branded prepaid ARPU increased \$0.58, or 2%, in 2015 primarily from:

- An increase in the mix of branded prepaid customers choosing plans with more data, which generate a higher ARPU; partially offset by
- Dilution from growth of customers on rate plan promotions.

***Adjusted EBITDA***

Adjusted EBITDA represents earnings before interest expense, net of Interest income, Income tax expense, Depreciation and amortization, non-cash Stock-based compensation and certain expenses not reflective of T-Mobile's operating performance.

Table of Contents

Net income margin represents Net income divided by Service revenues. Adjusted EBITDA margin represents Adjusted EBITDA divided by Service revenues.

Adjusted EBITDA is a non-GAAP financial measure utilized by our management to monitor the financial performance of our operations. We use Adjusted EBITDA internally as a metric to evaluate and compensate our personnel and management for their performance, and as a benchmark to evaluate our operating performance in comparison to our competitors. Management believes analysts and investors use Adjusted EBITDA as a supplemental measure to evaluate overall operating performance and facilitate comparisons with other wireless communications companies because it is indicative of our ongoing operating performance and trends by excluding the impact of interest expense from financing, non-cash depreciation and amortization from capital investments, non-cash stock-based compensation, network decommissioning costs as they are not indicative of our ongoing operating performance and certain other nonrecurring expenses. Adjusted EBITDA has limitations as an analytical tool and should not be considered in isolation or as a substitute for income from operations, net income or any other measure of financial performance reported in accordance with GAAP.

The following table illustrates the calculation of Adjusted EBITDA and reconciles Adjusted EBITDA to Net income, which we consider to be the most directly comparable GAAP financial measure:

(in millions)	Year Ended December 31,			2016 Versus 2015		2015 Versus 2014	
	2016	2015	2014	\$ Change	% Change	\$ Change	% Change
Net income	\$ 1,460	\$ 733	\$ 247	\$ 727	99 %	\$ 486	197%
Adjustments:							
Interest expense	1,418	1,085	1,073	333	31 %	12	1%
Interest expense to affiliates	312	411	278	(99)	(24)%	133	48%
Interest income	(261)	(420)	(359)	159	(38)%	(61)	17%
Other expense, net	6	11	11	(5)	(45)%	—	—%
Income tax expense	867	245	166	622	254 %	79	48%
Operating income	3,802	2,065	1,416	1,737	84 %	649	46%
Depreciation and amortization	6,243	4,688	4,412	1,555	33 %	276	6%
Cost of MetroPCS business combination	104	376	299	(272)	(72)%	77	26%
Stock-based compensation <sup>(1)</sup>	235	222	211	13	6 %	11	5%
Gains on disposal of spectrum licenses <sup>(1)</sup>	—	—	(720)	—	NM	720	NM
Other, net <sup>(1)</sup>	7	42	18	(35)	(83)%	24	NM
Adjusted EBITDA	\$ 10,391	\$ 7,393	\$ 5,636	\$ 2,998	41 %	\$ 1,757	31%
Net income margin (Net income divided by service revenues)	5%	3%	1%		200 bps		200 bps
Adjusted EBITDA margin (Adjusted EBITDA divided by service revenues)	37%	30%	25%		700 bps		500 bps

NM - Not Meaningful

(1) Stock-based compensation includes payroll tax impacts and may not agree to stock-based compensation expense in the consolidated financial statements. Gains on disposal of spectrum licenses may not agree to the Consolidated Statements of Comprehensive Income primarily due to certain routine operating activities, such as routine spectrum license exchanges that would be expected to reoccur, and are therefore included in Adjusted EBITDA. Other, net may not agree to the Consolidated Statements of Comprehensive Income primarily due to certain non-routine operating activities, such as other special items that would not be expected to reoccur, and are therefore excluded in Adjusted EBITDA.

Adjusted EBITDA increased \$3.0 billion, or 41%, in 2016 primarily from:

- Increased branded postpaid and prepaid service revenues primarily due to strong customer response to our Un-carrier initiatives and the ongoing success of our promotional activities;
- Higher gains on disposal of spectrum licenses of \$672 million; gains on disposal were \$835 million in 2016 compared to \$163 million in 2015;
- Lower losses on equipment in 2016 primarily due to an increase in lease revenues resulting from the launch of our JUMP! On Demand program at the end of the second quarter of 2015. Additionally, the costs of leased devices, which are capitalized and depreciated over the lease term, are excluded from Adjusted EBITDA. In connection with JUMP! On Demand, we had lease revenues of \$1.4 billion in 2016, and depreciation expense of \$1.5 billion related to leased wireless devices in 2016; and
- Focused cost control and synergies realized from the MetroPCS business combination, primarily in cost of services; partially

offset by

Table of Contents

- Higher selling, general and administrative expenses primarily due to strategic investments to support our growing customer base, including higher employee-related costs, higher commissions driven by an increase in branded customer additions and higher promotional costs.

We are making an accounting change in 2017 to include imputed interest associated with EIP receivables in Other revenues in our Consolidated Statements of Comprehensive Income, which will be included in Adjusted EBITDA. The impact from this accounting change is expected to be approximately \$0.2 to \$0.3 billion in 2017.

Adjusted EBITDA increased \$1.8 billion, or 31%, in 2015 primarily from:

- Increased branded postpaid and prepaid revenues driven by strong customer response to our Un-carrier initiatives and the ongoing success of our promotional activities;
- Focused cost control and synergies realized from the MetroPCS business combination, especially in cost of services;
- Lower losses on equipment in 2015 primarily due to an increase in lease revenues, which are recognized over the lease term, resulting from the launch of our JUMP! On Demand at the end of the second quarter of 2015. Additionally, the costs of leased devices, which are capitalized and depreciated over the lease term, are excluded from Adjusted EBITDA. In connection with JUMP! On Demand, we had lease revenues of \$224 million in 2015, and depreciation expense of \$312 million related to leased wireless devices in 2015; partially offset by
- Higher selling, general and administrative expenses.

**Liquidity and Capital Resources**

Our principal sources of liquidity are our cash and cash equivalents and cash generated from operations, proceeds from issuance of long-term debt, capital leases, common and preferred stock, the sale of certain receivables, financing arrangements of vendor payables which effectively extend payment terms and an unsecured revolving credit facility with Deutsche Telekom.

**Cash Flows**

The following is an analysis of our year-to-date cash flows:

(in millions)	Year Ended December 31,			2016 Versus 2015		2017 Versus 2014	
	2016	2015	2014	\$ Change	% Change	\$ Change	% Change
Net cash provided by operating activities	\$ 6,135	\$ 5,414	\$ 4,146	\$ 721	13 %	\$ 1,268	31%
Net cash used in investing activities	(5,680)	(9,560)	(7,246)	3,880	(41)%	(2,314)	32%
Net cash provided by financing activities	463	3,413	2,524	(2,950)	(86)%	889	35%

**Operating Activities**

Cash provided by operating activities increased \$721 million, or 13%, in 2016 primarily from:

- \$727 million increase in Net income;
- \$1.4 billion increase in net non-cash income and expenses included in Net income primarily due to changes in Depreciation and amortization, Deferred income tax expense and Gains on disposal of spectrum licenses; partially offset by
- \$1.4 billion increase in net cash outflows from changes in working capital primarily due to changes in Accounts payable and accrued liabilities of \$1.9 billion as well as the change in Equipment installment plan receivables, including inflows from the sale of certain EIP receivables, partially offset by the change in Inventories. Net cash used for Accounts payable and accrued liabilities was \$1.2 billion in 2016 as compared to net cash provided by Accounts payable and accrued liabilities of \$693 million in 2015. Net cash proceeds from the sale of EIP and service receivables was \$536 million in 2016 as compared to \$884 million in 2015.

Cash provided by operating activities increased \$1.3 billion, or 31%, in 2015 primarily from:

- \$486 million increase in Net income;
- \$1.3 billion increase in net non-cash income and expenses included in Net income primarily due to changes in Depreciation and amortization, Gains on disposal of spectrum licenses and Deferred income tax expense; partially offset by



Table of Contents

- \$509 million increase in net cash outflows from changes in working capital primarily due to changes in Inventories, Accounts payable and accrued liabilities, and Equipment installment plan receivables, including inflows from the sale of certain EIP receivables.

**Investing Activities**

Cash used in investing activities decreased \$3.9 billion, or 41%, in 2016, to a use of \$5.7 billion primarily from:

- \$4.7 billion for Purchases of property and equipment, including capitalized interest of \$142 million primarily related to the build out of our 4G LTE network;
- \$4.0 billion for Purchases of spectrum licenses and other intangible assets, including a \$2.2 billion deposit made to a third party in connection with a potential asset purchase; partially offset by
- \$3.0 billion in Sales of short-term investments.

Cash used in investing activities increased \$2.3 billion, or 32%, in 2015, to a use of \$9.6 billion primarily from:

- \$4.7 billion for Purchases of property and equipment, including capitalized interest of \$246 million primarily related to the build out of our 4G LTE network;
- \$1.9 billion for Purchases of spectrum licenses and other intangible assets and
- \$3.0 billion in Purchases of short-term investments.

**Financing Activities**

Cash provided by financing activities decreased \$3.0 billion, or 86%, in 2016 to an inflow of \$463 million primarily from:

- \$997 million Proceeds from issuance of long-term debt; partially offset by
- \$205 million for Repayments of capital lease obligations;
- \$150 million for Repayments of short-term debt for purchases of inventory, property and equipment, net; and
- \$121 million for Tax withholdings on share-based awards.

Cash provided by financing activities increased \$889 million, or 35%, in 2015 to inflow of \$3.4 billion primarily from:

- \$4.0 billion Proceeds from issuance of long-term debt; partially offset by
- \$564 million for Repayments of short-term debt for purchases of inventory, property and equipment, net.

**Cash and Cash Equivalents**

As of December 31, 2016, our Cash and cash equivalents were \$5.5 billion.

**Free Cash Flow**

Free Cash Flow represents net cash provided by operating activities less payments for purchases of property and equipment. Free Cash Flow is a non-GAAP financial measure utilized by our management, investors and analysts of T-Mobile's financial information to evaluate cash available to pay debt and provide further investment in the business.

The following table illustrates the calculation of Free Cash Flow and reconciles Free Cash Flow to Net cash provided by operating activities, which we consider to be the most directly comparable GAAP financial measure:

(in millions)	Year Ended December 31,			2016 Versus 2015		2015 Versus 2014	
	2016	2015	2014	\$ Change	% Change	\$ Change	% Change
Net cash provided by operating activities	\$ 6,135	\$ 5,414	\$ 4,146	\$ 721	13 %	\$ 1,268	31 %
Cash purchases of property and equipment	(4,702)	(4,724)	(4,317)	22	— %	(407)	9 %
Free Cash Flow	\$ 1,433	\$ 690	\$ (171)	\$ 743	108 %	\$ 861	(504)%



Table of Contents

Free Cash Flow increased \$743 million in 2016 and increased \$861 million for 2015 primarily from:

- Higher net cash provided by operating activities, as described above; and
- Lower purchases of property and equipment from the build-out of our 4G LTE network in 2016, as described above. In 2015, purchases of property and equipment were higher compared to 2014 from the build-out of our 4G LTE network, as described above. Cash purchases of property and equipment includes capitalized interest of \$142 million, \$246 million and \$64 million for 2016, 2015 and 2014, respectively.

**Debt**

As of December 31, 2016, our total debt was \$27.8 billion, excluding our tower obligations, of which \$27.4 billion was classified as long-term debt. Significant debt-related activity during 2016 included:

- In March 2016, T-Mobile USA, a subsidiary of T-Mobile US, Inc., and certain of its affiliates, as guarantors, entered into a purchase agreement with Deutsche Telekom AG (“Deutsche Telekom”), our majority stockholder, under which T-Mobile USA may, at its option, issue and sell to Deutsche Telekom \$2.0 billion of 5.300% Senior Notes due 2021 (the “5.300% Senior Notes”) for an aggregate purchase price of \$2.0 billion. As amended in October 2016, if T-Mobile USA does not elect to issue the 5.300% Senior Notes on or prior to May 5, 2017, the commitment under the purchase agreement terminates and T-Mobile USA must reimburse Deutsche Telekom for the cost of its hedging arrangements (if any) related to the transaction. In addition, T-Mobile USA is required to reimburse Deutsche Telekom for its cost of hedging arrangements related to the extension for the duration of the extended commitments.
- In April 2016, T-Mobile USA issued \$1.0 billion of public 6.000% Senior Notes due 2024.
- In April 2016, T-Mobile USA entered into a purchase agreement with Deutsche Telekom, under which T-Mobile USA may, at its option, issue and sell to Deutsche Telekom up to \$1.35 billion of 6.000% Senior Notes due 2024 and (iii) entered into another purchase agreement with Deutsche Telekom, under which T-Mobile USA may, at its option, issue and sell to Deutsche Telekom up to an additional \$650 million of 6.000% Senior Notes due 2024.
- The purchase price for the 6.000% Senior Notes that may be issued under the \$1.35 billion purchase agreement will be approximately 103.316% of the outstanding principal balance of the notes issued. As amended in October 2016, if T-Mobile USA does not elect to issue the 6.000% Senior Notes under the \$1.35 billion purchase agreement on or prior to May 5, 2017 or elects to issue less than \$1.35 billion of 6.000% Senior Notes, any unused portion of the commitment under the purchase agreement terminates and T-Mobile USA must reimburse Deutsche Telekom for the cost of its hedging arrangements (if any) related to the transaction. In addition, T-Mobile USA is required to reimburse Deutsche Telekom for its cost of hedging arrangements related to the extension for the duration of the extended commitments.
- In April 2016, T-Mobile USA entered into another purchase agreement with Deutsche Telekom, in which T-Mobile USA may, at its option, issue and sell to Deutsche Telekom up to an additional \$650 million of 6.000% Senior Notes due 2024. The purchase price for the 6.000% Senior Notes that may be issued under the \$650 million purchase agreement will be approximately 104.047% of the outstanding principal balance of the notes issued. As amended in October 2016, if T-Mobile USA does not elect to issue the 6.000% Senior Notes under the \$650 million purchase agreement on or prior to May 5, 2017 or elects to issue less than \$650 million Senior Notes, any unused portion of the commitment under the purchase agreement terminates and T-Mobile USA must reimburse Deutsche Telekom for the cost of its hedging arrangements (if any) related to the transaction. In addition, T-Mobile USA is required to reimburse Deutsche Telekom for its cost of hedging arrangements related to the extension for the duration of the extended commitments.
- We have entered into uncommitted capital lease facilities with certain partners, which provide us with the ability to enter into capital leases for network equipment and services. As of December 31, 2016, we have committed to \$1.3 billion of capital leases under these capital lease facilities, of which \$799 million was executed during the year ended December 31, 2016. We expect to enter into up to an additional \$900 million in capital lease commitments during 2017.
- In December 2016, we terminated our \$500 million unsecured revolving credit facility with Deutsche Telekom. In addition, T-Mobile USA entered into a \$2.5 billion revolving credit facility with Deutsche Telekom which comprised of (i) a three-year \$1.0 billion senior unsecured revolving credit agreement and (ii) a three-year \$1.5 billion senior

Table of Contents

secured revolving credit agreement. As of December 31, 2016, there were no outstanding borrowings under the revolving credit facility.

- In January 2017, T-Mobile USA borrowed \$4.0 billion under a secured term loan facility (“Incremental Term Loan Facility”) with Deutsche Telekom to refinance \$1.98 billion of outstanding secured term loans under its Term Loan Credit Agreement dated November 9, 2015, with the remaining net proceeds from the transaction intended to be used to redeem callable high yield debt. The loans under the Incremental Term Loan Facility were drawn in two tranches on January 31, 2017 (i) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.00% and will mature on November 9, 2022 and (ii) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.25% and will mature on January 31, 2024. The Incremental Term Loan Facility increases Deutsche Telekom’s incremental term loan commitment provided to T-Mobile USA under that certain First Incremental Facility Amendment dated as of December 29, 2016 from \$660 million to \$2.0 billion and provides to T-Mobile USA an additional \$2.0 billion incremental term loan commitment. See Note 14 – Subsequent Events of the Notes to the Consolidated Financial Statements for further information.

See Note 7 – Debt of the Notes to the Consolidated Financial Statements for additional details.

We could seek additional sources of liquidity, including through the issuance of additional long-term debt in 2017, to continue to opportunistically acquire spectrum licenses in private party transactions and future FCC spectrum license auctions or for the refinancing of existing long-term debt on an opportunistic basis. Excluding liquidity that could be needed for spectrum acquisitions, we expect our principal sources of funding to be sufficient to meet our anticipated liquidity needs for business operations for the next 12 months. Our intended use of any such funds is for general corporate purposes, including for capital expenditures and redemption of high yield callable debt.

We determine future liquidity requirements, for both operations and capital expenditures, based in large part upon projected financial and operating performance, and opportunities to acquire additional spectrum. We regularly review and update these projections for changes in current and projected financial and operating results, general economic conditions, the competitive landscape and other factors. There are a number of risks and uncertainties that could cause our financial and operating results and capital requirements to differ materially from our projections, which could cause future liquidity to differ materially from our assessment.

The indentures and credit facilities governing our long-term debt to affiliates and third parties, excluding capital leases, contain covenants that, among other things, limit the ability of the Issuer and the Guarantor Subsidiaries to: incur more debt; pay dividends and make distributions on our common stock; make certain investments; repurchase stock; create liens or other encumbrances; enter into transactions with affiliates; enter into transactions that restrict dividends or distributions from subsidiaries; and merge, consolidate, or sell, or otherwise dispose of, substantially all of their assets. Certain provisions of each of the credit facilities, indentures and supplemental indentures relating to the long-term debt to affiliates and third parties restrict the ability of the Issuer to loan funds or make payments to the Parent. However, the Issuer is allowed to make certain permitted payments to the Parent under the terms of each of the credit facilities, indentures and supplemental indentures relating to the long-term debt to affiliates and third parties. We were in compliance with all restrictive debt covenants as of December 31, 2016.

### *Capital Expenditures*

Our liquidity requirements have been driven primarily by capital expenditures for spectrum licenses and the construction, expansion and upgrading of our network infrastructure. Property and equipment capital expenditures primarily relate to our network transformation, including the build out of 700 MHz A-Block spectrum licenses. We expect cash capital expenditures for property and equipment to be in the range of \$4.8 billion to \$5.1 billion in 2017, excluding capitalized interest. This does not include property and equipment obtained through capital lease agreements, leased wireless devices transferred from inventory or purchases of spectrum licenses. Similar to 2016, cash capital expenditures will be front-end loaded in 2017 due to the completion of the 700 MHz A-Block build-out.

In particular, we are participating in the FCC broadcast incentive auction of low-band 600 MHz spectrum licenses that is currently in-progress. If we win spectrum in the auction, we may incur substantial additional expenditures for the purchase price and to gain access to such spectrum. Any such amounts would be funded primarily through cash on hand and borrowings. As a result, our level of debt could increase.

Table of Contents**Contractual Obligations**

The following table summarizes our contractual obligations and borrowings as of December 31, 2016 and the timing and effect that such commitments are expected to have on our liquidity and capital requirements in future periods:

(in millions)	Less Than 1 Year	1 - 3 Years	4 - 5 Years	More Than 5 Years	Total
Long-term debt <sup>(1)</sup>	\$ 20	\$ 3,040	\$ 7,790	\$ 15,330	\$ 26,180
Interest on long-term debt	1,679	3,270	2,568	1,925	9,442
Capital lease obligations, including interest	390	669	350	214	1,623
Tower obligations <sup>(2)</sup>	184	368	370	1,164	2,086
Operating leases <sup>(3)</sup>	2,417	3,950	2,613	2,188	11,168
Purchase obligations <sup>(4)</sup>	2,011	1,818	1,330	960	6,119
Network decommissioning <sup>(5)</sup>	112	176	83	48	419
Total contractual obligations	\$ 6,813	\$ 13,291	\$ 15,104	\$ 21,829	\$ 57,037

- (1) Represents principal amounts of long-term debt to affiliates and third parties at maturity, excluding unamortized premium from purchase price allocation fair value adjustment, capital lease obligations and vendor financing arrangements. See Note 7 – Debt of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for further information.
- (2) Future minimum payments, including principal and interest payments and imputed lease rental income, related to the tower obligations. See Note 8 – Tower Obligations of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for further information.
- (3) As of December 31, 2016, we have updated the future minimum lease payments for all cell site leases presented above to include only payments due for the initial non-cancelable lease term only as they represent the payments which we cannot avoid at our option and also corresponds to our lease term assessment for new leases. This update had the effect of reducing our operating lease commitments included in the table above by \$4.6 billion as of December 31, 2016. See Note 12 – Commitments and Contingencies of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for further information.
- (4) T-Mobile calculated the minimum obligation for certain agreements to purchase goods or services based on termination fees that can be paid to exit the contract. Termination penalties are included in the above table as payments due in less than one year, as this is the earliest T-Mobile could exit these contracts. For certain contracts that include fixed volume purchase commitments and fixed prices for various products, the purchase obligations are calculated using fixed volumes and contractually fixed prices for the products that are expected to be purchased. This table does not include open purchase orders as of December 31, 2016 under normal business purposes. See Note 12 – Commitments and Contingencies of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for further information.
- (5) Represents future undiscounted cash flows related to decommissioned MetroPCS CDMA network and certain other redundant cell sites as of December 31, 2016.

Certain commitments and obligations are included in the table based on the year of required payment or an estimate of the year of payment. Other long-term liabilities, excluding network decommissioning, have been omitted from the table above due to the uncertainty of the timing of payments, combined with the absence of historical trending to be used as a predictor of such payments. In addition, because dividends on preferred stock are subject to approval by our Board of Directors, amounts are not included in the preceding table unless such authorization has occurred and the dividend has not been paid. See Note 13 – Additional Financial Information of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for further information.

The purchase obligations reflected in the table above are primarily commitments to purchase handsets and accessories, equipment, software, programming and network services, and marketing activities, which will be used or sold in the ordinary course of business. These amounts do not represent T-Mobile's entire anticipated purchases in the future, but represent only those items for which T-Mobile is contractually committed. Where T-Mobile is committed to make a minimum payment to the supplier regardless of whether it takes delivery, T-Mobile has included only that minimum payment as a purchase obligation. Additionally, included within purchase obligations are amounts for the acquisition of spectrum licenses, which are subject to regulatory approval and other customary closing conditions.

**Off-Balance Sheet Arrangements**

In 2015, we entered into an arrangement, as amended, to sell certain EIP accounts receivable on a revolving basis through November 2017 as an additional source of liquidity. In June 2016, the arrangement was amended to increase the maximum funding commitment to \$1.3 billion with a scheduled expiration date in November 2017. In 2014, we entered into an arrangement, as amended, to sell certain service accounts receivable on a revolving basis through March 2017 as an additional source of liquidity. In November 2016, the arrangement was amended to increase the maximum funding commitment to \$950 million with a scheduled expiration date in March 2018. As of December 31, 2016, T-Mobile derecognized net receivables of \$2.5 billion upon sale through these arrangements. See Note 3 – Sales of Certain Receivables of the Notes to the Consolidated Financial Statements.

Table of Contents**Related-Party Transactions**

In March 2016, T-Mobile USA entered into a purchase agreement with Deutsche Telekom under which T-Mobile USA may, at its option, issue and sell to Deutsche Telekom \$2.0 billion of 5.300% Senior Notes due 2021 for an aggregate purchase price of \$2.0 billion.

In April 2016, T-Mobile USA entered into a purchase agreement with Deutsche Telekom under which T-Mobile USA may, at its option, issue and sell to Deutsche Telekom up to \$1.35 billion of 6.000% Senior Notes due 2024. The purchase price for the 6.000% Senior Notes that may be issued under the \$1.35 billion purchase agreement will be approximately 103.316% of the outstanding principal balance of the notes issued.

In April 2016, T-Mobile USA entered into a purchase agreement with Deutsche Telekom under which T-Mobile USA may, at its option, issue and sell to Deutsche Telekom up to \$650 million of 6.000% Senior Notes due 2024. The purchase price for the 6.000% Senior Notes that may be issued under the \$650 million purchase agreement will be approximately 104.047% of the outstanding principal balance of the notes issued.

The purchase agreements were amended in October 2016, see Note 7 – Debt of the Notes to the Consolidated Financial Statements.

In December 2016, we terminated our \$500 million unsecured revolving credit facility with Deutsche Telekom. In addition, T-Mobile USA entered into a \$2.5 billion revolving credit facility with Deutsche Telekom which comprised of (i) a three-year \$1.0 billion senior unsecured revolving credit agreement and (ii) a three-year \$1.5 billion senior secured revolving credit agreement. As of December 31, 2016, there were no outstanding borrowings under the revolving credit facility.

In January 2017, T-Mobile USA borrowed \$4.0 billion under a secured term loan facility (“Incremental Term Loan Facility”) with Deutsche Telekom to refinance \$1.98 billion of outstanding secured term loans under its Term Loan Credit Agreement dated November 9, 2015, with the remaining net proceeds from the transaction intended to be used to redeem callable high yield debt. The loans under the Incremental Term Loan Facility were drawn in two tranches on January 31, 2017 (i) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.00% and will mature on November 9, 2022 and (ii) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.25% and will mature on January 31, 2024. The Incremental Term Loan Facility increases Deutsche Telekom’s incremental term loan commitment provided to T-Mobile USA under that certain First Incremental Facility Amendment dated as of December 29, 2016 from \$660 million to \$2.0 billion and provides to T-Mobile USA an additional \$2.0 billion incremental term loan commitment. See Note 14 – Subsequent Events of the Notes to the Consolidated Financial Statements for further information.

We also have related party transactions associated with Deutsche Telekom or its affiliates in the ordinary course of business, including intercompany servicing and licensing. See Note 13 – Additional Financial Information of the Notes to the Consolidated Financial Statements.

***Disclosure of Iranian Activities under Section 13(r) of the Securities Exchange Act of 1934***

Section 219 of the Iran Threat Reduction and Syria Human Rights Act of 2012 added Section 13(r) to the Exchange Act of 1934, as amended (“Exchange Act”). Section 13(r) requires an issuer to disclose in its annual or quarterly reports, as applicable, whether it or any of its affiliates knowingly engaged in certain activities, transactions or dealings relating to Iran or with designated natural persons or entities involved in terrorism or the proliferation of weapons of mass destruction. Disclosure is required even where the activities, transactions or dealings are conducted outside the U.S. by non-U.S. affiliates in compliance with applicable law, and whether or not the activities are sanctionable under U.S. law.

As of the date of this report, we are not aware of any activity, transaction or dealing by us or any of our affiliates in 2016 that requires disclosure in this report under Section 13(r) of the Exchange Act, except as set forth below with respect to affiliates that we do not control and that are our affiliates solely due to their common control with Deutsche Telekom. We have relied upon Deutsche Telekom for information regarding their activities, transactions and dealings.

Deutsche Telekom, through certain of its non-U.S. subsidiaries, is party to roaming and interconnect agreements with the following mobile and fixed line telecommunication providers in Iran, some of which are or may be government-controlled entities: Gostaresh Ertebatat Taliya, Irancell Telecommunications Services Company (“MTN Irancell”), Telecommunication Kish Company, Mobile Telecommunication Company of Iran, and Telecommunication Infrastructure Company of Iran. In

Table of Contents

2016, gross revenues of all Deutsche Telekom affiliates generated by roaming and interconnection traffic with Iran were less than \$1.0 million and estimated net profits were less than \$1.0 million.

In addition, Deutsche Telekom, through certain of its non-U.S. subsidiaries, operating a fixed line network in their respective European home countries (in particular Germany), provides telecommunications services in the ordinary course of business to the Embassy of Iran in those European countries. Gross revenues and net profits recorded from these activities in 2016 were less than \$0.1 million. We understand that Deutsche Telekom intends to continue these activities.

**Critical Accounting Policies and Estimates**

Our significant accounting policies are fundamental to understanding our financial condition and results as they require the use of estimates and assumptions which affect the financial statements and accompanying notes. See Note 1 – Summary of Significant Accounting Policies of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for further information.

These policies are critical because they require management to make difficult, subjective and complex judgments about matters that are inherently uncertain. These estimates are inherently subject to judgment and actual results could differ from those estimates.

**Allowances**

We maintain an allowance for estimated losses inherent in the accounts receivable and EIP receivable portfolios. When determining the allowance, we consider a number of factors, including historical experience and current collection trends, aging of the receivable portfolio, credit quality of the customer base and other qualitative factors such as macro-economic conditions.

Credit collection risks are assessed for each type of receivable, such as EIP receivables, based upon historical and expected write-offs, net of recoveries, and an analysis of the aged receivable balances with reserves generally increasing as the receivable ages. To the extent that actual loss experience differs significantly from historical trends or assumptions, the required allowance amounts could differ from the estimate. We write off account balances if collection efforts are unsuccessful and the receivable balance is deemed uncollectible, based on customer credit ratings and the length of time from the original billing date.

We offer certain retail customers the option to pay for their devices and other purchases in installments over a period of up to 24 months using an EIP. At the time of an installment sale, we impute a discount for interest as there is no stated rate of interest on the EIP receivables and record the EIP receivables at their present value, which is determined by discounting future payments at the imputed interest rate. The difference between the present value of the EIP receivables and their face amount results in a discount which is recorded as a direct reduction to the carrying value with a corresponding reduction to equipment revenues. We determine the imputed discount rate based primarily on current market interest rates and the amount of expected credit losses on the EIP receivables. As a result, we do not recognize a separate valuation allowance at the time of issuance as the effects of uncertainty about future cash flows are included in the initial present value measurement of the receivable. The imputed discount on EIP receivables is amortized over the financed installment term using the effective interest method and recognized as Interest income in our Consolidated Statements of Comprehensive Income.

Subsequent to the initial determination of the imputed discount, we assess the need for and, if necessary, recognize an allowance for credit losses to the extent the amount of estimated probable losses on the gross EIP receivables exceed the remaining unamortized imputed discount balances.

Total imputed discount and allowances as of December 31, 2016 and 2015 was approximately 8.0% and 8.2%, respectively, of the total amount of gross accounts receivable, including EIP receivables.

**Depreciation**

Depreciation commences once assets have been placed in service. We generally depreciate property and equipment over the period the property and equipment provide economic benefit. Leased wireless devices are depreciated to their estimated residual value over the period expected to provide utility to T-Mobile, which is generally the lease term. Depreciable life studies are performed periodically to confirm the appropriateness of depreciable lives for certain categories of property, plant and equipment. These studies take into account actual usage, physical wear and tear, replacement history, assumptions about technology evolution and expected loss of leased wireless devices. When these factors indicate that an asset's useful life is different from the previous assessment, the remaining book values are depreciated prospectively over the adjusted remaining



## Table of Contents

estimated useful life. See Note 1 – Summary of Significant Accounting Policies and Note 4 – Property and Equipment of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for information regarding depreciation of assets, including management’s underlying estimates of useful lives.

### *Evaluation of Goodwill and Indefinite-Lived Intangible Assets for Impairment*

We assess the carrying value of goodwill and other indefinite-lived intangible assets, such as our spectrum licenses, for potential impairment annually as of December 31 or more frequently if events or changes in circumstances indicate that assets might be impaired.

We may elect to first perform a qualitative assessment to determine whether it is more likely than not the fair value of the single reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. If we do not perform a qualitative assessment, or if the qualitative assessment indicates it is more likely than not the fair value of the single reporting unit is less than its carrying amount, goodwill is tested for impairment based on a two-step test. In the first step, we compare the fair value of the reporting unit to its carrying value. The fair value of the reporting unit is determined using a market approach, which is based on market capitalization. We recognize market capitalization is subject to volatility and will monitor changes in market capitalization to determine whether declines, if any, necessitate an interim impairment review. In the event market capitalization does decline below its book value, we will consider the length, severity and reasons for the decline when assessing whether potential impairment exists, including considering whether a control premium should be added to the market capitalization. We believe short-term fluctuations in share price may not necessarily reflect the underlying aggregate fair value.

In the second step, we determine the fair values of all of the assets and liabilities of the reporting unit, including those that currently may not be recorded. The excess of the fair value of the reporting unit over the sum of the fair value of all of those assets and liabilities represents the implied goodwill amount. If the implied fair value of goodwill is lower than the carrying amount of goodwill, then an impairment loss is recognized for the difference.

We test spectrum licenses for impairment on an aggregate basis, consistent with the management of the overall business at a national level. We may elect to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of an intangible asset group is less than its carrying value. If we do not perform the qualitative assessment, or if the qualitative assessment indicates it is more likely than not the fair value of the intangible asset group is less than its carrying amount, we calculate the estimated fair value of the intangible asset group. If the carrying amount of spectrum licenses exceeds the fair value, an impairment loss is recognized. We estimate the fair value of the spectrum licenses using the Greenfield approach, which is an income approach that estimates the price at which an orderly transaction to sell the asset would take place between market participants at the measurement date under current market conditions. The Greenfield approach values the spectrum licenses by calculating the cash flow generating potential of a hypothetical start-up company that goes into business with no assets except the asset to be valued (in this case, spectrum licenses). The value of the spectrum licenses can be considered as equal to the present value of the cash flows of this hypothetical start-up company. We base the assumptions underlying the Greenfield approach on a combination of market participant data and our historical results, trends and business plans. Future cash flows in the Greenfield approach are based on estimates and assumptions of market participant revenues, EBITDA margin, network build-out period and a long-term growth rate for a market participant. The cash flows are discounted using a weighted average cost of capital.

The valuation approaches utilized to estimate fair value for the purposes of the impairment tests of goodwill and spectrum licenses require the use of assumptions and estimates, which involve a degree of uncertainty. If actual results or future expectations are not consistent with the assumptions, this may result in the recording of significant impairment charges on goodwill or spectrum licenses. The most significant assumptions within the valuation models are the discount rate, revenues, EBITDA margins and the long-term growth rate. See Note 1 – Summary of Significant Accounting Policies and Note 5 – Goodwill, Spectrum Licenses and Other Intangible Assets of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for information regarding our annual impairment test and impairment charges.

### *Guarantee Liabilities*

In 2013, we introduced a device trade-in program, Just Upgrade My Phone (“JUMP!”), which provides eligible customers a specified-price trade-in right to upgrade their device. Participating customers must finance the purchase of a device on an EIP and have a qualifying T-Mobile monthly wireless service plan, which is treated as a single multiple-element arrangement when entered into at or near the same time. Upon qualifying JUMP! program upgrades, the customers’ remaining EIP balance is settled provided they trade-in their eligible used device in good working condition and purchase a new device from us on a new EIP.

Table of Contents

For customers who enroll in JUMP!, we defer and recognize a liability, for the portion of revenue which represents the estimated fair value of the specified-price trade-in right guarantee. The guarantee liability is valued based on various economic and customer behavioral assumptions, which requires judgment, including estimating the customer's remaining EIP balance at trade-in, the expected fair value of the used device at trade-in, and the probability and timing of trade-in. When customers upgrade their device, the difference between the EIP balance credit to the customer and the fair value of the returned device is recorded against the guarantee liabilities. All assumptions are reviewed periodically.

***Rent Expense***

Most of the leases on our tower sites have fixed rent escalations which provide for periodic increases in the amount of rent payable over time. We calculate straight-line rent expense for each of these leases based on the fixed non-cancellable term of the lease plus all periods, if any, for which failure to renew the lease imposes a penalty on us in such amount that a renewal appears, at lease inception or significant modification, to be reasonably assured. We consider several factors in assessing whether renewal periods are reasonably assured of being exercised, including the continued maturation of our network nationwide, technological advances within the telecommunications industry and the availability of alternative sites. We make significant assumptions at lease inception in determining and assessing the factors that constitute a "penalty." In doing so, we primarily consider costs incurred in acquiring and developing new sites, the useful life of site improvements and equipment costs, future economic conditions and the extent to which improvements in wireless technologies can be incorporated into a current assessment of whether an economic compulsion will exist in the future to renew a lease.

***Income Taxes***

We recognize deferred tax assets and liabilities based on temporary differences between the financial statement and tax basis of assets and liabilities using enacted tax rates expected to be in effect when these differences are realized. A valuation allowance is maintained against deferred tax assets when it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of a deferred tax asset depends on the ability to generate sufficient taxable income of the appropriate character and in the appropriate taxing jurisdictions within the carryforward periods available. We consider many factors when determining whether a valuation allowance is needed, including recent cumulative earnings experience by taxing jurisdiction, expectations of future income, the carryforward periods available for tax reporting purposes and other relevant factors.

We account for uncertainty in income taxes recognized in the financial statements in accordance with the accounting guidance on the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. We assess whether it is more likely than not that a tax position will be sustained upon examination based on the technical merits of the position and adjust the unrecognized tax benefits in light of changes in facts and circumstances, such as changes in tax law, interactions with taxing authorities and developments in case law.

**Accounting Pronouncements Not Yet Adopted**

See Note 1 – Summary of Significant Accounting Policies of the Notes to the Consolidated Financial Statements included in Part II, Item 8 of this Form 10-K for information regarding recently issued accounting standards.

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to economic risks in the normal course of business, primarily from changes in interest rates. These risks, along with other business risks, impact our cost of capital. Our policy is to manage exposure related to fluctuations in interest rates in order to manage capital costs, control financial risks and maintain financial flexibility over the long term. We have established interest rate risk limits that are closely monitored by measuring interest rate sensitivities of our debt portfolio. We do not foresee significant changes in the strategies used to manage market risk in the near future.

Table of Contents

To perform the sensitivity analysis, we assessed the risk of a change in the fair value from the effect of a hypothetical interest rate change of positive 150 and negative 50 basis points. As of December 31, 2016, the change in the fair value of our Senior Secured Term Loans, based on this hypothetical change, is shown in the table below:

(in millions)	Carrying Amount		Fair Value	Fair Value Assuming				
				+150 Basis Point Shift	-50 Basis Point Shift			
Senior Secured Term Loans	\$	1,980	\$	2,005	\$	1,864	\$	2,055

Table of Contents**Item 8. Financial Statements and Supplementary Data****Financial Statements****Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders of T-Mobile US, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of comprehensive income, of stockholders' equity and of cash flows present fairly, in all material respects, the financial position of T-Mobile US, Inc. and its subsidiaries at December 31, 2016 and December 31, 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Annual Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP  
Seattle, Washington  
February 14, 2017

Table of Contents

**T-Mobile US, Inc.**  
**Consolidated Balance Sheets**

(in millions, except share and per share amounts)	December 31, 2016	December 31, 2015
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 5,500	\$ 4,582
Short-term investments	—	2,998
Accounts receivable, net of allowances of \$102 and \$116	1,896	1,788
Equipment installment plan receivables, net	1,930	2,378
Accounts receivable from affiliates	40	36
Inventories	1,111	1,295
Asset purchase deposit	2,203	—
Other current assets	1,537	1,813
Total current assets	14,217	14,890
Property and equipment, net	20,943	20,000
Goodwill	1,683	1,683
Spectrum licenses	27,014	23,955
Other intangible assets, net	376	594
Equipment installment plan receivables due after one year, net	984	847
Other assets	674	444
Total assets	\$ 65,891	\$ 62,413
<b>Liabilities and Stockholders' Equity</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	\$ 7,152	\$ 8,084
Payables to affiliates	125	135
Short-term debt	354	182
Deferred revenue	986	717
Other current liabilities	405	410
Total current liabilities	9,022	9,528
Long-term debt	21,832	20,461
Long-term debt to affiliates	5,600	5,600
Tower obligations	2,621	2,658
Deferred tax liabilities	4,938	4,061
Deferred rent expense	2,616	2,481
Other long-term liabilities	1,026	1,067
Total long-term liabilities	38,633	36,328
Commitments and contingencies (Note 12)		
<b>Stockholders' equity</b>		
5.50% Mandatory Convertible Preferred Stock Series A, par value \$0.00001 per share, 100,000,000 shares authorized; 20,000,000 and 20,000,000 shares issued and outstanding; \$1,000 and \$1,000 aggregate liquidation value	—	—
Common Stock, par value \$0.00001 per share, 1,000,000,000 shares authorized; 827,768,818 and 819,773,724 shares issued, 826,357,331 and 818,391,219 shares outstanding	—	—
Additional paid-in capital	38,846	38,666
Treasury stock, at cost, 1,411,487 and 1,382,505 shares issued	(1)	—
Accumulated other comprehensive income (loss)	1	(1)
Accumulated deficit	(20,610)	(22,108)
Total stockholders' equity	18,236	16,557

Total liabilities and stockholders' equity

\$ 65,891 \$ 62,413

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

Table of Contents

**T-Mobile US, Inc.**  
**Consolidated Statements of Comprehensive Income**

Year Ended December 31,

(in millions, except share and per share amounts)

	2016	2015	2014
<b>Revenues</b>			
Branded postpaid revenues	\$ 18,138	\$ 16,383	\$ 14,392
Branded prepaid revenues	8,553	7,553	6,986
Wholesale revenues	903	692	731
Roaming and other service revenues	250	193	266
Total service revenues	27,844	24,821	22,375
Equipment revenues	8,727	6,718	6,789
Other revenues	671	514	400
Total revenues	37,242	32,053	29,564
<b>Operating expenses</b>			
Cost of services, exclusive of depreciation and amortization shown separately below	5,731	5,554	5,788
Cost of equipment sales	10,819	9,344	9,621
Selling, general and administrative	11,378	10,189	8,863
Depreciation and amortization	6,243	4,688	4,412
Cost of MetroPCS business combination	104	376	299
Gains on disposal of spectrum licenses	(835)	(163)	(840)
Other, net	—	—	5
Total operating expenses	33,440	29,988	28,148
Operating income	3,802	2,065	1,416
<b>Other income (expense)</b>			
Interest expense	(1,418)	(1,085)	(1,073)
Interest expense to affiliates	(312)	(411)	(278)
Interest income	261	420	359
Other expense, net	(6)	(11)	(11)
Total other expense, net	(1,475)	(1,087)	(1,003)
Income before income taxes	2,327	978	413
Income tax expense	(867)	(245)	(166)
Net income	1,460	733	247
Dividends on preferred stock	(55)	(55)	—
Net income attributable to common stockholders	\$ 1,405	\$ 678	\$ 247
Net income	\$ 1,460	\$ 733	\$ 247
<b>Other comprehensive income (loss), net of tax</b>			
Unrealized gain (loss) on available-for-sale securities, net of tax effect of \$1, \$(1) and \$(1)	2	(2)	(2)
Other comprehensive income (loss)	2	(2)	(2)
Total comprehensive income	\$ 1,462	\$ 731	\$ 245
<b>Earnings per share</b>			
Basic	\$ 1.71	\$ 0.83	\$ 0.31
Diluted	\$ 1.69	\$ 0.82	\$ 0.30
<b>Weighted average shares outstanding</b>			
Basic	822,470,275	812,994,028	805,284,712
Diluted	833,054,545	822,617,938	815,922,258

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

Table of Contents

**T-Mobile US, Inc.**  
**Consolidated Statements of Cash Flows**

(in millions)	Year Ended December 31,		
	2016	2015	2014
<b>Operating activities</b>			
Net income	\$ 1,460	\$ 733	\$ 247
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation and amortization	6,243	4,688	4,412
Stock-based compensation expense	235	201	196
Deferred income tax expense	914	256	122
Bad debt expense	477	547	444
Losses from sales of receivables	228	204	179
Deferred rent expense	121	167	225
Gains on disposal of spectrum licenses	(835)	(163)	(840)
Change in embedded derivatives	(25)	148	(18)
Changes in operating assets and liabilities			
Accounts receivable	(603)	(259)	(90)
Equipment installment plan receivables	97	1,089	(2,429)
Inventories	(802)	(2,495)	(499)
Deferred purchase price from sales of receivables	(270)	(185)	(204)
Other current and long-term assets	(133)	(217)	(328)
Accounts payable and accrued liabilities	(1,201)	693	2,395
Other current and long-term liabilities	158	22	312
Other, net	71	(15)	22
Net cash provided by operating activities	<u>6,135</u>	<u>5,414</u>	<u>4,146</u>
<b>Investing activities</b>			
Purchases of property and equipment, including capitalized interest of \$142, \$246 and \$64	(4,702)	(4,724)	(4,317)
Purchases of spectrum licenses and other intangible assets, including deposits	(3,968)	(1,935)	(2,900)
Purchases of short-term investments	—	(2,997)	—
Sales of short-term investments	2,998	—	—
Other, net	(8)	96	(29)
Net cash used in investing activities	<u>(5,680)</u>	<u>(9,560)</u>	<u>(7,246)</u>
<b>Financing activities</b>			
Proceeds from issuance of long-term debt	997	3,979	2,993
Proceeds from tower obligations	—	140	—
Repayments of capital lease obligations	(205)	(57)	(19)
Repayments of short-term debt for purchases of inventory, property and equipment, net	(150)	(564)	(418)
Repayments of long-term debt	(20)	—	(1,000)
Proceeds from exercise of stock options	29	47	27
Proceeds from issuance of preferred stock	—	—	982
Tax withholdings on share-based awards	(121)	(156)	(73)
Dividends on preferred stock	(55)	(55)	—
Other, net	(12)	79	32
Net cash provided by financing activities	<u>463</u>	<u>3,413</u>	<u>2,524</u>
Change in cash and cash equivalents	918	(733)	(576)
<b>Cash and cash equivalents</b>			
Beginning of period	<u>4,582</u>	<u>5,315</u>	<u>5,891</u>

End of period	\$	5,500	\$	4,582	\$	5,315
<b>Supplemental disclosure of cash flow information</b>						
Interest payments, net of amounts capitalized	\$	1,681	\$	1,298	\$	1,367
Income tax payments		25		54		36
Changes in accounts payable for purchases of property and equipment		285		46		402
Leased devices transferred from inventory to property and equipment		1,588		2,451		—
Returned leased devices transferred from property and equipment to inventory		(602)		(166)		—
Issuance of short-term debt for financing of property and equipment		150		500		256
Assets acquired under capital lease obligations		799		470		77

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

Table of Contents

**T-Mobile US, Inc.**  
**Consolidated Statement of Stockholders' Equity**

(in millions, except shares)	Preferred Stock Outstanding	Common Stock Outstanding	Treasury Stock at Cost	Par Value and Additional Paid-in Capital	Accumulated Other Comprehensive Income (loss)	Accumulated Debit	Total Stockholders' Equity
<b>Balance as of December 31, 2013</b>	—	801,879,804	\$ —	\$ 37,330	\$ 3	\$ (23,088)	\$ 14,245
Net income	—	—	—	—	—	247	247
Other comprehensive loss	—	—	—	—	(2)	—	(2)
Issuance of preferred stock	20,000,000	—	—	982	—	—	982
Stock-based compensation	—	—	—	196	—	—	196
Exercise of stock options	—	1,496,365	—	27	—	—	27
Issuance of vested restricted stock units	—	6,296,107	—	—	—	—	—
Shares withheld related to net share settlement of stock awards	—	(2,203,673)	—	(73)	—	—	(73)
Excess tax benefit from stock-based compensation	—	—	—	34	—	—	34
Other	—	—	—	7	—	—	7
<b>Balance as of December 31, 2014</b>	20,000,000	807,468,603	—	38,503	1	(22,841)	15,663
Net income	—	—	—	—	—	733	733
Other comprehensive loss	—	—	—	—	(2)	—	(2)
Stock-based compensation	—	—	—	227	—	—	227
Exercise of stock options	—	2,381,650	—	47	—	—	47
Stock issued for employee stock purchase plan	—	761,085	—	21	—	—	21
Issuance of vested restricted stock units	—	11,956,345	—	—	—	—	—
Shares withheld related to net share settlement of stock awards and stock options	—	(4,176,464)	—	(156)	—	—	(156)
Excess tax benefit from stock-based compensation	—	—	—	79	—	—	79
Dividends on preferred stock	—	—	—	(55)	—	—	(55)
<b>Balance as of December 31, 2015</b>	20,000,000	818,391,219	—	38,666	(1)	(22,108)	16,557
Net income	—	—	—	—	—	1,460	1,460
Other comprehensive income	—	—	—	—	2	—	2
Stock-based compensation	—	—	—	264	—	—	264
Exercise of stock options	—	982,904	—	29	—	—	29
Stock issued for employee stock purchase plan	—	1,905,534	—	63	—	—	63
Issuance of vested restricted stock units	—	7,712,463	—	—	—	—	—
Shares withheld related to net share settlement of stock awards and stock options	—	(2,605,807)	—	(122)	—	—	(122)
Transfer RSU to NQDC plan	—	(28,982)	(1)	1	—	—	—
Dividends on preferred stock	—	—	—	(55)	—	—	(55)
Prior year Retained Earnings (Note 1)	—	—	—	—	—	38	38
<b>Balance as of December 31, 2016</b>	20,000,000	826,357,331	\$ (1)	\$ 38,846	\$ 1	\$ (20,610)	\$ 18,236

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

Table of Contents

**T-Mobile US, Inc.**  
**Index for Notes to the Consolidated Financial Statements**

<u>Note 1</u>	<u>Summary of Significant Accounting Policies</u>	<u>54</u>
<u>Note 2</u>	<u>Equipment Installment Plan Receivables</u>	<u>63</u>
<u>Note 3</u>	<u>Sales of Certain Receivables</u>	<u>64</u>
<u>Note 4</u>	<u>Property and Equipment</u>	<u>67</u>
<u>Note 5</u>	<u>Goodwill, Spectrum Licenses and Other Intangible Assets</u>	<u>68</u>
<u>Note 6</u>	<u>Fair Value Measurements and Derivative Instruments</u>	<u>70</u>
<u>Note 7</u>	<u>Debt</u>	<u>72</u>
<u>Note 8</u>	<u>Tower Obligations</u>	<u>74</u>
<u>Note 9</u>	<u>Employee Compensation and Benefit Plans</u>	<u>75</u>
<u>Note 10</u>	<u>Income Taxes</u>	<u>77</u>
<u>Note 11</u>	<u>Earnings Per Share</u>	<u>80</u>
<u>Note 12</u>	<u>Commitments and Contingencies</u>	<u>80</u>
<u>Note 13</u>	<u>Additional Financial Information</u>	<u>82</u>
<u>Note 14</u>	<u>Subsequent Events</u>	<u>84</u>
<u>Note 15</u>	<u>Guarantor Financial Information</u>	<u>84</u>

Table of Contents

**T-Mobile US, Inc.**  
**Notes to the Consolidated Financial Statements**

**Note 1 – Summary of Significant Accounting Policies****Description of Business**

T-Mobile US, Inc. (“T-Mobile,” “we,” “our,” “us” or the “Company”), together with its consolidated subsidiaries, is a leading provider of mobile communications services, including voice, messaging and data, under its flagship brands, T-Mobile and MetroPCS, in the United States (“U.S.”), Puerto Rico and the U.S. Virgin Islands. We provide mobile communications services primarily using 4G Long-Term Evolution (“LTE”) technology. We also offer a wide selection of wireless devices, including handsets, tablets and other mobile communication devices, and accessories for sale, as well as financing through Equipment Installment Plans (“EIP”) and leasing through JUMP On Demand™. Additionally, we provide reinsurance for handset insurance policies and extended warranty contracts offered to our mobile communications customers.

**Basis of Presentation**

The consolidated financial statements include the balances and results of operations of T-Mobile and our consolidated subsidiaries. We operate as a single operating segment. We consolidate majority-owned subsidiaries over which we exercise control, as well as variable interest entities (“VIE”) where we are deemed to be the primary beneficiary and VIEs, which cannot be deconsolidated, such as those related to Tower obligations. Intercompany transactions and balances have been eliminated in consolidation.

Certain prior year amounts relating to the adoption of Accounting Standards Update (“ASU”) 2015-03, “Simplifying the Presentation of Debt Issuance Costs,” have been reclassified to conform to the current presentation. See “Accounting Pronouncements Adopted During the Current Year” below.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (“GAAP”) requires our management to make estimates and assumptions which affect the financial statements and accompanying notes. Examples include service revenues earned but not yet billed, service revenues billed but not yet earned, relative selling prices, allowances for uncollectible accounts and sales returns, discounts for imputed interest on EIP receivables, guarantee liabilities, losses incurred but not yet reported, tax liabilities, deferred income taxes including valuation allowances, useful lives of long-lived assets, cost estimates of asset retirement obligations, residual values on leased handsets, reasonably assured renewal terms for operating leases, stock-based compensation forfeiture rates, and fair value measurements related to goodwill, spectrum licenses, intangible assets, and derivative financial instruments. Estimates are based on historical experience, where applicable, and other assumptions which our management believes are reasonable under the circumstances. These estimates are inherently subject to judgment and actual results could differ from those estimates.

**Cash and Cash Equivalents**

Cash equivalents consist of highly liquid money market funds and U.S. Treasury securities with remaining maturities of three months or less at the date of purchase.

**Short-Term Investments**

Our short-term investments consist of U.S. Treasury securities classified as available for sale, which are stated at fair value and have remaining maturities of more than three months at the date of purchase. Unrealized gains and losses, net of related income taxes, on available for sale securities are reported as net increases and decreases to Accumulated other comprehensive income (loss) (“AOCI”), a component of stockholders' equity, until realized. The estimated fair values of our short-term investments are based on quoted market prices as of the end of the reporting period. The U.S. Treasury securities reported as of December 31, 2015 matured during 2016.

We review our available-for-sale securities for impairment on a quarterly basis or more often if a potential loss-triggering event occurs. If there has been a decline in the fair value below the amortized cost basis, we assess whether the impairment is other-than-temporary by considering, among other factors, the reason for the decline in fair value, our intent to sell the security, whether it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis and whether we do not expect to recover the entire amortized cost basis of the security. If we determine the impairment is other-than-temporary, we record a charge to Other expense, net in our Consolidated Statements of Comprehensive Income.



Table of Contents**Accounts Receivable and Allowances**

Accounts receivable consist primarily of amounts billed and currently due from customers, other carriers and third-party retail channels ("dealers"), as well as revenues earned but not yet billed at the end of each period. Accounts receivable not held for sale are reported in the balance sheet at outstanding principal adjusted for any charge-offs and the allowance for credit losses. Accounts receivable held for sale are reported at the lower of amortized cost or fair value. We have an arrangement to sell the majority of service accounts receivable on a revolving basis, which are treated as sales of financial assets. We maintain an allowance for estimated losses inherent in the accounts receivable portfolio based on a number of factors, including historical experience and current collection trends, aging of the receivable portfolio, credit quality of the customer base and other qualitative factors such as macro-economic conditions. We write off account balances if collection efforts are unsuccessful and the receivable balance is deemed uncollectible, based on customer credit ratings and the length of time from the original billing date.

**Equipment Installment Plan Receivables**

We offer certain retail customers the option to pay for their devices and other purchases in installments over a period of up to 24 months using an EIP. EIP not held for sale are reported in the balance sheet at outstanding principal adjusted for any charge-offs, allowance for credit losses and unamortized discounts. Accounts receivable held for sale are reported at the lower of amortized cost or fair value. At the time of an installment sale, we impute a discount for interest as there is no stated rate of interest on the EIP receivables and record the EIP receivables at their present value, which is determined by discounting future payments at the imputed interest rate. The difference between the present value of the EIP receivables and their face amount results in a discount which is recorded as a direct reduction to the carrying value with a corresponding reduction to equipment revenues in our Consolidated Statements of Comprehensive Income. We determine the imputed discount rate based primarily on current market interest rates and the amount of expected credit losses on the EIP receivables. As a result, we do not recognize a separate valuation allowance at the time of issuance as the effects of uncertainty about future cash flows are included in the initial present value measurement of the receivable. The imputed discount on EIP receivables is amortized over the financed installment term using the effective interest method and recognized as Interest income in our Consolidated Statements of Comprehensive Income.

Subsequent to the initial determination of the imputed discount, we assess the need for and, if necessary, recognize an allowance for credit losses to the extent the amount of estimated probable losses on the gross EIP receivable balances exceed the remaining unamortized imputed discount balances. The allowance is based on a number of factors, including collection experience, aging of the EIP receivable portfolio, credit quality of the customer base and other qualitative factors such as macro-economic conditions. We write off account balances if collection efforts are unsuccessful and the receivable balance is deemed uncollectible, based on customer credit ratings and the length of time from the original billing date. Equipment sales not reasonably assured to be collectible are recorded on a cash basis as payments are received.

The current portion of the EIP receivables is included in Equipment installment plan receivables, net and the long-term portion of the EIP receivables is included in Equipment installment plan receivables due after one year, net in our Consolidated Balance Sheets. We have an arrangement to sell certain EIP receivables on a revolving basis, which are treated as sales of financial assets.

**Inventories**

Inventories consist primarily of wireless devices and accessories, which are valued at the lower of cost or market. Cost is determined using standard cost which approximates average cost. Shipping and handling costs paid to wireless device and accessories vendors, and costs to refurbish used devices recovered through our device upgrade programs are included in the standard cost of inventory. We record inventory write-downs to net realizable value for obsolete and slow-moving items based on inventory turnover trends and historical experience.

**Long-Lived Assets**

Long-lived assets include assets that do not have indefinite lives, such as property and equipment and other intangible assets. We assess potential impairments to our long-lived assets when events or changes in circumstances indicate the carrying amount of the asset may not be recoverable. If any indicators of impairment are present, we test recoverability. The carrying value of a long-lived asset or asset group is not recoverable if it exceeds the sum of the undiscounted cash flows expected to be generated from the use and eventual disposition of the asset or asset group. If the undiscounted cash flows do not exceed the asset or asset group's carrying amount, then an impairment loss is recorded, measured as the amount by which the carrying amount of a long-lived asset or asset group exceeds its fair value.

Table of Contents***Property and Equipment***

Property and equipment consists of buildings and equipment, wireless communication systems, leasehold improvements, capitalized software, leased wireless devices and construction in progress. Buildings and equipment include certain network server equipment. Wireless communication systems include assets to operate our wireless network and IT data centers, including tower assets and leasehold improvements, assets related to the liability for the retirement of long-lived assets and capital leases. Leasehold improvements include asset improvements other than those related to the wireless network.

Property and equipment are recorded at cost less accumulated depreciation and impairments, if any, in Property and equipment, net on our Consolidated Balance Sheets. We generally depreciate property and equipment over the period the property and equipment provide economic benefit. Depreciable life studies are performed periodically to confirm the appropriateness of useful lives for certain categories of property and equipment. These studies take into account actual usage, physical wear and tear, replacement history and assumptions about technology evolution. When these factors indicate the useful life of an asset is different from the previous assessment, the remaining book value is depreciated prospectively over the adjusted remaining estimated useful life. Leasehold improvements are depreciated over the shorter of their estimated useful lives or the related lease term.

In 2015, we introduced JUMP! On Demand which allows customers to lease a device over a period up to 18 months and upgrade it for a new one up to three times in a 12 month period. To date, all of our leased devices were classified as operating leases by considering critical elements of the lease arrangement such as the lease term and the economic life, fair value and residual value of the device. At operating lease inception, leased wireless devices are transferred from inventory to property and equipment. Leased wireless devices are depreciated to their estimated residual value over the period expected to provide utility to us, which is generally the lease term. Revenues associated with the leased wireless devices, net of incentives, are generally recognized over the lease term. Upon device upgrade or at lease end, customers must return or purchase their device. Returned devices transferred from Property and equipment, net are recorded as inventory and are valued at the lower of cost or market with any write-down to market recognized as Cost of equipment sales in our Consolidated Statements of Comprehensive Income.

Costs of major replacements and improvements are capitalized. Repair and maintenance expenditures which do not enhance or extend the asset's useful life are charged to operating expenses as incurred. Construction costs, labor and overhead incurred in the expansion or enhancement of our wireless network are capitalized. Capitalization commences with pre-construction period administrative and technical activities, which includes obtaining leases, zoning approvals and building permits, and ceases at the point at which the asset is ready for its intended use. We capitalize interest associated with the acquisition or construction of certain property and equipment. Capitalized interest is reported as a reduction in interest expense and depreciated over the useful life of the related assets.

Future obligations related to capital leases are included in Short-term debt and Long-term debt in our Consolidated Balance Sheets. Depreciation of assets held under capital leases is included in Depreciation and amortization expense in our Consolidated Statements of Comprehensive Income.

We record an asset retirement obligation for the fair value of legal obligations associated with the retirement of tangible long-lived assets and a corresponding increase in the carrying amount of the related asset in the period in which the obligation is incurred. In periods subsequent to initial measurement, we recognize changes in the liability resulting from the passage of time and revisions to either the timing or the amount of the original estimate. Over time, the liability is accreted to its present value and the capitalized cost is depreciated over the estimated useful life of the asset. Our obligations relate primarily to certain legal obligations to remediate leased property on which our network infrastructure and administrative assets are located.

We capitalize certain costs incurred in connection with developing or acquiring internal use software. Capitalization of software costs commences once the final selection of the specific software solution has been made and management authorizes and commits to funding the software project. Capitalized software costs are included in Property and equipment, net in our Consolidated Balance Sheets and are amortized on a straight-line basis over the estimated useful life of the asset. Costs incurred during the preliminary project stage, as well as maintenance and training costs are expensed as incurred.

***Other Intangible Assets***

Intangible assets that do not have indefinite useful lives are amortized over their estimated useful lives. Customer lists are amortized using the sum-of-the-years-digits method over the expected period in which the relationship is expected to contribute to future cash flows. The remaining finite-lived intangible assets are amortized using the straight-line method.

Table of Contents**Goodwill and Indefinite-Lived Intangible Assets***Goodwill*

Goodwill consists of the excess of the purchase price over the fair value of identifiable net assets acquired in a business combination.

*Spectrum Licenses*

Spectrum licenses are carried at costs incurred to acquire the spectrum licenses and the costs to prepare the spectrum licenses for their intended use, such as costs to clear acquired spectrum licenses. The Federal Communications Commission ("FCC") issues spectrum licenses which provide us with the exclusive right to utilize designated radio frequency spectrum within specific geographic service areas to provide wireless communication services. While spectrum licenses are issued for a fixed period of time, typically for up to fifteen years, the FCC has granted license renewals routinely and at a nominal cost. The spectrum licenses held by us expire at various dates. We believe we will be able to meet all requirements necessary to secure renewal of our spectrum licenses at nominal costs. Moreover, we determined there are currently no legal, regulatory, contractual, competitive, economic or other factors that limit the useful lives of our spectrum licenses. Therefore, we determined the spectrum licenses should be treated as indefinite-lived intangible assets.

At times, we enter into agreements to sell or exchange spectrum licenses. Upon entering into the arrangement, if the transaction has been deemed to have commercial substance, spectrum licenses are reviewed for impairment and transferred at their carrying value, net of any impairment, to assets held for sale included in Other current assets in our Consolidated Balance Sheets until approval and completion of the exchange or sale. Upon closing of the transaction, spectrum licenses acquired as part of an exchange of nonmonetary assets are valued at fair value and the difference between the fair value of the spectrum licenses obtained, book value of the spectrum licenses transferred and cash paid, if any, is recognized as a gain and included in Gains on disposal of spectrum licenses in our Consolidated Statements of Comprehensive Income. Our fair value estimates of spectrum licenses are based on information for which there is little or no observable market data. If the transaction lacks commercial substance or the fair value is not measurable, the acquired spectrum licenses are recorded at the book value of the assets transferred or exchanged.

*Impairment*

We assess the carrying value of our goodwill and other indefinite-lived intangible assets, such as our spectrum licenses, for potential impairment annually as of December 31, or more frequently if events or changes in circumstances indicate such assets might be impaired.

We may elect to first perform a qualitative assessment to determine whether it is more likely than not the fair value of the single reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. If we do not perform a qualitative assessment, or if the qualitative assessment indicates it is more likely than not the fair value of the single reporting unit is less than its carrying amount, goodwill is tested for impairment based on a two-step test. In the first step, we compare the fair value of the reporting unit to the carrying value. The fair value of the reporting unit is determined using a market approach, which is based on market capitalization. If the fair value is less than the carrying value, the second step is performed. In the second step, we determine the fair values of all of the assets and liabilities of the reporting unit, including those that may not be currently recorded. The excess of the fair value of the reporting unit over the sum of the fair value of all of those assets and liabilities represents the implied goodwill amount. If the implied fair value of goodwill is lower than its carrying amount, an impairment loss is recognized for the difference.

We test our spectrum licenses for impairment on an aggregate basis, consistent with our management of the overall business at a national level. We may elect to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of an intangible asset group is less than its carrying value. If we do not perform the qualitative assessment, or if the qualitative assessment indicates it is more likely than not the fair value of the intangible asset group is less than its carrying amount, we calculate the estimated fair value of the intangible asset group. If the estimated fair value of the spectrum licenses is lower than their carrying amount, an impairment loss is recognized for the difference. We estimate fair value using the Greenfield approach, which is an income approach, to estimate the price at which an orderly transaction to sell the asset would take place between market participants at the measurement date under current market conditions.

Table of Contents**Guarantee Liabilities**

We offer a device trade-in program, Just Upgrade My Phone ("JUMP!"), which provides eligible customers a specified-price trade-in right to upgrade their device. Participating customers must finance the purchase of a device on an EIP and have a qualifying T-Mobile monthly wireless service plan, which is treated as a single multiple-element arrangement when entered into at or near the same time. Upon a qualifying JUMP! program upgrade, the customer's remaining EIP balance is settled provided they trade-in their eligible used device in good working condition and purchase a new device from us on a new EIP.

For customers who enroll in JUMP!, we defer and recognize a liability for the portion of revenue which represents the estimated fair value of the specified-price trade-in right guarantee. The guarantee liability is valued based on various economic and customer behavioral assumptions, which requires judgment, including estimating the customer's remaining EIP balance at trade-in, the expected fair value of the used device at trade-in, and the probability and timing of trade-in. We assess our guarantee liability at each reporting date to determine if facts and circumstances would indicate the incurrence of an incremental contingent liability is probable and if so, reasonably estimable. The recognition and subsequent adjustments of the contingent guarantee liability as a result of these assessments are recorded as adjustments to revenue. When customers upgrade their device, the difference between the EIP balance credit to the customer and the fair value of the returned device is recorded against the guarantee liabilities.

**Fair Value Measurements**

We carry certain assets and liabilities at fair value. Fair value is defined as an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The three tier hierarchy for inputs used in measuring fair value, which prioritizes the inputs based on the observability as of the measurement date, is as follows:

- Level 1 Quoted prices in active markets for identical assets or liabilities;
- Level 2 Observable inputs other than the quoted prices in active markets for identical assets and liabilities; and
- Level 3 Unobservable inputs for which there is little or no market data, which require us to develop assumptions of what market participants would use in pricing the asset or liability.

Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the placement of assets and liabilities being measured within the fair value hierarchy.

The carrying values of cash and cash equivalents, short-term investments, accounts receivable, accounts receivable from affiliates and accounts payable approximate fair value due to the short-term maturities of these instruments. The carrying values of EIP receivables approximate fair value as the receivables are recorded at their present value, net of unamortized discount and allowance for credit losses. There were no financial instruments with a carrying value materially different from their fair value, based on quoted market prices or rates for the same or similar instruments, or internal valuation models.

**Derivative Financial Instruments**

Derivative financial instruments primarily relate to embedded derivatives for certain components of the reset feature of the Senior Reset Notes to affiliates, which are required to be bifurcated and are recorded on the Consolidated Balance Sheets at fair value. Changes in fair value are recognized in Interest expense to affiliates in our Consolidated Statements of Comprehensive Income. We do not enter into derivatives for trading or speculative purposes.

**Revenue Recognition**

We primarily generate our revenue from providing wireless services to customers and selling or leasing devices and accessories. We offer our wireless services and devices to customers through bundled arrangements, which may be comprised of multiple contracts entered into with a customer at or near the same time. In recognizing revenue, we assess such agreements as a single bundled arrangement that may involve multiple deliverables, which include wireless services, wireless devices or a combination thereof, and allocated revenue between each deliverable based on the relative selling prices of each deliverable on a standalone basis.

## Table of Contents

In June 2016, we introduced #GetThanked, which offers eligible customers the following free promotional items as part of their T-Mobile service:

- **T-Mobile stock** - A share of T-Mobile stock to eligible new (through December 31, 2016) or existing (as of June 6, 2016) customers. Shares issued to customers under this promotion are purchased by an independent third-party broker in the open market on behalf of eligible customers. The associated cost, which is paid by T-Mobile, is recorded as a reduction of service revenue for existing customers and as a reduction of equipment revenue for new customers in our Consolidated Statements of Comprehensive Income. Through December 31, 2016, existing eligible customers can also receive a share of T-Mobile stock (subject to a maximum of 100 shares in a calendar year) for every new active account they refer, purchased by the third-party broker and paid for by T-Mobile. The cost of shares issued under this refer-a-friend program are included in Selling, general and administrative expense in our Consolidated Statements of Comprehensive Income;
- **Weekly surprise items** - Each Tuesday, eligible customers who download the T-Mobile Tuesday app are informed about and can redeem products and services offered by participating business partners. The associated cost is included in Selling, general and administrative expense in our Consolidated Statements of Comprehensive Income; and
- **In-flight Wi-Fi** - A full hour of in-flight Wi-Fi free to eligible customers on their smartphone on all Gogo-equipped domestic flights. The associated cost, which is paid by T-Mobile, is included in Cost of services in our Consolidated Statements of Comprehensive Income.

### *Wireless Services Revenue*

We generate our wireless service revenues from providing access to, and usage of, our wireless communications network. Service revenues also include revenues earned for providing value added services to customers, such as handset insurance services. Service revenues are billed either in advance or arrears or are prepaid and are recognized when the service is rendered and all other revenue recognition criteria have been met. Revenues that are not reasonably assured to be collectible are recorded on a cash basis as payments are received. The recognition of prepaid revenue is deferred until services are rendered or the prepaid balance expires. Incentives given to customers are recorded as a reduction to revenue. We recognize service revenues for Data Stash plans when such services are delivered and the data is consumed, or at time of forfeiture or expiration. Revenues relating to unused data that is carried over to the following month are deferred and valued based on their relative standalone selling price. Revenue is recorded gross for arrangements involving the resale of third-party services where we are considered the primary obligor and is recorded net of associated costs incurred for services whereby we are not considered the primary obligor.

Federal Universal Service Fund ("USF") and other fees are assessed by various governmental authorities in connection with the services we provide to our customers. When we separately bill and collect these regulatory fees from customers, they are recorded gross in Total service revenues and cost of services in our Consolidated Statements of Comprehensive Income. For the years ended December 31, 2016, 2015 and 2014, we recorded approximately \$409 million, \$334 million and \$349 million, respectively, of USF and other fees on a gross basis.

### *Equipment Revenues*

We generate equipment revenues from the sale or lease of mobile communication devices and accessories. Device and accessory sales revenues are generally recognized when the products are delivered to, and accepted by, the customer or dealer. We defer a portion of equipment revenues and cost of equipment sales for expected device returns based on historical experience. We offer certain customers the option to pay for devices and accessories in installments using an EIP. See EIP Receivables section above for further information.

In addition, for customers enrolled in JUMP!, we separate the JUMP! trade-in right from the multiple element arrangement at its fair value and defer the portion of revenue which represents the fair value of the trade-in right. See Guarantee Liabilities section above for further information. In 2015, we introduced JUMP! On Demand, which allows customers to lease a device and upgrade their leased wireless device for a new one up to three times in a 12 month period. Leased wireless devices are accounted for as operating leases and lease revenues are recognized as earned on a straight-line basis over the lease term. The residual value of purchased leased devices is recorded as equipment revenues and cost of equipment sales. See Property and Equipment section above for further information.

## Table of Contents

### **Rent Expense**

We have operating leases for cell sites, retail locations, corporate offices and dedicated transportation lines, some of which have escalating rentals during the initial lease term and during subsequent optional renewal periods. We recognize rent expense on a straight-line basis, over the non-cancelable lease term and renewal periods that are considered reasonably assured at the inception of the lease. We consider several factors in assessing whether renewal periods are reasonably assured of being exercised, including the continued maturation of our network nationwide, technological advances within the telecommunications industry and the availability of alternative sites.

### **Advertising Expense**

We expense the cost of advertising and other promotional expenditures to market our services and products as incurred. For the years ended December 31, 2016, 2015 and 2014, advertising expenses included in Selling, general and administrative expenses in our Consolidated Statements of Comprehensive Income were \$1.7 billion, \$1.6 billion and \$1.4 billion, respectively.

### **Income Taxes**

Deferred tax assets and liabilities are recognized based on temporary differences between the financial statement and tax bases of assets and liabilities using enacted tax rates expected to be in effect when these differences are realized. A valuation allowance is recorded when it is more likely than not that some portion or all of a deferred tax asset will not be realized. The ultimate realization of a deferred tax asset depends on the ability to generate sufficient taxable income of the appropriate character and in the appropriate taxing jurisdictions within the carryforward periods available.

We account for uncertainty in income taxes recognized in the financial statements in accordance with the accounting guidance on the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. We assess whether it is more likely than not that a tax position will be sustained upon examination based on the technical merits of the position and adjust the unrecognized tax benefits in light of changes in facts and circumstances, such as changes in tax law, interactions with taxing authorities and developments in case law.

### **Other Comprehensive Income (Loss)**

Other comprehensive income (loss) consists of adjustments, net of tax, related to unrealized gains (losses) on available-for-sale securities. This is reported in AOCI as a separate component of stockholders' equity until realized in earnings.

### **Stock-Based Compensation**

Stock-based compensation cost for stock awards, which include restricted stock units ("RSUs") and performance-based restricted stock units ("PRSUs"), is measured at fair value on the grant date and recognized as expense, net of expected forfeitures, over the related service period. The fair value of stock awards is based on the closing price of our common stock on the date of grant. RSUs are recognized as expense using the straight-line method. PSUs are recognized as expense following a graded vesting schedule.

### **Earnings Per Share**

Basic earnings per share is computed by dividing Net income attributable to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted earnings per share is computed by giving effect to all potentially dilutive common shares outstanding during the period. Potentially dilutive common shares consist of outstanding stock options, RSUs and PRSUs, calculated using the treasury stock method, and mandatory convertible preferred stock ("preferred stock"), calculated using the if-converted method.

### **Variable Interest Entities**

VIEs are entities which lack sufficient equity to permit the entity to finance its activities without additional subordinated financial support from other parties, have equity investors which do not have the ability to make significant decisions relating to the entity's operations through voting rights, do not have the obligation to absorb the expected losses or do not have the right to receive the residual returns of the entity. The most common type of VIE is a special purpose entity ("SPE"). SPEs are commonly used in securitization transactions in order to isolate certain assets and distribute the cash flows from those assets to investors. SPEs are generally structured to insulate investors from claims on the SPE's assets by creditors of other entities, including the creditors of the seller of the assets.



Table of Contents

The primary beneficiary is required to consolidate the assets and liabilities of the VIE. The primary beneficiary is the party which has both the power to direct the activities of an entity that most significantly impact the VIE's economic performance, and through its interests in the VIE, the obligation to absorb losses or the right to receive benefits from the VIE which could potentially be significant to the VIE. We consolidate VIEs when we are deemed to be the primary beneficiary or when the VIE cannot be deconsolidated.

In assessing which party is the primary beneficiary, all the facts and circumstances are considered, including each party's role in establishing the VIE and its ongoing rights and responsibilities. This assessment includes, first, identifying the activities that most significantly impact the VIE's economic performance; and second, identifying which party, if any, has power over those activities. In general, the parties that make the most significant decisions affecting the VIE (such as asset managers and servicers) or have the right to unilaterally remove those decision-makers are deemed to have the power to direct the activities of a VIE.

**Accounting Pronouncements Adopted During the Current Year**

In March 2016, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update (ASU) 2016-09, "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting," which simplifies several aspects of the accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. We elected to adopt this standard effective as of January 1, 2016. The impacts on our consolidated financial statements from the adoption of this standard are as follows:

- Consolidated Balance Sheets - A \$38 million decrease to the January 1, 2016 Accumulated deficit balance from the recognition, on a modified retrospective basis, of all previously unrecognized income tax attributes related to share-based payments;
- Consolidated Statements of Comprehensive Income - On a prospective basis, all excess tax benefits and deficiencies related to share-based payments will be recognized through Income tax expense. Prior period amounts were not adjusted; and
- Consolidated Statements of Cash Flows - On a prospective basis, as permitted, excess tax benefits related to share-based payments will be presented as operating activities. Prior period amounts were not adjusted.

In April 2015, the FASB issued ASU 2015-03, "Simplifying the Presentation of Debt Issuance Costs." The standard requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected. We adopted this new guidance in the first quarter of 2016 and applied the changes retrospectively. The implementation of this standard did not have a significant impact on our consolidated financial statements.

In August 2014, the FASB issued ASU 2014-15, "Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern." The standard requires us to assess our ability to continue as a going concern each interim and annual reporting period and provide certain disclosures if there is substantial doubt about our ability to continue as a going concern, including management's plan to alleviate the substantial doubt. We adopted this new guidance in the fourth quarter of 2016. The implementation of this standard did not have an impact on our consolidated financial statements.

**Accounting Pronouncements Not Yet Adopted**

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09"), and has since modified the standard with several ASU's.

The standard requires entities to recognize revenue through the application of a five-step model, which includes the: identification of the contract; identification of the performance obligations; determination of the transaction price; allocation of the transaction price to the performance obligations; and recognition of revenue as the entity satisfies the performance obligations.

The standard becomes effective for us beginning January 1, 2018; however, early adoption with the original effective date for periods beginning January 1, 2017 is permitted. We plan to adopt the standard when it becomes effective for us beginning January 1, 2018.

Table of Contents

The guidance permits two methods of adoption, the full retrospective method applying the standard to each prior reporting period presented, or the modified retrospective method with a cumulative effect of initially applying the guidance recognized at the date of initial application. The standard also allows entities to apply certain practical expedients at their discretion. We currently anticipate adopting the standard using the modified retrospective method with a cumulative catch up adjustment and providing additional disclosures comparing results to previous rules.

We continue to evaluate the impact of the new standard on our consolidated financial statements but anticipate this standard will have a material impact on our consolidated financial statements. While we are continuing to assess all potential impacts of the standard, we currently believe the most significant impacts may include the following items:

- Whether our EIP contracts contain a significant financing component, which is similar to our current practice of imputing interest, and would similarly impact the amount of revenue recognized at the time of an EIP sale and whether or not a portion of the revenue is recognized as interest rather than equipment revenue.
- As we currently expense contract acquisition costs and believe that the requirement to defer incremental contract acquisition costs and recognize them over the term of the initial contract and anticipated renewal contracts to which the costs relate will have a significant impact to our consolidated financial statements.
- Whether bill credits earned over time result in extended service contracts, which would impact the allocation and timing of revenue between service revenue and equipment revenue.
- Overall, with the exception of the aforementioned impacts, we do not expect that the new standard will result in a substantive change to the method of allocation of contract revenues between various services and equipment, nor to the timing of when revenues are recognized for most of our service contracts.

We are still in the process of evaluating these impacts, and our initial assessment may change as we continue to refine our systems, process and assumptions.

We are in the process of implementing significant new revenue accounting systems, processes and internal controls over revenue recognition which will ultimately assist us in the application of the new standard.

In February 2016, the FASB issued ASU 2016-02, "Leases." The standard requires all lessees to report a right-of-use asset and a lease liability for most leases. The income statement recognition is similar to existing lease accounting and is based on lease classification. The standard requires lessees and lessors to classify most leases using principles similar to existing lease accounting, but eliminates the "bright line" classification tests. For lessors, the standard modifies the classification criteria and the accounting for sales-type and direct financing leases. The standard will become effective for us beginning January 1, 2019 and will require recognizing and measuring leases at the beginning of the earliest period presented using a modified retrospective approach. Early adoption is permitted. We are currently evaluating the standard and the timing of adoption but expect that it will have a material impact on our consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, "Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The standard requires a financial asset (or a group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The measurement of expected credit losses is based on relevant information about past events, including historical experience, current conditions and reasonable and supportable forecasts that affect the collectibility of the reported amount. The standard will become effective for us beginning January 1, 2020 and will require a cumulative-effect adjustment to Accumulated deficit as of the beginning of the first reporting period in which the guidance is effective (that is, a modified-retrospective approach). Early adoption is permitted for us as of January 1, 2019. We are currently evaluating the impact this guidance will have on our consolidated financial statements and the timing of adoption.

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments." The standard provides guidance on how certain cash receipts and payments are presented and classified in the statement of cash flows, including beneficial interests in securitization, which would impact the presentation of the deferred purchase price from sales of receivables. The standard is intended to reduce current diversity in practice. The standard will become effective for us beginning January 1, 2018 and will require a retrospective approach. Early adoption is permitted, including adoption in an interim period. We are currently evaluating the impact this guidance will have on our consolidated financial statements and the timing of adoption.

In October 2016, the FASB issued ASU 2016-16, "Accounting for Income Taxes: Intra-Entity Transfers of Assets Other Than Inventory." The standard requires that the income tax impact of intra-entity sales and transfers of property, except for



Table of Contents

inventory, be recognized when the transfer occurs. The standard will become effective for us beginning January 1, 2018 and will require any deferred taxes not yet recognized on intra-entity transfers to be recorded to retained earnings under a modified retrospective approach. Early adoption is permitted. We are currently evaluating the standard, but expect that it will not have a material impact on our consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, "Statement of Cash Flows (Topic 230): Restricted Cash." The standard requires entities to include in their cash and cash-equivalent balances in the statement of cash flows those amounts that are deemed to be restricted cash and restricted cash equivalents. The ASU does not define the terms "restricted cash" and "restricted cash equivalents." The standard will be effective for us beginning January 1, 2018 and will require a retrospective approach. Early adoption is permitted. We are currently evaluating the standard, but expect that it will not have a material impact on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, "Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment." The standard eliminates the requirement to measure the implied fair value of goodwill by assigning the fair value of a reporting unit to all assets and liabilities within that unit ("the Step 2 test") from the goodwill impairment test. Instead, if the carrying amount of a reporting unit exceeds its fair value, an impairment loss is recognized in an amount equal to that excess, limited by the amount of goodwill in that reporting unit. The standard will become effective for us beginning January 1, 2020 and must be applied to any annual or interim goodwill impairment assessments after that date. Early adoption is permitted. We are currently evaluating the standard, but expect that it will not have a material impact on our consolidated financial statements.

**Note 2 – Equipment Installment Plan Receivables**

We offer certain retail customers the option to pay for their devices and accessories in installments over a period of up to 24 months using an EIP.

The following table summarizes the EIP receivables:

(in millions)	December 31, 2016	December 31, 2017
EIP receivables, gross	\$ 3,230	\$ 3,558
Unamortized imputed discount	(195)	(185)
EIP receivables, net of unamortized imputed discount	3,035	3,373
Allowance for credit losses	(121)	(148)
EIP receivables, net	\$ 2,914	\$ 3,225
<b>Classified on the balance sheet as:</b>		
Equipment installment plan receivables, net	\$ 1,930	\$ 2,378
Equipment installment plan receivables due after one year, net	984	847
EIP receivables, net	\$ 2,914	\$ 3,225

We use a proprietary credit scoring model that measures the credit quality of a customer at the time of application for mobile communications service using several factors, such as credit bureau information, consumer credit risk scores and service plan characteristics. Based upon customer credit profiles, we classify EIP receivables into the credit categories of "Prime" and "Subprime." Prime customer receivables are those with lower delinquency risk and Subprime customer receivables are those with higher delinquency risk. Subprime customers may be required to make a down payment on their equipment purchases. In addition, certain customers within the Subprime category are required to pay an advance deposit.

EIP receivables for which invoices have not yet been generated for the customer are classified as Unbilled. EIP receivables for which invoices have been generated but which are not past the contractual due date are classified as Billed – Current. EIP receivables for which invoices have been generated and the payment is past the contractual due date are classified as Billed – Past Due.

Table of Contents

The balance and aging of the EIP receivables on a gross basis by credit category were as follows:

(in millions)	December 31, 2016			December 31, 2015		
	Prime	Subprime	Total	Prime	Subprime	Total
Unbilled	\$ 1,343	\$ 1,686	\$ 3,029	\$ 1,593	\$ 1,698	\$ 3,291
Billed – Current	51	77	128	77	91	168
Billed – Past Due	25	48	73	37	62	99
EIP receivables, gross	<u>\$ 1,419</u>	<u>\$ 1,811</u>	<u>\$ 3,230</u>	<u>\$ 1,707</u>	<u>\$ 1,851</u>	<u>\$ 3,558</u>

The increase in subprime EIP receivables as a percentage of total EIP receivables is primarily due to the EIP sale arrangement funding increase during the year ended December 31, 2016.

Activity for the years ended December 31, 2016 and 2015 in the unamortized imputed discount and allowance for credit losses balances for the EIP receivables was as follows:

(in millions)	December 31, 2016	December 31, 2015
Imputed discount and allowance for credit losses, beginning of year	\$ 333	\$ 448
Bad debt expense	250	365
Write-offs, net of recoveries	(277)	(333)
Change in imputed discount on short-term and long-term EIP receivables	186	(84)
Impacts from sales of EIP receivables	(176)	(63)
Imputed discount and allowance for credit losses, end of year	<u>\$ 316</u>	<u>\$ 333</u>

The EIP receivables had weighted average effective imputed interest rates of 9.0% and 8.8% as of December 31, 2016 and 2015, respectively.

### Note 3 – Sales of Certain Receivables

We have entered into transactions to sell certain service and EIP accounts receivables. The transactions, including our continuing involvement with the sold receivables and the respective impacts to our financial statements, are described below.

#### Sales of Service Receivables

##### Overview of the Transaction

In 2014, we entered into an arrangement to sell certain service accounts receivables on a revolving basis with a maximum funding commitment of \$750 million (the “service receivable sale arrangement”). In November 2016, the arrangement was amended to increase the maximum funding commitment to \$950 million with a scheduled expiration date in March 2018. As of December 31, 2016 and 2015, the service receivable sale arrangement provided funding of \$907 million and \$750 million, respectively. Sales of receivables occur daily and are settled on a monthly basis. The receivables consist of service charges currently due from customers and are short-term in nature.

In connection with the service receivable sale arrangement, we formed a wholly-owned subsidiary, which qualifies as a bankruptcy remote entity to sell service accounts receivables (the “Service BRE”). The Service BRE does not qualify as a Variable Interest Entity (“VIE”), and due to the significant level of control we exercise over the entity, it is consolidated. Pursuant to the arrangement, certain of our wholly-owned subsidiaries transfer selected receivables to the Service BRE. The Service BRE then sells the receivables to an unaffiliated entity (the “Service VIE”), which was established to facilitate the sale of beneficial ownership interests in the receivables to certain third parties.

##### Variable Interest Entity

We determined that the Service VIE qualifies as a VIE as it lacks sufficient equity to finance its activities. We have a variable interest in the Service VIE, but are not the primary beneficiary as we lack the power to direct the activities that most significantly impact the Service VIE’s economic performance. Those activities include committing the Service VIE to legal agreements to purchase or sell assets, selecting which receivables are purchased in the service receivable sale arrangement, determining whether the Service VIE will sell interests in the purchased service receivables to other parties, funding of the entities and servicing of receivables. We do not hold

the power to direct the key decisions underlying these activities. For example, while we act as the servicer of the sold receivables, which is considered a significant activity of the Service VIE, we

Table of Contents

are acting as an agent in our capacity as the servicer and the counterparty to the service receivable sale arrangement has the ability to remove us as the servicing agent of the receivables at will with no recourse available to us. As we have determined we are not the primary beneficiary, the results of the Service VIE are not consolidated into our consolidated financial statements.

The following table summarizes the carrying amounts and classification of assets, which consists primarily of the deferred purchase price and liabilities included in our Consolidated Balance Sheets that relate to our variable interest in the Service VIE:

(in millions)	December 31, 2016	December 31, 2015
Other current assets	\$ 207	\$ 206
Accounts payable and accrued liabilities	17	—
Other current liabilities	129	73

**Sales of EIP Receivables***Overview of the Transaction*

In 2015, we entered into an arrangement to sell certain EIP accounts receivables on a revolving basis with a maximum funding commitment of \$800 million (the "EIP sale arrangement"). In June 2016, the EIP sale arrangement was amended to increase the maximum funding commitment to \$1.3 billion with a scheduled expiration date in November 2017. As of December 31, 2016 and 2015, the EIP sale arrangement provided funding of \$1.2 billion and \$800 million, respectively. Sales of EIP receivables occur daily and are settled on a monthly basis. The receivables consist of customer EIP balances, which require monthly customer payments for up to 24 months.

In connection with this EIP sale arrangement, we formed a wholly-owned subsidiary, which qualifies as a bankruptcy remote entity (the "EIP BRE"). Pursuant to the EIP sale arrangement, our wholly-owned subsidiary transfers selected receivables to the EIP BRE. The EIP BRE then sells the receivables to a non-consolidated and unaffiliated third-party entity for which we do not exercise any level of control, nor does the entity qualify as a VIE.

*Variable Interest Entity*

We determined that the EIP BRE is a VIE as its equity investment at risk lacks the obligation to absorb a certain portion of its expected losses. We have a variable interest in the EIP BRE and determined that we are the primary beneficiary based on our ability to direct the activities which most significantly impact the EIP BRE's economic performance. Those activities include selecting which receivables are transferred into the EIP BRE and sold in the EIP sale arrangement and funding of the EIP BRE. Additionally, our equity interest in the EIP BRE obligates us to absorb losses and gives us the right to receive benefits from the EIP BRE that could potentially be significant to the EIP BRE. Accordingly, we determined that we are the primary beneficiary, and include the balances and results of operations of the EIP BRE in our consolidated financial statements.

The following table summarizes the carrying amounts and classification of assets (primarily the deferred purchase price) and liabilities included in our Consolidated Balance Sheets that relate to the EIP BRE:

(in millions)	December 31, 2016	December 31, 2015
Other current assets	\$ 371	\$ 164
Other assets	83	44
Accounts payable and accrued liabilities	—	14
Other long-term liabilities	4	3

In addition, the EIP BRE is a separate legal entity with its own separate creditors who will be entitled, prior to any liquidation of the EIP BRE, to be satisfied prior to any value in the EIP BRE becoming available to us. Accordingly, the assets of the EIP BRE may not be used to settle our general obligations and creditors of the EIP BRE have limited recourse to our general credit.

Table of Contents**Sales of Receivables**

The transfers of service receivables and EIP receivables to the non-consolidated entities are accounted for as sales of financial assets. Once identified for sale, the receivable is recorded at the lower of cost or fair value. Upon sale, we derecognize the net carrying amount of the receivables. We recognize the net cash proceeds in Net cash provided by operating activities in our Consolidated Statements of Cash Flows.

The proceeds are net of the deferred purchase price, consisting of a receivable from the purchasers that entitles us to certain collections on the receivables. We recognize the collection of the deferred purchase price in Net cash provided by operating activities as it is dependent on collection of the customer receivables and is not subject to significant interest rate risk. The deferred purchase price represents a financial asset that is primarily tied to the creditworthiness of the customers and which can be settled in such a way that we may not recover substantially all of our recorded investment, due to default by the customers on the underlying receivables. We elected, at inception, to measure the deferred purchase price at fair value with changes in fair value included in Selling, general and administrative expense in our Consolidated Statements of Comprehensive Income. The fair value of the deferred purchase price is determined based on a discounted cash flow model which uses primarily unobservable inputs (Level 3 inputs), including customer default rates. As of December 31, 2016 and 2015, our deferred purchase price related to the sales of service receivables and EIP receivables was \$659 million and \$389 million, respectively.

The following table summarizes the impacts of the sale of certain service receivables and EIP receivables in our Consolidated Balance Sheets:

(in millions)	December 31, 2016	December 31, 2015
Derecognized net service receivables and EIP receivables	\$ 2,502	\$ 1,850
Other current assets	578	370
<i>of which, deferred purchase price</i>	576	345
Other long-term assets	83	44
<i>of which, deferred purchase price</i>	83	44
Accounts payable and accrued liabilities	17	14
Other current liabilities	129	73
Other long-term liabilities	4	3
Net cash proceeds since inception	2,030	1,494
Of which:		
Net cash proceeds during the year-to-date period	536	884
Net cash proceeds funded by reinvested collections	1,494	610

We recognized losses from sales of receivables of \$228 million, \$204 million and \$179 million for the years ended December 31, 2016, 2015 and 2014, respectively. These losses from sales of receivables were recognized in Selling, general and administrative expense in our Consolidated Statements of Comprehensive Income. Losses from sales of receivables include adjustments to the receivables' fair values and changes in fair value of the deferred purchase price.

**Continuing Involvement**

Pursuant to the sale arrangements described above, we have continuing involvement with the service receivables and EIP receivables we sell as we service the receivables and are required to repurchase certain receivables, including ineligible receivables, aged receivables and receivables where write-off is imminent. We continue to service the customers and their related receivables, including facilitating customer payment collection, in exchange for a monthly servicing fee. As the receivables are sold on a revolving basis, the customer payment collections on sold receivables may be reinvested in new receivable sales. While servicing the receivables, we apply the same policies and procedures to the sold receivables as we apply to our owned receivables, and we continue to maintain normal relationships with our customers. Pursuant to the EIP sale arrangement, under certain circumstances, we are required to deposit cash or replacement EIP receivables primarily for contracts terminated by customers under our JUMP! Program.

In addition, we have continuing involvement with the sold receivables as we may be responsible for absorbing additional credit losses pursuant to the sale arrangements. Our maximum exposure to loss related to the involvement with the service receivables and EIP receivables sold under the sale arrangements was \$1.1 billion as of December 31, 2016. The maximum exposure to loss, which is a

required disclosure under GAAP, represents an estimated loss that would be incurred under severe, hypothetical circumstances whereby we would not receive the deferred purchase price portion of the contractual proceeds

Table of Contents

withheld by the purchasers and would also be required to repurchase the maximum amount of receivables pursuant to the sale arrangements without consideration for any recovery. As we believe the probability of these circumstances occurring is remote, the maximum exposure to loss is not an indication of our expected loss.

**Note 4 – Property and Equipment**

The components of property and equipment were as follows:

(in millions)	Useful Lives	December 31, 2016	December 31, 2015
Buildings and equipment	Up to 40 years	\$ 1,657	\$ 1,900
Wireless communications systems	Up to 20 years	29,272	27,063
Leasehold improvements	Up to 12 years	1,068	1,003
Capitalized software	Up to 7 years	8,488	8,524
Leased wireless devices	Up to 18 months	2,624	2,236
Construction in progress		2,613	2,466
Accumulated depreciation and amortization		(24,779)	(23,192)
Property and equipment, net		<u>\$ 20,943</u>	<u>\$ 20,000</u>

Wireless communication systems include capital lease agreements for network equipment with varying expiration terms through 2030. Capital lease assets and accumulated amortization were \$1.6 billion and \$300 million, and \$839 million and \$117 million, as of December 31, 2016 and 2015, respectively.

We capitalize interest associated with the acquisition or construction of certain property and equipment. We recognized capitalized interest of \$142 million, \$230 million and \$81 million for the years ended December 31, 2016, 2015 and 2014, respectively.

The components of leased wireless devices under our JUMP! On Demand program were as follows:

(in millions)	December 31, 2016	December 31, 2015
Leased wireless devices, gross	\$ 2,624	\$ 2,236
Accumulated depreciation	(1,193)	(263)
Leased wireless devices, net	<u>\$ 1,431</u>	<u>\$ 1,973</u>

Future minimum payments expected to be received over the lease term related to the leased wireless devices, which exclude optional residual buy-out amounts at the end of the lease term, are summarized below:

(in millions)	Total
Year Ending December 31, 2017	\$ 710
2018	92
Total	<u>\$ 802</u>

Depreciation expense relating to property and equipment was \$6.0 billion, \$4.4 billion and \$4.1 billion for the years ended December 31, 2016, 2015 and 2014, respectively. Depreciation expense for the years ended December 31, 2016 and 2015 included \$1.5 billion and \$312 million, respectively, related to leased wireless devices.

For the years ended December 31, 2016, 2015 and 2014, we recorded additional depreciation expense of \$101 million, \$85 million and \$242 million, respectively, as a result of adjustments to useful lives of network equipment expected to be replaced in connection with our network transformation and decommissioning the MetroPCS CDMA network and redundant network cell sites.

Asset retirement obligations are primarily for certain legal obligations to remediate leased property on which our network infrastructure and administrative assets are located.

Table of Contents

Activity in our asset retirement obligations was as follows:

(in millions)	December 31, 2016	December 31, 2015
Asset retirement obligations, beginning of year	\$ 483	\$ 390
Liabilities incurred	50	19
Liabilities settled	(67)	(130)
Accretion expense	24	17
Changes in estimated cash flows	49	187
Asset retirement obligations, end of year	<u>\$ 539</u>	<u>\$ 483</u>
<b>Classified on the balance sheet as:</b>		
Other current liabilities	\$ 16	\$ 41
Other long-term liabilities	523	442
Asset retirement obligations	<u>\$ 539</u>	<u>\$ 483</u>

The corresponding assets, net of accumulated depreciation, related to asset retirement obligations were \$258 million and \$241 million as of December 31, 2016 and 2015, respectively. For the year ended December 31, 2015, we settled asset retirement obligations in connection with the decommissioning of certain cell sites. Due to new information gained throughout 2015, primarily from decommissioning the MetroPCS CDMA network cell sites, we reassessed the expected cash flows related to its asset retirement obligations for all remaining T-Mobile network cell sites. As a result, we recorded asset retirement obligations and corresponding assets in the fourth quarter of 2015 to reflect the change in estimated cash flows.

**Note 5 – Goodwill, Spectrum Licenses and Other Intangible Assets****Goodwill**

There were no changes in carrying values of goodwill for the years ended December 31, 2016 and 2015.

**Spectrum Licenses**

The following table summarizes our spectrum license activity:

(in millions)	December 31, 2016	December 31, 2015
Spectrum licenses, beginning of year	\$ 23,955	\$ 21,955
Spectrum license acquisitions	3,334	2,615
Spectrum licenses transferred to held for sale	(324)	(727)
Costs to clear spectrum	49	112
Spectrum licenses, end of year	<u>\$ 27,014</u>	<u>\$ 23,955</u>

We had the following spectrum license transactions during 2016:

- We closed on the agreement with AT&T Inc. for the acquisition and exchange of certain spectrum licenses. Upon closing of the transaction during the first quarter of 2016, we recorded the spectrum licenses received at their estimated fair value of approximately \$1.2 billion and recognized a gain of \$636 million included in Gains on disposal of spectrum licenses in our Consolidated Statements of Comprehensive Income.
- We closed on agreements with multiple third parties for the purchase and exchange of certain spectrum licenses for \$1.3 billion in cash. Upon closing of the transactions, we recorded spectrum licenses received at their estimated fair values totaling approximately \$1.7 billion and recognized gains of \$199 million included in Gains on disposal of spectrum licenses in our Consolidated Statements of Comprehensive Income.
- We closed on an agreement with a third party for the purchase of certain spectrum licenses covering approximately 11 million people for approximately \$420 million during the fourth quarter of 2016.



Table of Contents

- We entered into an agreement with a third party for the exchange of certain spectrum licenses, which is expected to close in the first half of 2017. Our spectrum licenses to be transferred as part of the exchange transaction were reclassified as assets held for sale and were included in Other current assets in our Consolidated Balance Sheets at their carrying value of \$86 million as of December 31, 2016.

We had the following spectrum license transactions during 2015:

- Upon conclusion of the 2014 Advanced Wireless Services ("AWS") auction, we were awarded AWS spectrum licenses covering approximately 97 million people for an aggregate bid price of approximately \$1.8 billion.
- We closed on the agreement with Verizon Communications Inc. for the exchange of certain spectrum licenses. Upon closing of the transaction, we recorded the spectrum licenses received at their estimated fair value of \$311 million and recognized a non-cash gain of \$139 million included in Gains on disposal of spectrum licenses in our Consolidated Statements of Comprehensive Income.
- We closed on agreements with multiple third parties for the purchase and exchange of certain spectrum licenses for \$459 million in cash. Upon closing of the transactions, we recorded spectrum licenses received at their estimated fair values totaling approximately \$530 million and recognized gains of \$24 million included in Gains on disposal of spectrum licenses in our Consolidated Statements of Comprehensive Income.
- We entered into multiple agreements with third parties for the exchange of certain spectrum licenses. Our spectrum licenses to be transferred as part of the exchange transaction were reclassified as assets held for sale and were included in Other current assets in our Consolidated Balance Sheets at their carrying value of \$554 million as of December 31, 2015.

**Goodwill and Other Intangible Assets Impairment Assessments**

Our impairment assessment of goodwill and indefinite-lived intangible assets (spectrum licenses) resulted in no impairment as of December 31, 2016 and 2015.

**Other Intangible Assets**

The components of intangible assets were as follows:

(in millions)	Useful Lives	December 31, 2016			December 31, 2015		
		Gross Amount	Accumulated Amortization	Net Amount	Gross Amount	Accumulated Amortization	Net Amount
Customer lists	Up to 6 years	\$ 1,104	\$ (894)	\$ 210	\$ 1,104	\$ (719)	\$ 385
Trademarks and patents	Up to 12 years	303	(156)	147	300	(115)	185
Other	Up to 28 years	50	(31)	19	51	(27)	24
Other intangible assets		\$ 1,457	\$ (1,081)	\$ 376	\$ 1,455	\$ (861)	\$ 594

Amortization expense for intangible assets subject to amortization was \$220 million, \$276 million and \$333 million for the years ended December 31, 2016, 2015 and 2014, respectively.

The estimated aggregate future amortization expense for intangible assets subject to amortization are summarized below:

(in millions)	Estimated future Amortization
Year Ending December 31,	
2017	\$ 163
2018	104
2019	52
2020	34
2021	14
Thereafter	9
Total	\$ 376



Table of Contents**Note 6 – Fair Value Measurements and Derivative Instruments****Embedded Derivative Instruments**

In connection with the business combination with MetroPCS, we issued senior reset notes to Deutsche Telekom. The interest rates were adjusted at the reset dates to rates defined in the applicable supplemental indentures to manage interest rate risk related to the senior reset notes. We determined certain components of the reset feature are required to be bifurcated from the senior reset notes and separately accounted for as embedded derivative instruments. As of December 31, 2015, one embedded derivative related to the 5.950% Senior Reset Notes to affiliates due 2023 was subject to interest rate volatility. In April 2016, the interest rate related to the 5.950% Senior Reset Notes to affiliates due 2023 was adjusted from 5.950% to 9.332%. See Note 7 – Debt for further information. As of December 31, 2016, there were no embedded derivatives subject to interest rate volatility related to the Senior Reset Notes to affiliates.

The fair value of our embedded derivatives was determined using a lattice-based valuation model by determining the fair value of the senior reset notes with and without the embedded derivatives included. The fair value of the senior reset notes with the embedded derivatives utilizes the contractual term of each senior reset note, reset rates calculated based on the spread between specified yield curves and the yield curve on certain T-Mobile long-term debt adjusted pursuant to the applicable supplemental indentures and interest rate volatility. Interest rate volatility is a significant unobservable input (Level 3) as it is derived based on weighted risk-free rate volatility and credit spread volatility. Significant increases or decreases in the weighting of risk-free volatility and credit spread volatility, in isolation, would result in a higher or lower fair value of the embedded derivatives. The embedded derivatives were classified as Level 3 in the fair value hierarchy.

The fair value of embedded derivative instruments by balance sheet location and level were as follows:

(in millions)	December 31, 2015			
	Level 1	Level 2	Level 3	Total
Other long-term liabilities	\$ —	\$ —	\$ 118	\$ 118

(in millions)	December 31, 2016			
	Level 1	Level 2	Level 3	Total
Other long-term liabilities	\$ —	\$ —	\$ 143	\$ 143

The following table summarizes the gain (loss) activity related to embedded derivatives instruments recognized in Interest expense to affiliates:

(in millions)	Year ended December 31,		
	2016	2015	2014
Embedded derivatives	\$ 25	\$ (148)	\$ 18

**Assets and Liabilities Measured at Fair Value on a Recurring Basis**

The carrying amounts and fair values of our short-term investments and long-term debt included in our Consolidated Balance Sheets were as follows:

(in millions)	Level within the Fair Value Hierarchy	December 31, 2016		December 31, 2015	
		Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Assets:</b>					
Short-term investments	1	\$ —	\$ —	\$ 2,998	\$ 2,998
Deferred purchase price assets	3	659	659	389	389
<b>Liabilities:</b>					
Senior Notes to third parties	1	\$ 18,600	\$ 19,584	\$ 17,600	\$ 18,098
Senior Reset Notes to affiliates	2	5,600	5,955	5,600	6,072
Senior Secured Term Loans	2	1,980	2,005	2,000	1,990
Guarantee Liabilities	3	135	135	163	163



Table of Contents***Short-term Investments***

The fair value of our short-term investments as of December 31, 2015, which consisted of U.S. Treasury securities, was determined based on quoted market prices in active markets, and therefore was classified as Level 1 in the fair value hierarchy. We did not have any short-term investments as of December 31, 2016.

***Long-term Debt***

The fair value of our Senior Notes to third parties was determined based on quoted market prices in active markets, and therefore was classified as Level 1 in the fair value hierarchy. The fair value of the Senior Secured Term Loans and Senior Reset Notes to affiliates was determined based on a discounted cash flow approach using quoted prices of instruments with similar terms and maturities and an estimate for our standalone credit risk. Accordingly, our Senior Secured Term Loans and Senior Reset Notes to affiliates were classified as Level 2 in the fair value hierarchy.

Although we have determined the estimated fair values using available market information and commonly accepted valuation methodologies, considerable judgment was required in interpreting market data to develop fair value estimates for the Senior Secured Term Loans and Senior Reset Notes to affiliates. The fair value estimates were based on information available as of December 31, 2016 and 2015. As such, our estimates are not necessarily indicative of the amount we could realize in a current market exchange.

***Deferred Purchase Price Assets***

In connection with the sales of certain service and EIP receivables pursuant to the sale arrangements, we have deferred purchase price assets measured at fair value that are based on a discounted cash flow model using unobservable Level 3 inputs, including customer default rates. See Note 3 – Sales of Certain Receivables.

***Guarantee Liabilities***

Our guarantee liabilities were valued based on various economic and customer behavioral assumptions, including expected trade-in period, volumes of trade-in, and the fair value of handsets traded in and therefore were classified as Level 3 in the fair value hierarchy.

The total estimated remaining gross EIP receivable balances of all enrolled handset upgrade program customers, which are the remaining EIP amounts underlying the JUMP! guarantee, including EIP receivables that have been sold, was \$2.1 billion as of December 31, 2016. This is not an indication of our expected loss exposure as it does not consider the expected fair value of the used handset or the probability and timing of the trade-in.

Table of Contents**Note 7 – Debt**

Debt was as follows:

(in millions)	December 31, 2016	December 31, 2015
5.250% Senior Notes due 2018	\$ 500	\$ 500
6.288% Senior Reset Notes to affiliates due 2019	1,250	1,250
6.464% Senior Notes due 2019	1,250	1,250
6.366% Senior Reset Notes to affiliates due 2020	1,250	1,250
6.542% Senior Notes due 2020	1,250	1,250
6.625% Senior Notes due 2020	1,000	1,000
6.250% Senior Notes due 2021	1,750	1,750
6.633% Senior Notes due 2021	1,250	1,250
8.097% Senior Reset Notes to affiliates due 2021	1,250	1,250
6.125% Senior Notes due 2022	1,000	1,000
6.731% Senior Notes due 2022	1,250	1,250
8.195% Senior Reset Notes to affiliates due 2022	1,250	1,250
6.000% Senior Notes due 2023	1,300	1,300
6.625% Senior Notes due 2023	1,750	1,750
6.836% Senior Notes due 2023	600	600
9.332% Senior Reset Notes to affiliates due 2023	600	600
6.000% Senior Notes due 2024	1,000	—
6.500% Senior Notes due 2024	1,000	1,000
6.375% Senior Notes due 2025	1,700	1,700
6.500% Senior Notes due 2026	2,000	2,000
Senior Secured Term Loans	1,980	2,000
Capital leases	1,425	826
Unamortized premium from purchase price allocation fair value adjustment	212	250
Unamortized discount on Senior Secured Term Loans	(8)	(10)
Debt issuance cost	(23)	(23)
Total debt	27,786	26,243
Less: Current portion of Senior Secured Term Loans	20	20
Less: Current portion of capital leases	334	162
Total long-term debt	\$ 27,432	\$ 26,061
 <b>Classified on the balance sheet as:</b>		
Long-term debt	\$ 21,832	\$ 20,461
Long-term debt to affiliates	5,600	5,600
Total long-term debt	\$ 27,432	\$ 26,061

**Long-term Debt**

In March 2016, T-Mobile USA, Inc. (“T-Mobile USA”), a subsidiary of T-Mobile US, Inc., and certain of its affiliates, as guarantors, entered into a purchase agreement with Deutsche Telekom AG (“Deutsche Telekom”), our majority stockholder, under which T-Mobile USA may, at its option, issue and sell to Deutsche Telekom \$2.0 billion of 5.300% Senior Notes due 2021 (the “5.300% Senior Notes”) for an aggregate purchase price of \$2.0 billion. As amended in October 2016, if T-Mobile USA does not elect to issue the 5.300% Senior Notes on or prior to May 5, 2017, the commitment under the purchase agreement terminates and T-Mobile USA must reimburse Deutsche Telekom for the cost of its hedging arrangements (if any) related to the transaction. As of December 31, 2016, if the commitment under this purchase agreement was terminated, the reimbursement amount due to Deutsche Telekom would not be

significant. In addition, T-Mobile USA is required to reimburse Deutsche Telekom for its cost of hedging arrangements related to the extension for the duration of the extended commitments, which is not expected to be significant.

In April 2016, T-Mobile USA and certain of its affiliates, as guarantors, (i) issued \$1.0 billion of public 6.000% Senior Notes due 2024, (ii) entered into a purchase agreement with Deutsche Telekom, under which T-Mobile USA may, at its option, issue

## Table of Contents

and sell to Deutsche Telekom up to \$1.35 billion of 6.000% Senior Notes due 2024 and (iii) entered into another purchase agreement with Deutsche Telekom, under which T-Mobile USA may, at its option, issue and sell up to an additional \$650 million of 6.000% Senior Notes due 2024.

The purchase price for the 6.000% Senior Notes that may be issued under the \$1.35 billion purchase agreement will be approximately 103.316% of the outstanding principal balance of the notes issued. As amended in October 2016, if T-Mobile USA does not elect to issue the 6.000% Senior Notes under the \$1.35 billion purchase agreement on or prior to May 5, 2017 or elects to issue less than \$1.35 billion of 6.000% Senior Notes, any unused portion of the commitment under the purchase agreement terminates and T-Mobile USA must reimburse Deutsche Telekom for the cost of its hedging arrangements (if any) related to the transaction. As of December 31, 2016, if the commitment under this purchase agreement was terminated, the reimbursement amount due to Deutsche Telekom would not be significant. In addition, T-Mobile USA is required to reimburse Deutsche Telekom for its cost of hedging arrangements related to the extension for the duration of the extended commitments, which is not expected to be significant.

The purchase price for the 6.000% Senior Notes that may be issued under the \$650 million purchase agreement will be approximately 104.047% of the outstanding principal balance of the notes issued. As amended in October 2016, if T-Mobile USA does not elect to issue the 6.000% Senior Notes under the \$650 million purchase agreement on or prior to May 5, 2017 or elects to issue less than \$650 million of 6.000% Senior Notes, any unused portion of the commitment under the purchase agreement terminates and T-Mobile USA must reimburse Deutsche Telekom for the cost of its hedging arrangements (if any) related to the transaction. As of December 31, 2016, if the commitment under this purchase agreement was terminated, the reimbursement amount due to Deutsche Telekom would not be significant. In addition, T-Mobile USA is required to reimburse Deutsche Telekom for its cost of hedging arrangements related to the extension for the duration of the extended commitments, which is not expected to be significant.

In January 2017, T-Mobile USA borrowed \$4.0 billion under a secured term loan facility ("Incremental Term Loan Facility") with Deutsche Telekom to refinance \$1.98 billion of outstanding secured term loans under its Term Loan Credit Agreement dated November 9, 2015, with the remaining net proceeds from the transaction intended to be used to redeem callable high yield debt. The loans under the Incremental Term Loan Facility were drawn in two tranches on January 31, 2017 (i) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.00% and will mature on November 9, 2022 and (ii) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.25% and will mature on January 31, 2024. The Incremental Term Loan Facility increases Deutsche Telekom's incremental term loan commitment provided to T-Mobile USA under that certain First Incremental Facility Amendment dated as of December 29, 2016 from \$660 million to \$2.0 billion and provides to T-Mobile USA an additional \$2.0 billion incremental term loan commitment. See Note 14 – Subsequent Events for further information.

In addition to the new debt issued, and purchase commitments with Deutsche Telekom, the supplemental indentures governing the Senior Reset Notes to affiliates provided for the adjustment of the interest rates on such Notes at various reset dates to rates determined in accordance with the applicable supplemental indenture. In April 2016, the interest rate on the \$600 million of Senior Reset Notes to affiliates due 2023 was adjusted from 5.950% to 9.332%.

## Capital Leases

Capital lease agreements relate to network and IT equipment with varying expiration terms through 2030. Future minimum payments required under capital leases, including interest, over their remaining terms are summarized below:

(in millions)	Future Minimum Payments
Year Ending December 31,	
2017	\$ 390
2018	354
2019	315
2020	200
2021	150
Thereafter	214
Total	<u>\$ 1,623</u>
Interest included	<u>\$ 198</u>

Table of Contents**Financing Arrangements**

We maintain a handset financing arrangement with Deutsche Bank AG (“Deutsche Bank”), which allows for up to \$108 million in borrowings. Under the handset financing arrangement, we can effectively extend payment terms for invoices payable to certain handset vendors. The interest rate on the handset financing arrangement is determined based on LIBOR plus a specified margin per the arrangement. Obligations under the handset financing arrangement are included in Short-term debt in our Consolidated Balance Sheets. In 2016 and 2015, we utilized and repaid \$100 million under the financing arrangement. As of December 31, 2016 and 2015, there was no outstanding balance.

We maintain vendor financing arrangements with our primary network equipment suppliers. Under the respective agreements, we can obtain extended financing terms. The interest rate on the vendor financing arrangements is determined based on the difference between LIBOR and a specified margin per the agreements. Obligations under the vendor financing arrangements are included in Short-term debt in our Consolidated Balance Sheets. As of December 31, 2016 and 2015, there was no outstanding balance.

**Revolving Credit Facility and Standby Letters of Credit**

We had an unsecured revolving credit facility with Deutsche Telekom which allowed for up to \$500 million in borrowings. In December 2016, we terminated our \$500 million unsecured revolving credit facility with Deutsche Telekom. As of December 31, 2016, there were no outstanding borrowings outstanding under this facility.

In December 2016, T-Mobile USA entered into a \$2.5 billion revolving credit facility with Deutsche Telekom which comprised of (i) a three-year \$1.0 billion unsecured revolving credit agreement and (ii) a three-year \$1.5 billion secured revolving credit agreement. The applicable margin for the Unsecured Revolving Credit Facility ranges from 2.00% to 3.25% per annum for Eurodollar Rate loans. The applicable margin for the Secured Revolving Credit Facility ranges from 1.00% to 1.75% per annum for Eurodollar Rate loans. As of December 31, 2016, there were no outstanding borrowings under the revolving credit facility.

For the purposes of securing our obligations to provide handset insurance services, we maintain an agreement for standby letters of credit with JP Morgan Chase Bank, N.A. (“JP Morgan Chase”). For purposes of securing our general purpose obligations, we maintain a letter of credit reimbursement agreement with Deutsche Bank.

The following table summarizes the outstanding standby letters of credit under each agreement:

(in millions)	December 31, 2016	December 31, 2015
JP Morgan Chase	\$ 20	\$ 36
Deutsche Bank	54	54
Total outstanding balance	<u>\$ 74</u>	<u>\$ 90</u>

**Note 8 – Tower Obligations**

In 2012, we conveyed to Crown Castle International Corp. (“CCI”) the exclusive right to manage and operate approximately 7,100 T-Mobile-owned wireless communication tower sites (“CCI Tower Sites”) in exchange for net proceeds of \$2.5 billion (“2012 Tower Transaction”). Rights to approximately 6,200 of the tower sites were transferred to CCI via a Master Prepaid Lease with site lease terms ranging from 23 to 37 years (“CCI Lease Sites”), while the remaining tower sites were sold to CCI (“CCI Sales Sites”). CCI has fixed-price purchase options for these towers totaling approximately \$2.0 billion, based on the estimated fair market value at the end of the lease term. We lease back space at certain tower sites for an initial term of ten years, followed by optional renewals at customary terms.

In 2015, we conveyed to Phoenix Tower International (“PTI”) the exclusive right to manage and operate approximately 600 T-Mobile-owned wireless communication tower sites (“PTI Tower Sites”) in exchange for net proceeds of approximately \$140 million (“2015 Tower Transaction”). As of December 31, 2016, rights to approximately 200 of the tower sites remain operated by PTI under a management agreement (“PTI Managed Sites”). We lease back space at certain tower sites for an initial term of ten years, followed by optional renewals at customary terms.

Assets and liabilities associated with the operation of certain of the tower sites were transferred to SPEs. Assets included ground lease agreements or deeds for the land on which the towers are situated, the towers themselves and existing subleasing agreements with other mobile network operator tenants, who lease space at the tower sites. Liabilities included the obligation



Table of Contents

to pay ground lease rentals, property taxes and other executory costs. Upon closing of the 2012 Tower Transaction, CCI acquired all of the equity interests in the SPEs containing CCI Sales Sites and an option to acquire the CCI Lease Sites at the end of their respective lease terms and entered into a master lease agreement under which we agreed to lease back space at certain of the tower sites. Upon closing of the 2015 Tower Transaction, PTI acquired all of the equity interests in the SPEs containing PTI Sales Sites and entered into a master lease agreement under which we agreed to lease back space at certain of the tower sites.

We determined the SPEs containing the CCI Lease Sites ("Lease Site SPEs") are VIEs as the Company's equity investment lacks the power to direct the activities that most significantly impact the economic performance of the VIEs. These activities include managing tenants and underlying ground leases, performing repair and maintenance on the towers, the obligation to absorb expected losses and the right to receive the expected future residual returns from the purchase option to acquire the CCI Lease Sites. As we determined that we are not the primary beneficiary and do not have a controlling financial interest in the Lease Site SPEs, the results of the Lease Site SPEs are not consolidated into our consolidated financial statements.

Due to our continuing involvement with the tower sites, we determined that we were precluded from applying sale-leaseback accounting. We recorded long-term financial obligations in the amount of the net proceeds received and recognized interest on the tower obligations at a rate of approximately 8% for the 2012 Tower Transaction and 3% for the 2015 Tower Transaction using the effective interest method. The tower obligations are increased by interest expense and amortized through contractual leaseback payments made by us to CCI or PTI and through estimated future net cash flows generated and retained by CCI or PTI from operation of the tower sites. Our historical tower site asset costs continue to be reported in Property and equipment, net in our Consolidated Balance Sheets and are depreciated.

The following table summarizes the impacts to the Consolidated Balance Sheets:

(in millions)	December 31, 2016	December 31, 2015
Property and equipment, net	\$ 485	\$ 601
Tower obligations	2,621	2,658

Future minimum payments related to the tower obligations are summarized below:

(in millions)	Future Minimum Payments
Year Ending December 31,	
2017	\$ 184
2018	184
2019	184
2020	185
2021	185
Thereafter	1,164
Total	<u>\$ 2,086</u>

We are contingently liable for future ground lease payments through the remaining term of the CCI Lease Sites. These contingent obligations are not included in the above table as any amount due is contractually owed by CCI based on the subleasing arrangement. See Note 12 – Commitments and Contingencies for further information.

#### Note 9 – Employee Compensation and Benefit Plans

Under our 2013 Omnibus Incentive Plan (the "Incentive Plan"), we are authorized to issue up to 63 million shares of our common stock. Under the Incentive Plan, we can grant stock options, stock appreciation rights, restricted stock, restricted stock units ("RSUs"), and performance awards to eligible employees, consultants, advisors and non-employee directors. As of December 31, 2016, there were 22 million shares of common stock available for future grants under the Incentive Plan.

We grant RSUs to eligible employees and certain non-employee directors and performance-based restricted stock units ("PRSUs") to eligible key executives. RSUs entitle the grantee to receive shares of our common stock at the end of a vesting period of generally up to 3 years, subject to continued service through the applicable vesting date. PRSUs entitle the holder to receive shares of our common stock at the end of a vesting period of generally up to 3 years if the applicable performance goals are achieved and generally subject to continued employment through the vesting period. The number of shares ultimately

Table of Contents

received by the holder of PRSUs is dependent on our business performance against the specified performance goal(s) over a pre-established performance period. We also maintain an employee stock purchase plan ("ESPP"), under which eligible employees can purchase our common stock at a discounted price.

Stock-based compensation expense and related income tax benefits were as follows:

(in millions, except shares, per share and contractual life amounts)	December 31, 2016	December 31, 2015	December 31, 2014
Stock-based compensation expense	\$ 235	\$ 201	\$ 196
Income tax benefit related to stock-based compensation	80	71	73
Realized excess tax benefit	—	79	34
Weighted average fair value per stock award granted	45.07	35.56	28.52
Unrecognized compensation expense	389	327	271
Weighted average period to be recognized (years)	2.0	2.0	1.9
Fair value of stock awards vested	354	445	209

**Stock Awards***RSU and PRSU Awards*

The following activity occurred under the RSU and PRSU awards:

(in millions, except shares, per share and contractual life amounts)	Number of Units	Weighted Average Grant Date Fair Value	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Nonvested, December 31, 2015	16,334,271	\$ 29.95	1.2	\$ 639
Granted	8,431,980	45.07		
Vested	(7,712,463)	28.33		
Forfeited	(1,338,397)	34.42		
Nonvested, December 31, 2016	15,715,391	\$ 37.93	1.1	\$ 904

Payment of the underlying shares in connection with the vesting of stock awards generally triggers a tax obligation for the employee, which is required to be remitted to the relevant tax authorities. We have agreed to withhold stock otherwise issuable under the award to cover certain of these tax obligations, with the net shares issued to the employee accounted for as outstanding common stock. We withheld 2,605,807 and 4,176,464 shares of stock to cover tax obligations associated with the payment of shares upon vesting of stock awards and remitted cash of \$121 million and \$156 million to the appropriate tax authorities for the years ended December 31, 2016 and 2015, respectively.

**Employee Stock Purchase Plan**

Our ESPP allows eligible employees to contribute up to 15% of their eligible earnings toward the semi-annual purchase of our common stock at a discounted price, subject to an annual maximum dollar amount. Employees can purchase stock at a 15% discount applied to the closing stock price on the first or last day of the six month offering period, whichever price is lower. The number of shares issued under our ESPP was 1,905,534 and 761,085 for the years ended December 31, 2016 and 2015, respectively.

**Stock Options**

Prior to the business combination, MetroPCS had established the MetroPCS Communications, Inc. 2010 Equity Incentive Compensation Plan, the Amended and Restated MetroPCS Communications, Inc. 2004 Equity Incentive Compensation Plan and the Second Amended and Restated 1995 Stock Option Plan ("Predecessor Plans"). Following stockholder approval of the Incentive Plan, no new awards have been or may be granted under the Predecessor Plans.

Table of Contents

The following activity occurred under the Predecessor Plans:

	Stock	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)
Outstanding and exercisable, December 31, 2015	1,824,354	\$ 30.50	2.7
Exercised	(982,904)	29.34	
Expired	(7,519)	44.21	
Outstanding and exercisable, December 31, 2016	833,931	\$ 31.75	2.3

Stock options exercised under the Predecessor Plans generated proceeds of approximately \$29 million and \$47 million for the years ended December 31, 2016 and 2015, respectively.

**Employee Retirement Savings Plan**

We sponsor a retirement savings plan for the majority of our employees under section 401(k) of the Internal Revenue Code and similar plans. The plans allow employees to contribute a portion of their pretax income in accordance with specified guidelines. The plans provide that we match a percentage of employee contributions up to certain limits. Employer matching contributions were \$83 million, \$73 million and \$66 million for the years ended December 31, 2016, 2015 and 2014, respectively.

**Legacy Long Term Incentive Plan**

Prior to the business combination with MetroPCS Communications, Inc., we maintained a performance-based Long Term Incentive Plan ("LTIP") which aligned to our long-term business strategy. As of December 31, 2016, there were no LTIP awards outstanding and no new awards are expected to be granted under the LTIP.

Compensation expense reported within operating expenses related to our LTIP and payments to participants related to our LTIP were as follows:

(in millions)	December 31, 2016	December 31, 2015	December 31, 2014
Compensation expense	\$ —	\$ 27	\$ 44
Payments	52	57	60

**Note 10 – Income Taxes**

Our sources of income before income taxes were as follows:

(in millions)	Year Ended December 31,		
	2016	2015	2014
U.S.	\$ 2,286	\$ 898	\$ 347
Puerto Rico	41	80	66
Income before income taxes	\$ 2,327	\$ 978	\$ 413

Table of Contents

Income tax expense is summarized as follows:

(in millions)	Year Ended December 31,		
	2016	2015	2014
Current tax expense (benefit)			
Federal	\$ (66)	\$ (30)	\$ —
State	29	2	6
Puerto Rico	(10)	17	38
Total current tax expense (benefit)	(47)	(11)	44
Deferred tax expense (benefit)			
Federal	804	281	79
State	96	(37)	40
Puerto Rico	14	12	3
Total deferred tax expense	914	256	122
Total income tax expense	\$ 867	\$ 245	\$ 166

The reconciliation between the U.S. federal statutory income tax rate and our effective income tax rate is as follows:

	Year Ended December 31,		
	2016	2015	2014
Federal statutory income tax rate	35.0 %	35.0 %	35.0 %
State taxes, net of federal benefit	4.0	(1.1)	(8.8)
Puerto Rico taxes, net of federal benefit	—	3.3	5.0
Change in valuation allowance	1.0	(3.2)	18.8
Permanent differences	0.6	1.6	1.4
Federal tax credits, net of reserves	(0.5)	(9.5)	(10.6)
Equity-based compensation	(2.2)	—	—
Other, net	(0.6)	(1.0)	(0.6)
Effective income tax rate	37.3 %	25.1 %	40.2 %

Significant components of deferred income tax assets and liabilities, tax effected, are as follows:

(in millions)	December 31, 2015	December 31, 2014
Deferred tax assets		
Loss carryforwards	\$ 1,442	\$ 1,997
Deferred rents	1,153	1,136
Reserves and accruals	1,058	928
Federal and state tax credits	284	349
Debt fair market value adjustment	83	97
Other	430	317
Deferred tax assets, gross	4,450	4,824
Valuation allowance	(573)	(583)
Deferred tax assets, net	3,877	4,241
Deferred tax liabilities		
Spectrum licenses	6,952	6,174
Property and equipment	1,732	1,950
Other intangible assets	119	178
Other	12	—
Total deferred tax liabilities	8,815	8,302

Net deferred tax liabilities

\$	4,938	\$	4,061
----	-------	----	-------

**Classified on the balance sheet as:**

Deferred tax liabilities

\$	4,938	\$	4,061
----	-------	----	-------

Table of Contents

As of December 31, 2016, we have net operating loss ("NOL") carryforwards, tax effected, of \$1.1 billion for federal income tax purposes and \$689 million for state income tax purposes, expiring through 2036. As of December 31, 2016, our federal and state NOL carryforwards for financial reporting purposes were approximately \$204 million and \$167 million, respectively, tax effected, less than our NOL carryforwards for federal and state income tax purposes, due to unrecognized tax benefits of the same amount.

As of December 31, 2016, we have available Alternative Minimum Tax credit carryforwards of \$89 million, which may be used to reduce regular federal income taxes and have no expiration. We also have research and development and foreign tax credit carryforwards of \$174 million for federal income tax purposes, which begin to expire in 2018.

As of December 31, 2016 and 2015, our valuation allowance was \$573 million and \$583 million, respectively. The change in the valuation allowance of \$10 million is primarily related to the adoption of ASU 2016-09 and the related release of a \$33 million valuation allowance on stock option deductions included in NOL carryforwards, partially offset by 2016 activity related to state deferred tax assets for which a valuation allowance exists. Based on recent earnings in certain jurisdictions, sufficient positive evidence may exist within the next twelve months such that we may release a portion of our valuation allowance.

We file income tax returns in the U.S. federal jurisdiction, various state jurisdictions and in Puerto Rico. We are currently under examination by various states. Management does not believe the resolution of any of the audits will result in a material change to our financial condition, results of operations or cash flows. The IRS has concluded its audits of our federal tax returns through the 2013 tax year, however, NOL carryforwards for certain audited periods remain open for examination. We are generally closed to U.S. federal, state and Puerto Rico examination for years prior to 1998.

A reconciliation of the beginning and ending amount of unrecognized tax benefits were as follows:

(in millions)	Year Ended December 31,		
	2016	2015	2014
Unrecognized tax benefits, beginning of year	\$ 411	\$ 388	\$ 178
Gross decreases to tax positions in prior periods	(5)	(112)	(52)
Gross increases to current period tax positions	4	135	262
Unrecognized tax benefits, end of year	<u>\$ 410</u>	<u>\$ 411</u>	<u>\$ 388</u>

As of December 31, 2016 and 2015, we had \$168 million and \$163 million, respectively, in unrecognized tax benefits that, if recognized, would affect our annual effective tax rate. Penalties and interest on income tax assessments are included in Selling, general and administrative expenses and Interest expense, respectively, in our Consolidated Statements of Comprehensive Income. The accrued interest and penalties associated with unrecognized tax benefits are insignificant.

Table of Contents**Note 11 – Earnings Per Share**

The computation of basic and diluted earnings per share was as follows:

(in millions, except shares and per share amounts)	Year Ended December 31,		
	2016	2015	2014
Net income	\$ 1,460	\$ 733	\$ 247
Less: Dividends on mandatory convertible preferred stock	(55)	(55)	—
Net income attributable to common stockholders - basic and diluted	\$ 1,405	\$ 678	\$ 247
Weighted average shares outstanding - basic	822,470,275	812,994,028	805,284,712
Effect of dilutive securities:			
Outstanding stock options and unvested stock awards	10,584,270	9,623,910	8,893,887
Mandatory convertible preferred stock	—	—	1,743,659
Weighted average shares outstanding - diluted	833,054,545	822,617,938	815,922,258
Earnings per share - basic	\$ 1.71	\$ 0.83	\$ 0.31
Earnings per share - diluted	\$ 1.69	\$ 0.82	\$ 0.30
Potentially dilutive securities:			
Outstanding stock options and unvested stock awards	3,528,683	4,842,370	1,426,331
Mandatory convertible preferred stock	32,237,266	32,237,266	—

Potentially dilutive securities were not included in the computation of diluted earnings per share if to do so would have been anti-dilutive.

**Note 12 – Commitments and Contingencies****Commitments*****Operating Leases and Purchase Commitments***

Future minimum payments for non-cancelable operating leases and purchase commitments are summarized below:

(in millions)	Operating Leases	Purchase Commitments
Year Ending December 31,		
2017	\$ 2,417	\$ 2,011
2018	2,118	977
2019	1,832	841
2020	1,511	704
2021	1,102	626
Thereafter	2,188	960
Total	\$ 11,168	\$ 6,119

***Operating Leases***

We have operating leases for cell sites, switch sites, retail stores and office facilities with contractual terms expiring through 2026.

The majority of cell site leases have an initial non-cancelable term of five years to ten years with several renewal options. Historically, our assessment of cell site lease terms included renewal options on certain cell site leases which were reasonably assured of exercise and we had included such renewal options in the future minimum lease payments presented in the Operating Lease and Purchase Commitments table, above. As of December 31, 2016, we have updated the future minimum lease payments for all cell site leases

presented above to include only payments due for the initial non-cancelable lease term as they represent the payments which we cannot avoid at our option and also correspond to our lease term assessment for new leases. This update had the effect of reducing our contractual operating lease commitments included in the table above by \$4.6

## Table of Contents

billion as of December 31, 2016.

In addition, we have operating leases for dedicated transportation lines with varying expiration terms through 2026.

As of December 31, 2016, we were contingently liable for future ground lease payments related to the tower obligations. These contingent obligations are not included in the above table as the amounts due are contractually owed by CCI based on the subleasing arrangement. See Note 8 – Tower Obligations for further information.

Total rent expense under operating leases, including dedicated transportation lines, was \$2.8 billion, \$2.8 billion and \$3.0 billion for the years ended December 31, 2016, 2015 and 2014, respectively, and is classified as Cost of services and Selling, general and administrative in our Consolidated Statements of Comprehensive Income.

### ***Purchase Commitments***

We have commitments for non-dedicated transportation lines with varying expiration terms through 2028. In addition, we have commitments to purchase spectrum licenses, handsets, network services, equipment, software, marketing sponsorship agreements and other items in the ordinary course of business, with various terms through 2028. These amounts are not reflective of our entire anticipated purchases under the related agreements, but are determined based on the non-cancelable quantities or termination amounts to which we are contractually obligated.

### ***Related-Party Commitments***

In 2016, T-Mobile USA entered into three purchase agreements with Deutsche Telekom under which T-Mobile USA may, at its option, issue and sell to Deutsche Telekom certain Senior Notes. The purchase agreements were amended in October 2016. See Note 7 – Debt for further information.

In January 2017, T-Mobile USA borrowed \$4.0 billion under a secured term loan facility (“Incremental Term Loan Facility”) with Deutsche Telekom to refinance \$1.98 billion of outstanding secured term loans under its Term Loan Credit Agreement dated November 9, 2015, with the remaining net proceeds from the transaction intended to be used to redeem callable high yield debt. The loans under the Incremental Term Loan Facility were drawn in two tranches on January 31, 2017 (i) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.00% and will mature on November 9, 2022 and (ii) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.25% and will mature on January 31, 2024. The Incremental Term Loan Facility increases Deutsche Telekom’s incremental term loan commitment provided to T-Mobile USA under that certain First Incremental Facility Amendment dated as of December 29, 2016 from \$660 million to \$2.0 billion and provides to T-Mobile USA an additional \$2.0 billion incremental term loan commitment. See Note 14 – Subsequent Events for further information.

In December 2016, T-Mobile USA also entered into a \$2.5 billion revolving credit facility with Deutsche Telekom which comprised of (i) a three-year \$1.0 billion senior unsecured revolving credit agreement and (ii) a three-year \$1.5 billion senior secured revolving credit agreement. As of December 31, 2016, there were no outstanding borrowings under the revolving credit facility. See Note 7 – Debt for further information.

### ***Contingencies and Litigation***

We are involved in various lawsuits, claims, government agency investigations and enforcement actions, and other proceedings (“Litigation Matters”) that arise in the ordinary course of business, which include numerous court actions alleging that we are infringing various patents. Virtually all of the patent infringement cases are brought by non-practicing entities and effectively seek only monetary damages, although they occasionally seek injunctive relief as well. The Litigation Matters described above have progressed to various stages and some of them may proceed to trial, arbitration, hearing or other adjudication that could include an award of monetary or injunctive relief in the coming 12 months, if they are not otherwise resolved. We have established an accrual with respect to certain of these matters, where appropriate, which is reflected in the consolidated financial statements but that we do not consider, individually or in the aggregate, material. An accrual is established when we believe it is both probable that a loss has been incurred and an amount can be reasonably estimated. For other matters, where we have not determined that a loss is probable or because the amount of loss cannot be reasonably estimated, we have not recorded an accrual due to various factors typical in contested proceedings, including but not limited to: uncertainty concerning legal theories and their resolution by courts or regulators; uncertain damage theories and demands; and a less than fully developed factual record. While we do not expect that the ultimate resolution of these proceedings, individually or in the aggregate will have a material adverse effect on our financial position, an unfavorable outcome of some or all of these proceedings could have a material adverse impact on results of operations or cash flows for a particular period. This



Table of Contents

assessment is based on our current understanding of relevant facts and circumstances. As such, our view of these matters is subject to inherent uncertainties and may change in the future.

**Note 13 – Additional Financial Information****Supplemental Consolidated Balance Sheets Information***Allowances and Imputed Discount*

The following table summarizes the changes in allowances and unamortized imputed discount related to our current accounts receivables and EIP receivables:

(in millions)	2016	2015	2014
Allowances, beginning of year	\$ 264	\$ 199	\$ 169
Bad debt expense	477	547	444
Write-offs, net of recoveries	(518)	(482)	(414)
Allowances, end of year	<u>\$ 223</u>	<u>\$ 264</u>	<u>\$ 199</u>
Imputed discount, beginning of year	\$ 159	\$ 271	\$ 212
Additions	362	310	380
Interest income	(248)	(414)	(355)
Cancellations and other	(47)	(78)	(92)
Impacts from sales of EIP receivables	(152)	(55)	—
Transfer from long-term	100	125	126
Imputed discount, end of year	<u>\$ 174</u>	<u>\$ 159</u>	<u>\$ 271</u>

The following table summarizes the changes in unamortized imputed discount related to our long-term EIP receivables:

(in millions)	2016	2015	2014
Imputed discount, beginning of year	\$ 26	\$ 61	\$ 64
Additions	134	111	141
Cancellations and other	(15)	(13)	(18)
Impacts from sales of EIP receivables	(24)	(8)	—
Transfer to current	(100)	(125)	(126)
Imputed discount, end of year	<u>\$ 21</u>	<u>\$ 26</u>	<u>\$ 61</u>

See Note 3 – Sales of Certain Receivables on sales of EIP receivables and Note 2 – Equipment Installment Plan Receivables on EIP receivables and related unamortized imputed discount and allowance for credit losses for further information.

*Accounts Payable and Accrued Liabilities*

Accounts payable and accrued liabilities are summarized as follows:

(in millions)	December 31, 2016	December 31, 2015
Accounts payable	\$ 5,163	\$ 6,137
Payroll and related benefits	559	521
Property and other taxes, including payroll	525	494
Interest	423	371
Commissions	159	190
Network decommissioning	101	117
Toll and interconnect	85	68
Advertising	44	77

7/20/2017

Document

Other

93

109

Accounts payable and accrued liabilities

\$	7,152	\$	8,084
----	-------	----	-------

82

Table of Contents

Book overdrafts included in accounts payable and accrued liabilities were \$356 million and \$501 million as of December 31, 2016 and 2015, respectively.

**Other**

In June 2016, we made a refundable deposit of \$2.2 billion to a third party in connection with a potential asset purchase. The deposit is included in Asset purchase deposit in our Consolidated Balance Sheets.

During the quarter ended and subsequent to September 30, 2016, a handset Original Equipment Manufacturer ("OEM") announced recalls on certain of its smartphone devices. As a result, we recorded no revenue associated with the device sales to customers and impaired the devices to their net realizable value. The OEM has agreed to reimburse T-Mobile, as such, we have recorded an amount due from the OEM as an offset to the loss recorded in Cost of equipment sales in our Consolidated Statements of Comprehensive Income and a reduction to Accounts payable and accrued liabilities in our Consolidated Balance Sheets.

**Supplemental Consolidated Statements of Comprehensive Income Information****Related Party Transactions**

We have related party transactions associated with Deutsche Telekom or its affiliates in the ordinary course of business, which are included in the consolidated financial statements.

The following table summarizes the impact of significant transactions with Deutsche Telekom or its affiliates included in operating expenses in the Consolidated Statements of Comprehensive Income:

(in millions)	Year Ended December 31,		
	2016	2015	2014
Discount related to roaming expenses	\$ (15)	\$ (21)	\$ (61)
Fees incurred for use of the T-Mobile brand	74	65	60
Expenses for telecommunications and IT services	25	23	24
International long distance agreement	60	—	—

We have an agreement with Deutsche Telekom for the reimbursement of certain administrative expenses, which were \$11 million and \$2 million for the years ended December 31, 2016 and 2015, respectively. There were no reimbursements for the year ended December 31, 2014.

**Supplemental Consolidated Statement of Stockholders' Equity Information****Preferred Stock**

In 2014, we completed a public offering of 20 million shares of mandatory convertible preferred stock for net proceeds of \$982 million. Dividends on the preferred stock are payable on a cumulative basis when and if declared by our board of directors at an annual rate of 5.5%. The dividends may be paid in cash, shares of common stock, subject to certain limitations, or any combination of cash and shares of common stock.

Unless converted earlier, each share of preferred stock will convert automatically on December 15, 2017 into between 1.6119 and 1.9342 shares of common stock, subject to customary anti-dilution adjustments, depending on the applicable market value of the common stock. At any time, the preferred shares may be converted, in whole or in part, at the minimum conversion rate of 1.6119 shares of common stock, except during a fundamental change conversion period. In addition, holders may be entitled to shares based on the amount of accumulated and unpaid dividends. If certain fundamental changes involving the Company occur, the preferred stock may be converted into common shares at the applicable conversion rate, subject to certain anti-dilution adjustments, and holders will also be entitled to a make-whole amount. The preferred stock ranks senior with respect to liquidation preference and dividend rights to common stock. In the event of any voluntary or involuntary liquidation, winding-up or dissolution of the Company, each holder of preferred stock will be entitled to receive a liquidation preference in the amount of \$50 per share, plus an amount equal to accumulated and unpaid dividends, after satisfaction of liabilities to our creditors and before any distribution or payment is made to any holders of common stock. The preferred stock is not redeemable.



Table of Contents**Note 14 – Subsequent Events**

In January 2017, we delivered a notice of redemption on \$1.0 billion aggregate principal amount of our 6.625% Senior Notes due 2020. The notes were redeemed on February 10, 2017 at a redemption price equal to 102.208% of the principal amount of the notes (plus accrued and unpaid interest thereon).

In January 2017, T-Mobile USA borrowed \$4.0 billion under a secured term loan facility (“Incremental Term Loan Facility”) with Deutsche Telekom to refinance \$1.98 billion of outstanding secured term loans under its Term Loan Credit Agreement dated November 9, 2015, with the remaining net proceeds from the transaction intended to be used to redeem callable high yield debt. The loans under the Incremental Term Loan Facility were drawn in two tranches on January 31, 2017 (i) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.00% and will mature on November 9, 2022 and (ii) \$2.0 billion of which will bear interest at a rate equal to a per annum rate of LIBOR plus a margin of 2.25% and will mature on January 31, 2024. The Incremental Term Loan Facility increases Deutsche Telekom’s incremental term loan commitment provided to T-Mobile USA under that certain First Incremental Facility Amendment dated as of December 29, 2016 from \$660 million to \$2.0 billion and provides to T-Mobile USA an additional \$2.0 billion incremental term loan commitment.

In February 2017, we delivered a notice of redemption on \$500 million aggregate principal amount of our 5.250% Senior Notes due 2018. The notes will be redeemed on March 6, 2017 at a redemption price equal to 101.313% of the principal amount of the notes (plus accrued and unpaid interest thereon).

**Note 15 – Guarantor Financial Information**

Pursuant to the applicable indentures and supplemental indentures, the long-term debt to affiliates and third parties, excluding Senior Secured Term Loans and capital leases, issued by T-Mobile USA (“Issuer”) is fully and unconditionally guaranteed, jointly and severally, on a senior unsecured basis by T-Mobile (“Parent”) and certain of the Issuer’s 100% owned subsidiaries (“Guarantor Subsidiaries”).

In April 2016, T-Mobile USA and certain of its affiliates, as guarantors, issued \$1.0 billion of public 6.000% Senior Notes due 2024.

The guarantees of the Guarantor Subsidiaries are subject to release in limited circumstances only upon the occurrence of certain customary conditions. The indentures governing the long-term debt contain covenants that, among other things, limit the ability of the Issuer and the Guarantor Subsidiaries to: incur more debt; pay dividends and make distributions; make certain investments; repurchase stock; create liens or other encumbrances; enter into transactions with affiliates; enter into transactions that restrict dividends or distributions from subsidiaries; and merge, consolidate, or sell, or otherwise dispose of, substantially all of their assets. Certain provisions of each of the indentures and the supplemental indentures relating to the long-term debt restrict the ability of the Issuer to loan funds or make payments to Parent. However, the Issuer and Guarantor Subsidiaries are allowed to make certain permitted payments to the Parent under the terms of the indentures and the supplemental indentures.

Presented below is the condensed consolidating financial information as of December 31, 2016 and 2015 and for the years ended December 31, 2016, 2015 and 2014.

Table of Contents

**Condensed Consolidating Balance Sheet Information**  
**December 31, 2016**

(in millions)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating and Eliminating Adjustments	Consolidated
<b>Assets</b>					
<b>Current assets</b>					
Cash and cash equivalents	\$ 358	\$ 2,733	\$ 2,342	\$ 67	\$ 5,500
Accounts receivable, net	—	—	1,675	221	1,896
Equipment installment plan receivables, net	—	—	1,930	—	1,930
Accounts receivable from affiliates	—	—	40	—	40
Inventories	—	—	1,111	—	1,111
Asset purchase deposit	—	—	2,203	—	2,203
Other current assets	—	—	972	565	1,537
<b>Total current assets</b>	<b>358</b>	<b>2,733</b>	<b>10,273</b>	<b>853</b>	<b>14,217</b>
Property and equipment, net <sup>(1)</sup>	—	—	20,568	375	20,943
Goodwill	—	—	1,683	—	1,683
Spectrum licenses	—	—	27,014	—	27,014
Other intangible assets, net	—	—	376	—	376
Investments in subsidiaries, net	17,682	35,095	—	(52,777)	—
Intercompany receivables	196	6,826	—	(7,022)	—
Equipment installment plan receivables due after one year, net	—	—	984	—	984
Other assets	—	7	600	262	674
<b>Total assets</b>	<b>\$ 18,236</b>	<b>\$ 44,661</b>	<b>\$ 61,498</b>	<b>\$ 1,490</b>	<b>\$ 65,891</b>
<b>Liabilities and Stockholders' Equity</b>					
<b>Current liabilities</b>					
Accounts payable and accrued liabilities	\$ —	\$ 423	\$ 6,474	\$ 255	\$ 7,152
Payables to affiliates	—	79	46	—	125
Short-term debt	—	20	334	—	354
Deferred revenue	—	—	986	—	986
Other current liabilities	—	—	258	147	405
<b>Total current liabilities</b>	<b>—</b>	<b>522</b>	<b>8,098</b>	<b>402</b>	<b>9,022</b>
Long-term debt	—	20,741	1,091	—	21,832
Long-term debt to affiliates	—	5,600	—	—	5,600
Tower obligations <sup>(1)</sup>	—	—	400	2,221	2,621
Deferred tax liabilities	—	—	5,133	—	4,938
Deferred rent expense	—	—	2,616	—	2,616
Negative carrying value of subsidiaries, net	—	—	568	—	(568)
Intercompany payables	—	—	6,785	237	(7,022)
Other long-term liabilities	—	116	906	4	1,026
<b>Total long-term liabilities</b>	<b>—</b>	<b>26,457</b>	<b>17,499</b>	<b>2,462</b>	<b>38,633</b>
<b>Total stockholders' equity (deficit)</b>	<b>18,236</b>	<b>17,682</b>	<b>35,901</b>	<b>(1,374)</b>	<b>18,236</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 18,236</b>	<b>\$ 44,661</b>	<b>\$ 61,498</b>	<b>\$ 1,490</b>	<b>\$ 65,891</b>

(1) Assets and liabilities for Non-Guarantor Subsidiaries are primarily included in VIEs related to the 2012 Tower Transaction. See Note 5 – Tower Obligations for further information.



Table of Contents

**Condensed Consolidating Balance Sheet Information**  
**December 31, 2015**

(in millions)	Parent	Issuer	Consolidator Subsidiaries	Non-Guarantor Subsidiaries	Consolidating and Eliminating Adjustments	Consolidated
<b>Assets</b>						
<b>Current assets</b>						
Cash and cash equivalents	\$ 378	\$ 1,767	\$ 2,364	\$ 73	\$ —	\$ 4,582
Short-term investments	—	1,999	999	—	—	2,998
Accounts receivable, net	—	—	1,574	214	—	1,788
Equipment installment plan receivables, net	—	—	2,378	—	—	2,378
Accounts receivable from affiliates	—	—	36	—	—	36
Inventories	—	—	1,295	—	—	1,295
Other current assets	—	—	1,413	400	—	1,813
<b>Total current assets</b>	<b>378</b>	<b>3,766</b>	<b>10,059</b>	<b>687</b>	<b>—</b>	<b>14,890</b>
Property and equipment, net <sup>(1)</sup>	—	—	19,546	454	—	20,000
Goodwill	—	—	1,683	—	—	1,683
Spectrum licenses	—	—	23,955	—	—	23,955
Other intangible assets, net	—	—	594	—	—	594
Investments in subsidiaries, net	16,184	32,280	—	—	(48,464)	—
Intercompany receivables	—	6,130	—	—	(6,130)	—
Equipment installment plan receivables due after one year, net	—	—	847	—	—	847
Other assets	—	5	387	219	(167)	444
<b>Total assets</b>	<b>\$ 16,562</b>	<b>\$ 42,181</b>	<b>\$ 57,071</b>	<b>\$ 1,360</b>	<b>\$ (54,761)</b>	<b>\$ 62,413</b>
<b>Liabilities and Stockholders' Equity</b>						
<b>Current liabilities</b>						
Accounts payable and accrued liabilities	\$ —	\$ 368	\$ 7,496	\$ 220	\$ —	\$ 8,084
Payables to affiliates	—	70	65	—	—	135
Short-term debt	—	20	162	—	—	182
Deferred revenue	—	—	717	—	—	717
Other current liabilities	—	—	327	83	—	410
<b>Total current liabilities</b>	<b>—</b>	<b>458</b>	<b>8,767</b>	<b>303</b>	<b>—</b>	<b>9,528</b>
Long-term debt	—	19,797	664	—	—	20,461
Long-term debt to affiliates	—	5,600	—	—	—	5,600
Tower obligations <sup>(1)</sup>	—	—	411	2,247	—	2,658
Deferred tax liabilities	—	—	4,228	—	(167)	4,061
Deferred rent expense	—	—	2,481	—	—	2,481
Negative carrying value of subsidiaries, net	—	—	628	—	(628)	—
Intercompany payables	5	—	5,959	166	(6,130)	—
Other long-term liabilities	—	142	922	3	—	1,067
<b>Total long-term liabilities</b>	<b>5</b>	<b>25,539</b>	<b>15,293</b>	<b>2,416</b>	<b>(6,925)</b>	<b>36,328</b>
<b>Total stockholders' equity (deficit)</b>	<b>16,557</b>	<b>16,184</b>	<b>33,011</b>	<b>(1,359)</b>	<b>(47,836)</b>	<b>16,557</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 16,562</b>	<b>\$ 42,181</b>	<b>\$ 57,071</b>	<b>\$ 1,360</b>	<b>\$ (54,761)</b>	<b>\$ 62,413</b>

(1) Assets and liabilities for Non-Guarantor Subsidiaries are primarily included in VIEs related to the 2012 Tower Transaction. See Note 8 – Tower Obligations for further information.



Table of Contents

**Condensed Consolidating Statement of Comprehensive Income Information**  
**Year Ended December 31, 2016**

(in millions)	Parent	Sons	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating and Eliminating Adjustments	Consolidated
<b>Revenues</b>						
Service revenues	\$ —	\$ —	\$ 26,613	\$ 2,023	\$ (792)	\$ 27,844
Equipment revenues	—	—	9,145	—	(418)	8,727
Other revenues	—	3	491	195	(18)	671
Total revenues	—	3	36,249	2,218	(1,228)	37,242
<b>Operating expenses</b>						
Cost of services, exclusive of depreciation and amortization shown separately below	—	—	5,707	24	—	5,731
Cost of equipment sales	—	—	10,209	1,027	(417)	10,819
Selling, general and administrative	—	—	11,321	868	(811)	11,378
Depreciation and amortization	—	—	6,165	78	—	6,243
Cost of MetroPCS business combination	—	—	104	—	—	104
Gains on disposal of spectrum licenses	—	—	(835)	—	—	(835)
Total operating expenses	—	—	32,671	1,997	(1,228)	33,440
Operating income	—	3	3,578	221	—	3,802
<b>Other income (expense)</b>						
Interest expense	—	(1,147)	(82)	(189)	—	(1,418)
Interest expense to affiliates	—	(312)	—	—	—	(312)
Interest income	—	31	230	—	—	261
Other income (expense), net	—	2	(8)	—	—	(6)
Total other income (expense), net	—	(1,426)	140	(189)	—	(1,475)
Income (loss) before income taxes	—	(1,423)	3,718	32	—	2,327
Income tax expense	—	—	(857)	(10)	—	(867)
Earnings (loss) of subsidiaries	1,460	2,883	(17)	—	(4,326)	—
Net income	1,460	1,460	2,844	22	(4,326)	1,460
Dividends on preferred stock	(55)	—	—	—	—	(55)
Net income attributable to common stockholders	\$ 1,405	\$ 1,460	\$ 2,844	\$ 22	\$ (4,326)	\$ 1,405
Net Income	\$ 1,460	\$ 1,460	\$ 2,844	\$ 22	\$ (4,326)	\$ 1,460
<b>Other comprehensive income, net of tax</b>						
Other comprehensive income, net of tax	2	2	2	2	(6)	2
Total comprehensive income	\$ 1,462	\$ 1,462	\$ 2,846	\$ 24	\$ (4,332)	\$ 1,462

Table of Contents

**Condensed Consolidating Statement of Comprehensive Income Information**  
**Year Ended December 31, 2015**

(in millions)	Parent	Issuer	Controlled Subsidiaries	Non-Controlled Subsidiaries	Consolidating and Eliminating Adjustments	Consolidated
<b>Revenues</b>						
Service revenues	\$ —	\$ —	\$ 23,748	\$ 1,669	\$ (596)	\$ 24,821
Equipment revenues	—	—	7,148	—	(430)	6,718
Other revenues	—	1	356	171	(14)	514
Total revenues	—	1	31,252	1,840	(1,040)	32,053
<b>Operating expenses</b>						
Cost of services, exclusive of depreciation and amortization shown separately below	—	—	5,530	24	—	5,554
Cost of equipment sales	—	—	9,055	720	(431)	9,344
Selling, general and administrative	—	—	10,065	733	(609)	10,189
Depreciation and amortization	—	—	4,605	83	—	4,688
Cost of MetroPCS business combination	—	—	376	—	—	376
Gains on disposal of spectrum licenses	—	—	(163)	—	—	(163)
Total operating expenses	—	—	29,468	1,560	(1,040)	29,988
Operating income	—	1	1,784	280	—	2,065
<b>Other income (expense)</b>						
Interest expense	—	(847)	(50)	(188)	—	(1,085)
Interest expense to affiliates	—	(411)	—	—	—	(411)
Interest income	—	2	418	—	—	420
Other expense, net	—	(10)	—	(1)	—	(11)
Total other income (expense), net	—	(1,266)	368	(189)	—	(1,087)
Income (loss) before income taxes	—	(1,265)	2,152	91	—	978
Income tax expense	—	—	(214)	(31)	—	(245)
Earnings (loss) of subsidiaries	733	1,998	(48)	—	(2,683)	—
Net income	733	733	1,890	60	(2,683)	733
Dividends on preferred stock	(55)	—	—	—	—	(55)
Net income attributable to common stockholders	\$ 678	\$ 733	\$ 1,890	\$ 60	\$ (2,683)	\$ 678
Net income	\$ 733	\$ 733	\$ 1,890	\$ 60	\$ (2,683)	\$ 733
<b>Other comprehensive loss, net of tax</b>						
Other comprehensive loss, net of tax	(2)	(2)	(2)	—	4	(2)
Total comprehensive income	\$ 731	\$ 731	\$ 1,888	\$ 60	\$ (2,679)	\$ 731

Table of Contents

**Condensed Consolidating Statement of Comprehensive Income Information**  
**Year Ended December 31, 2014**

(in millions)	Parent	Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating and Eliminating Adjustments	Consolidated
<b>Revenues</b>						
Service revenues	\$ —	\$ —	\$ 21,483	\$ 1,302	\$ (410)	\$ 22,375
Equipment revenues	—	—	7,319	—	(530)	6,789
Other revenues	—	—	270	140	(10)	400
Total revenues	—	—	29,072	1,442	(950)	29,564
<b>Operating expenses</b>						
Cost of services, exclusive of depreciation and amortization shown separately below	—	—	5,767	21	—	5,788
Cost of equipment sales	—	—	9,491	702	(572)	9,621
Selling, general and administrative	—	—	8,723	518	(378)	8,863
Depreciation and amortization	—	—	4,330	82	—	4,412
Cost of MetroPCS business combination	—	—	299	—	—	299
Gains on disposal of spectrum licenses	—	—	(840)	—	—	(840)
Other, net	—	—	5	—	—	5
Total operating expenses	—	—	27,775	1,323	(950)	28,148
Operating income	—	—	1,297	119	—	1,416
<b>Other income (expense)</b>						
Interest expense	—	(838)	(55)	(180)	—	(1,073)
Interest expense to affiliates	—	(278)	—	—	—	(278)
Interest income	—	—	359	—	—	359
Other income (expense), net	—	(15)	4	—	—	(11)
Total other income (expense), net	—	(1,131)	308	(180)	—	(1,003)
Income (loss) before income taxes	—	(1,131)	1,605	(61)	—	413
Income tax (expense) benefit	—	—	(189)	23	—	(166)
Earnings (loss) of subsidiaries	247	1,278	(54)	—	(1,471)	—
Net income (loss)	\$ 247	\$ 147	\$ 1,362	\$ (38)	\$ (1,471)	\$ 247
<b>Other comprehensive loss, net of tax</b>						
Other comprehensive loss, net of tax	(2)	(2)	(2)	—	4	(2)
Total comprehensive income (loss)	\$ 245	\$ 145	\$ 1,360	\$ (38)	\$ (1,467)	\$ 245

Table of Contents

**Condensed Consolidating Statement of Cash Flows Information**  
**Year Ended December 31, 2016**

(in millions)	Parent	Issuer	Non-issuer subsidiaries	Non-issuer subsidiaries	Consolidating and Eliminating Adjustments	Consolidated
<b>Operating activities</b>						
Net cash provided by (used in) operating activities	\$ 6	\$ (2,031)	\$ 8,166	\$ 104	\$ (110)	\$ 6,135
<b>Investing activities</b>						
Purchases of property and equipment	—	—	(4,702)	—	—	(4,702)
Purchases of spectrum licenses and other intangible assets, including deposits	—	—	(3,968)	—	—	(3,968)
Sales of short-term investments	—	2,000	998	—	—	2,998
Other, net	—	—	(8)	—	—	(8)
Net cash provided by (used in) investing activities	—	2,000	(7,680)	—	—	(5,680)
<b>Financing activities</b>						
Proceeds from issuance of long-term debt	—	997	—	—	—	997
Repayments of capital lease obligations	—	—	(205)	—	—	(205)
Repayments of short-term debt for purchases of inventory, property and equipment, net	—	—	(150)	—	—	(150)
Repayments of long-term debt	—	—	(20)	—	—	(20)
Proceeds from exercise of stock options	29	—	—	—	—	29
Tax withholdings on share-based awards	—	—	(121)	—	—	(121)
Intercompany dividend paid	—	—	—	(110)	110	—
Dividends on preferred stock	(55)	—	—	—	—	(55)
Other, net	—	—	(12)	—	—	(12)
Net cash (used in) provided by financing activities	(26)	997	(508)	(110)	110	463
Change in cash and cash equivalents	(20)	966	(22)	(6)	—	918
<b>Cash and cash equivalents</b>						
Beginning of period	378	1,767	2,364	73	—	4,582
End of period	\$ 358	\$ 2,733	\$ 2,342	\$ 67	\$ —	\$ 5,500

Table of Contents

**Condensed Consolidating Statement of Cash Flows Information**  
**Year Ended December 31, 2015**

(in millions)	Parent	Issuor	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating and Eliminating Adjustments	Consolidated
<b>Operating activities</b>						
Net cash provided by (used in) operating activities	\$ (1)	\$ (4,504)	\$ 9,940	\$ 154	\$ (175)	\$ 5,414
<b>Investing activities</b>						
Purchases of property and equipment	—	—	(4,724)	—	—	(4,724)
Purchases of spectrum licenses and other intangible assets, including deposits	—	—	(1,935)	—	—	(1,935)
Purchases of short-term investments	—	(1,999)	(998)	—	—	(2,997)
Investment in subsidiaries	(1,905)	—	—	—	1,905	—
Other, net	—	—	96	—	—	96
Net cash used in investing activities	(1,905)	(1,999)	(7,561)	—	1,905	(9,560)
<b>Financing activities</b>						
Proceeds from capital contribution	—	1,905	—	—	(1,905)	—
Proceeds from issuance of long-term debt	—	3,979	—	—	—	3,979
Proceeds from tower obligations	—	140	—	—	—	140
Repayments of capital lease obligations	—	—	(57)	—	—	(57)
Repayments of short-term debt for purchases of inventory, property and equipment, net	—	—	(564)	—	—	(564)
Proceeds from exercise of stock options	47	—	—	—	—	47
Intercompany dividend paid	—	—	—	(175)	175	—
Tax withholdings on share-based awards	—	—	(156)	—	—	(156)
Dividends on preferred stock	(41)	—	(14)	—	—	(55)
Other, net	—	—	79	—	—	79
Net cash provided by (used in) financing activities	6	6,024	(712)	(175)	(1,730)	3,413
Change in cash and cash equivalents	(1,900)	(479)	1,667	(21)	—	(733)
<b>Cash and cash equivalents</b>						
Beginning of period	2,278	2,246	697	94	—	5,315
End of period	\$ 378	\$ 1,767	\$ 2,364	\$ 73	\$ —	\$ 4,582

Table of Contents

**Condensed Consolidating Statement of Cash Flows Information**  
**Year Ended December 31, 2014**

(in millions)	Parent	Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating and Eliminating Adjustments	Consolidated
<b>Operating activities</b>						
Net cash provided by (used in) operating activities	\$ 9	\$ (5,145)	\$ 9,364	\$ 18	\$ (100)	\$ 4,146
<b>Investing activities</b>						
Purchases of property and equipment	—	—	(4,317)	—	—	(4,317)
Purchases of spectrum licenses and other intangible assets, including deposits	—	—	(2,900)	—	—	(2,900)
Investment in subsidiaries	(1,700)	—	—	—	1,700	—
Other, net	—	—	(29)	—	—	(29)
Net cash used in investing activities	(1,700)	—	(7,246)	—	1,700	(7,246)
<b>Financing activities</b>						
Proceeds from capital contribution	—	1,700	—	—	(1,700)	—
Proceeds from issuance of long-term debt	—	2,993	—	—	—	2,993
Repayments of capital lease obligations	—	—	(19)	—	—	(19)
Repayments of short-term debt for purchases of inventory, property and equipment, net	—	—	(418)	—	—	(418)
Repayments of long-term debt	—	—	(1,000)	—	—	(1,000)
Proceeds from exercise of stock options	27	—	—	—	—	27
Proceeds from issuance of preferred stock	982	—	—	—	—	982
Intercompany dividend paid	—	—	—	(100)	100	—
Tax withholdings on share-based awards	—	—	(73)	—	—	(73)
Other, net	—	—	32	—	—	32
Net cash provided by (used in) financing activities	1,009	4,693	(1,478)	(100)	(1,600)	2,524
Change in cash and cash equivalents	(682)	(452)	640	(82)	—	(576)
<b>Cash and cash equivalents</b>						
Beginning of period	2,960	2,698	57	176	—	5,891
End of period	\$ 2,278	\$ 2,246	\$ 697	\$ 94	\$ —	\$ 5,315

Table of Contents**Supplementary Data****Quarterly Financial Information (Unaudited)**

(in millions, except shares and per share amounts)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Full Year
<b>2016</b>					
Total revenues	\$ 8,599	\$ 9,222	\$ 9,246	\$ 10,175	\$ 37,242
Operating income	1,103	768	989	942	3,802
Net income	479	225	366	390	1,460
Dividends on preferred stock	(14)	(14)	(13)	(14)	(55)
Net income attributable to common stockholders	465	211	353	376	1,405
Earnings per share					
Basic	\$ 0.57	\$ 0.26	\$ 0.43	\$ 0.46	\$ 1.71
Diluted	\$ 0.56	\$ 0.25	\$ 0.42	\$ 0.45	\$ 1.69
Weighted average shares outstanding					
Basic	819,431,761	822,434,490	822,998,697	824,982,734	822,470,275
Diluted	859,382,827	829,752,956	832,257,819	867,262,400	833,054,545
Net income includes					
Cost of MetroPCS business combination	\$ 36	\$ 59	\$ 15	\$ (6)	\$ 104
Gains on disposal of spectrum licenses	(636)	—	(199)	—	(835)
<b>2015</b>					
Total revenues	\$ 7,778	\$ 8,179	\$ 7,849	\$ 8,247	\$ 32,053
Operating income	117	597	513	838	2,065
Net income (loss)	(63)	361	138	297	733
Dividends on preferred stock	(14)	(14)	(13)	(14)	(55)
Net income (loss) attributable to common stockholders	(77)	347	125	283	678
Earnings (loss) per share					
Basic	\$ (0.09)	\$ 0.43	\$ 0.15	\$ 0.35	\$ 0.83
Diluted	\$ (0.09)	\$ 0.42	\$ 0.15	\$ 0.34	\$ 0.82
Weighted average shares outstanding					
Basic	808,605,526	811,605,031	815,069,272	816,585,782	812,994,028
Diluted	808,605,526	821,122,537	822,017,220	824,716,119	822,617,938
Net income (loss) includes					
Cost of MetroPCS business combination	\$ 128	\$ 34	\$ 193	\$ 21	\$ 376
Gains on disposal of spectrum licenses	—	(23)	(1)	(139)	(163)

Earnings (loss) per share is computed independently for each quarter and the sum of the quarters may not equal earnings (loss) per share for the full year.

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**Item 9A. Controls and Procedures****Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and procedures designed to ensure information required to be disclosed in our periodic reports filed or submitted under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Our disclosure controls are also designed to ensure that information required to be disclosed in the reports we file or

submit under the Exchange Act is accumulated and communicated to our management, including our Principal Executive Officer and Principal Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and

Table of Contents

procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective, as of the end of the period covered by this report.

The certifications required by Section 302 of the Sarbanes-Oxley Act of 2002 are filed as exhibits 31.1 and 31.2, respectively, to this Form 10-K.

**Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act, during our most recently completed fiscal quarter that materially affected or are reasonably likely to materially affect internal control over financial reporting.

**Management's Annual Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes maintaining records that in reasonable detail accurately and fairly reflect our transactions; providing reasonable assurance that transactions are recorded as necessary for preparation of our financial statements in accordance with generally accepted accounting principles; providing reasonable assurance that receipts and expenditures are made in accordance with management authorization; and providing reasonable assurance that unauthorized acquisition, use or disposition of company assets that could have a material effect on our financial statements would be prevented or detected on a timely basis. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with policies and procedures may deteriorate.

Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework and criteria established in Internal Control – Integrated Framework (2013), issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that our internal control over financial reporting was effective as of December 31, 2016.

The effectiveness of our internal control over financial reporting as of December 31, 2016 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report herein.

**Item 9B. Other Information**

None.

**PART III.****Item 10. Directors, Executive Officers and Corporate Governance**

We maintain a code of ethics applicable to our Chief Executive Officer, Chief Financial Officer, Chief Accounting Officer, Treasurer, and Controller, which is a "Code of Ethics for Senior Financial Officers" as defined by applicable rules of the SEC. This code is publicly available on our website at [investor.t-mobile.com](http://investor.t-mobile.com). If we make any amendments to this code other than technical, administrative or other non-substantive amendments, or grant any waivers, including implicit waivers, from a provision of this code we will disclose the nature of the amendment or waiver, its effective date and to whom it applies on our website at [investor.t-mobile.com](http://investor.t-mobile.com) or in a periodic report on Form 8-K filed with the SEC.

The remaining information required by this item, including information about our Directors, Executive Officers and Audit Committee, is incorporated by reference to the definitive Proxy Statement for our 2017 Annual Meeting of Stockholders, which will be filed with the SEC, no later than 120 days after December 31, 2016.

Table of Contents**Item 11. Executive Compensation**

The information required by this item is incorporated by reference to the definitive Proxy Statement for our 2017 Annual Meeting of Stockholders, which will be filed with the SEC no later than 120 days after December 31, 2016.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The information required by this item is incorporated by reference to the definitive Proxy Statement for our 2017 Annual Meeting of Stockholders, which will be filed with the SEC no later than 120 days after December 31, 2016.

**Item 13. Certain Relationships and Related Transactions, and Director Independence**

The information required by this item is incorporated by reference to the definitive Proxy Statement for our 2017 Annual Meeting of Stockholders, which will be filed with the SEC no later than 120 days after December 31, 2016.

**Item 14. Principal Accounting Fees and Services**

The information required by this item is incorporated by reference to the definitive Proxy Statement for our 2017 Annual Meeting of Stockholders, which will be filed with the SEC no later than 120 days after December 31, 2016.

**PART IV.****Item 15. Exhibits, Financial Statement Schedules**

(a) Documents filed as a part of this Form 10-K:

**1. Financial Statements**

The following financial statements are included in Part II, Item 8 of this Form 10-K:

**Report of Independent Registered Public Accounting Firm**

Consolidated Balance Sheets

Consolidated Statements of Comprehensive Income

Consolidated Statements of Cash Flows

Consolidated Statement of Stockholders' Equity

Notes to the Consolidated Financial Statements

**2. Financial Statement Schedules**

All other schedules have been omitted because they are not required, not applicable, or the required information is otherwise included.

**3. Exhibits**

See the Exhibit Index immediately following the signature page of this Form 10-K.

**Item 16. Form 10-K Summary**

None.

Table of Contents**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

**T-MOBILE US, INC.**

February 14, 2017

/s/ John J. Legere

John J. Legere  
President and Chief Executive Officer

Each person whose signature appears below constitutes and appoints John J. Legere and J. Braxton Carter, and each or either of them, his or her true and lawful attorney-in-fact and agent, each acting alone, with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign any or all amendments or supplements (including post-effective amendments) to this Report, and to file the same, with all exhibits thereto, and all documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorney-in-fact and agent, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent, or his or her substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated as of February 14, 2017.

<u>Signature</u>	<u>Title</u>
<u>/s/ John J. Legere</u> John J. Legere	President and Chief Executive Officer and Director (Principal Executive Officer)
<u>/s/ J. Braxton Carter</u> J. Braxton Carter	Executive Vice President and Chief Financial Officer (Principal Financial Officer)
<u>/s/ Peter Osvaldik</u> Peter Osvaldik	Senior Vice President, Finance and Chief Accounting Officer (Principal Accounting Officer)
<u>/s/ Timotheus Höttges</u> Timotheus Höttges	Chairman of the Board
<u>/s/ W. Michael Barnes</u> W. Michael Barnes	Director
<u>/s/ Thomas Dannenfeldt</u>	Director

Thomas Dannenfeldt

Table of Contents

<u>/s/ Srikant Datar</u> Srikant Datar	Director
<u>/s/ Lawrence H. Guffey</u> Lawrence H. Guffey	Director
<u>/s/ Bruno Jacobfeuerborn</u> Bruno Jacobfeuerborn	Director
<u>/s/ Raphael Kübler</u> Raphael Kübler	Director
<u>/s/ Thorsten Langheim</u> Thorsten Langheim	Director
<u>/s/ Teresa A. Taylor</u> Teresa A. Taylor	Director
<u>/s/ Kelvin R. Westbrook</u> Kevin R. Westbrook	Director

Table of Contents

## INDEX TO EXHIBITS

Exhibit No.	Exhibit Description	Incorporated by Reference			Exhibit Number	Filed Herein
		Form	Date of Filing			
2.1	Business Combination Agreement, dated as of October 3, 2012, by and among MetroPCS Communications, Inc., Deutsche Telekom AG, T-Mobile Zwischenholding GMBH, T-Mobile Global Holding GMBH and T-Mobile USA, Inc.	8-K	10/3/2012		2.1	
2.2	Consent Solicitation Letter Agreement, dated December 5, 2012, by and among MetroPCS Communications, Inc. and Deutsche Telekom AG, amending Exhibit G to the Business Combination Agreement.	8-K	12/7/2012		2.1	
2.3	Amendment No. 1 to the Business Combination Agreement by and among Deutsche Telekom AG, T-Mobile USA, Inc., T-Mobile Global Zwischenholding GmbH, T-Mobile Global Holding GmbH and MetroPCS Communications, Inc., dated April 14, 2013.	8-K	4/15/2013		2.1	
3.1	Fourth Amended and Restated Certificate of Incorporation.	8-K	5/2/2013		3.1	
3.2	Fifth Amended and Restated Bylaws.	8-K	5/2/2013		3.2	
3.3	Certificate of Designation of 5.50% Mandatory Convertible Preferred Stock, Series A, of T-Mobile US, Inc., dated December 12, 2014.	8-K	12/15/2014		3.1	
4.1	Rights Agreement, dated as of March 29, 2007, between MetroPCS Communications, Inc. and American Stock Transfer & Trust Company, as Rights Agent, which includes the form of Certificate of Designation of Series A Junior Participating Preferred Stock of MetroPCS Communications, Inc. as Exhibit A, the form of Rights Certificate as Exhibit B and the Summary of Rights as Exhibit C.	8-K	3/30/2007		4.1	
4.2	Amendment No. 1 to the Rights Agreement, dated as of October 3, 2012 between MetroPCS Communications, Inc. and American Stock Transfer & Trust Company, as Rights Agent.	8-K	10/3/2012		4.1	
4.3	Indenture, dated September 21, 2010, among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Wells Fargo Bank, N.A., a trustee.	8-K	9/21/2010		4.1	
4.4	First Supplemental Indenture, dated September 21, 2010, among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Wells Fargo Bank, N.A., as trustee.	8-K	9/21/2010		4.2	
4.5	Second Supplemental Indenture, dated November 17, 2010, among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Wells Fargo Bank, N.A., as trustee.	8-K	11/17/2010		4.1	
4.6	Third Supplemental Indenture, dated December 23, 2010, among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Wells Fargo Bank, N.A., as trustee.	10-K	3/1/2011		10.19(d)	
4.7	Fourth Supplemental Indenture, dated December 23, 2010, among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Wells Fargo Bank, N.A., as trustee.	10-K	3/1/2011		10.19(e)	
4.8	Fifth Supplemental Indenture, dated as of December 14, 2012, among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Wells Fargo Bank, N.A., as trustee.	8-K	12/17/2012		4.1	
4.9	Sixth Supplemental Indenture, dated as of December 14, 2012, among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Wells Fargo Bank, N.A., as trustee.	8-K	12/17/2012		4.2	
4.10	Seventh Supplemental Indenture, dated as of May 1, 2013, among T-Mobile USA, Inc., the guarantors party thereto, and Wells Fargo Bank, N.A., as trustee.	8-K	5/2/2013		4.15	

4.11	Eighth Supplemental Indenture, dated as of July 15, 2013, among T-Mobile USA, Inc., the guarantors party thereto, and Wells Fargo Bank, N.A., as trustee.	10-Q	8/8/2013	4.19
------	---	------	----------	------

Table of Contents

Exhibit No.	Exhibit Description	Incorporated by Reference			Filed Herein
		Form	Date of First Filing	Exhibit Number	
4.12	Ninth Supplemental Indenture, dated as of August 11, 2014, by and among T-Mobile USA, Inc., the guarantors party thereto and Wells Fargo Bank, N.A., as trustee.	10-Q	10/28/2014	4.2	
4.13	Tenth Supplemental Indenture, dated as of September 28, 2015, by and among T-Mobile USA, Inc., the guarantors party thereto and Wells Fargo Bank, N.A., as trustee.	10-Q	10/27/2015	4.2	
4.14	Eleventh Supplemental Indenture, dated as of August 11, 2014, by and among T-Mobile USA, Inc., the guarantors party thereto and Wells Fargo Bank, N.A., as trustee.	10-Q	10/24/2016	4.1	
4.15	Indenture, dated as of March 19, 2013, by and among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Deutsche Bank Trust Company Americas, as trustee.	8-K	3/22/2013	4.1	
4.16	First Supplemental Indenture, dated as of March 19, 2013, by and among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Deutsche Bank Trust Company Americas, as trustee.	8-K	3/22/2013	4.2	
4.17	Form of 6.250% Senior Notes due 2021.	8-K	3/22/2013	4.3	
4.18	Second Supplemental Indenture, dated as of March 19, 2013, by and among MetroPCS Wireless, Inc., the Guarantors (as defined therein) and Deutsche Bank Trust Company Americas, as trustee.	8-K	3/22/2013	4.4	
4.19	Form of 6.625% Senior Notes due 2023.	8-K	3/22/2013	4.5	
4.20	Third Supplemental Indenture, dated as of April 29, 2013, among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	10-Q	8/8/2013	4.17	
4.21	Fourth Supplemental Indenture, dated as of May 1, 2013, among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.16	
4.22	Fifth Supplemental Indenture, dated as of July 15, 2013, among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	10-Q	8/8/2013	4.20	
4.23	Sixth Supplemental Indenture, dated as of August 11, 2014, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Bank Trust Company Americas, as trustee.	10-Q	10/28/2014	4.1	
4.24	Seventh Supplemental Indenture, dated as of September 28, 2015, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Bank Trust Company Americas, as trustee.	10-Q	10/27/2015	4.1	
4.25	Eighth Supplemental Indenture, dated as of August 30, 2016, by and among T-Mobile USA, Inc., the other guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	10-Q	10/24/2016	4.20	
4.26	Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.10	
4.27	First Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.2	
4.28	Second Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.3	
4.29	Third Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.4	

7/20/2017

Document

4.30	Fourth Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.5
------	---	-----	----------	-----

Table of Contents

Exhibit No.	Exhibit Description	Incorporated by Reference			Filed Herein
		Form	Date of Filing	Exhibit Number	
4.31	Fifth Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.6	
4.32	Sixth Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.7	
4.33	Seventh Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.8	
4.34	Eighth Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.9	
4.35	Ninth Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.10	
4.36	Tenth Supplemental Indenture, dated as of April 28, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.11	
4.37	Eleventh Supplemental Indenture, dated as of May 1, 2013 among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	8-K	5/2/2013	4.12	
4.38	Twelfth Supplemental Indenture, dated as of July 15, 2013, among T-Mobile USA, Inc., the guarantors party thereto, and Deutsche Bank Trust Company Americas, as trustee.	10-Q	8/8/2013	4.18	
4.39	Thirteenth Supplemental Indenture, dated as of August 21, 2013, by and among T-Mobile USA, Inc., the Guarantors (as defined therein) and Deutsche Bank Trust Company Americas, as trustee, including the Form of 5.250% Senior Note due 2018.	8-K	8/22/2013	4.1	
4.40	Fourteenth Supplemental Indenture, dated as of November 21, 2013, by and among T-Mobile USA, Inc., the Guarantors and Deutsche Bank Trust Company Americas, as trustee, including the Form of 6.125% Senior Note due 2022.	8-K	11/22/2013	4.1	
4.41	Fifteenth Supplemental Indenture, dated as of November 21, 2013, by and among T-Mobile USA, Inc., the Guarantors and Deutsche Bank Trust Company Americas, as trustee, including the Form of 6.500% Senior Note due 2024.	8-K	11/22/2013	4.2	
4.42	Sixteenth Supplemental Indenture, dated as of August 11, 2014, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Bank Trust Company Americas, as trustee.	10-Q	10/28/2014	4.3	
4.43	Seventeenth Supplemental Indenture, dated as of September 5, 2014, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Bank Trust Company Americas, as trustee, including the Form of 6.000% Senior Notes due 2023.	8-K	9/5/2014	4.1	
4.44	Eighteenth Supplemental Indenture, dated as of September 5, 2014, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Bank Trust Company Americas, as trustee, including the Form of 6.375% Senior Notes due 2025.	8-K	9/5/2014	4.2	
4.45	Nineteenth Supplemental Indenture, dated as of September 28, 2015, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Bank Trust Company Americas, as trustee.	10-Q	10/27/2015	4.3	
4.46	Twentieth Supplemental Indenture, dated as of November 5, 2015,	8-K	11/5/2015	4.1	

by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Bank Trust Company Americas, as Trustee, including the Form of 6.500% Senior Notes due 2026.

4.47	Twenty-First Supplemental Indenture, dated as of November 5, 2015, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Bank Trust Company Americas, as Trustee, including the Form of 6.000% Senior Notes due 2024.	8-K	4/1/2016	4.1
------	--	-----	----------	-----

Table of Contents

Exhibit No.	Exhibit Description	Incorporated by Reference			Filed Herein
		Form	Date of First Filing	Exhibit Number	
4.48	Twenty-Second Supplemental Indenture, dated as of August 30, 2016, by and among T-Mobile USA, Inc., T-Mobile US, Inc., the other guarantors party thereto and Deutsche Bank Trust Company Americas, as trustee.	10-Q	10/24/2016	4.3	
4.49	Noteholder Agreement dated as of April 28, 2013, by and between Deutsche Telekom AG and T-Mobile USA, Inc.	8-K	5/2/2013	4.13	
10.1	Master Agreement, dated as of September 28, 2012, among T-Mobile USA, Inc., Crown Castle International Corp., and certain T-Mobile and Crown subsidiaries.	10-Q	8/8/2013	10.1	
10.2	Amendment No. 1, to Master Agreement, dated as of November 30, 2012, among Crown Castle International Corp., and certain T-Mobile and Crown subsidiaries.	10-Q	8/8/2013	10.2	
10.3	Master Prepaid Lease, dated as of November 30, 2012, by and among T-Mobile USA Tower LLC, T-Mobile West Tower LLC, T-Mobile USA, Inc. and CCTMO LLC.	10-Q	8/8/2013	10.3	
10.4	MPL Site Master Lease Agreement, dated as of November 30, 2012, by and among Cook Inlet/VS GSM IV PCS Holdings, LLC, T-Mobile Central LLC, T-Mobile South LLC, Powertel/Memphis, Inc., Voicestream Pittsburgh, L.P., T-Mobile West LLC, T-Mobile Northeast LLC, Wireless Alliance, LLC, Suncom Wireless Operating Company, L.L.C., T-Mobile USA, Inc. and CCTMO LLC.	10-Q	8/8/2013	10.4	
10.5	First Amendment to MPL Site Master Lease Agreement, dated as of November 30, 2012, by and among Cook Inlet/VS GSM IV PCS Holdings, LLC, T-Mobile Central LLC, T-Mobile South LLC, Powertel/Memphis, Inc., Voicestream Pittsburgh, L.P., T-Mobile West LLC, T-Mobile Northeast LLC, Wireless Alliance, LLC, Suncom Wireless Operating Company, L.L.C., T-Mobile USA, Inc. and CCTMO LLC.	10-Q	8/8/2013	10.5	
10.6	Sale Site Master Lease Agreement, dated as of November 30, 2012, by and among Cook Inlet/VS GSM IV PCS Holdings, LLC, T-Mobile Central LLC, T-Mobile South LLC, Powertel/Memphis, Inc., Voicestream Pittsburgh, L.P., T-Mobile West LLC, T-Mobile Northeast LLC, Wireless Alliance, LLC, Suncom Wireless Operating Company, L.L.C., T-Mobile USA, Inc., T3 Tower 1 LLC and T3 Tower 2 LLC.	10-Q	8/8/2013	10.6	
10.7	First Amendment to Sale Site Master Lease Agreement, dated as of November 30, 2012, by and among Cook Inlet/VS GSM IV PCS Holdings, LLC, T-Mobile Central LLC, T-Mobile South LLC, Powertel/Memphis, Inc., Voicestream Pittsburgh, L.P., T-Mobile West LLC, T-Mobile Northeast LLC, Wireless Alliance, LLC, Suncom Wireless Operating Company, L.L.C., T-Mobile USA, Inc., T3 Tower 1 LLC and T3 Tower 2 LLC.	10-Q	8/8/2013	10.7	
10.8	Management Agreement, dated as of November 30, 2012, by and among Suncom Wireless Operating Company, L.L.C., Cook Inlet/VS GSM IV PCS Holdings, LLC, T-Mobile Central LLC, T-Mobile South LLC, Powertel/Memphis, Inc., Voicestream Pittsburgh, L.P., T-Mobile West LLC, T-Mobile Northeast LLC, Wireless Alliance, LLC, Suncom Wireless Property Company, L.L.C., T-Mobile USA Tower LLC, T-Mobile West Tower LLC, CCTMO LLC, T3 Tower 1 LLC and T3 Tower 2 LLC.	10-Q	8/8/2013	10.8	
10.9	Stockholder's Agreement dated as of April 30, 2013 by and	8-K	5/2/2013	10.1	

7/20/2017

Document

between MetroPCS Communications, Inc. and Deutsche Telekom AG.

10.10	Waiver of Required Approval Under Section 3.6(a) of the Stockholder's Agreement, dated August 7, 2013, between T-Mobile US, Inc. and Deutsche Telekom AG.	10-Q	8/8/2013	10.10
10.11	License Agreement dated as of April 30, 2013 by and between T-Mobile US, Inc. and Deutsche Telekom AG.	8-K	5/2/2013	10.2

Table of Contents

Exhibit No.	Exhibit Description	Incorporated By Reference			Filed Herein
		Form	Date of First Filing	Exhibit Number	
10.12	Credit Agreement, dated as of May 1, 2013, among T-Mobile USA, Inc., as Borrower, Deutsche Telekom AG, as Lender, the other lenders party thereto from time to time, and JPMorgan Chase Bank, N.A., as Administrative Agent.	8-K	5/2/2013	4.14	
10.13	Amendment No. 1, dated as of November 15, 2013, to the Credit Agreement, dated May 1, 2013, among T-Mobile US, Inc., T-Mobile USA, Inc., each of the Subsidiaries signatory thereto, Deutsche Telekom AG and the other lenders party thereto from time to time, and JPMorgan Chase Bank, N.A., as Administrative Agent.	8-K	11/20/2013	10.1	
10.14	Amendment No. 2, dated as of September 3, 2014, to the Credit Agreement, dated as of May 1, 2013, among T-Mobile USA, Inc., Deutsche Telekom AG and the other lenders party thereto from time to time, and JPMorgan Chase Bank, N.A., as Administrative Agent.	8-K	9/5/2014	10.1	
10.15	Amendment No. 3, dated as of November 2, 2015, to the Credit Agreement, dated as of May 1, 2013, among T-Mobile USA, Inc., Deutsche Telekom AG and the other lenders party thereto from time to time, and JPMorgan Chase Bank N.A., as Administrative Agent.	8-K	11/5/2015	10.2	
10.16	Registration Rights Agreement, dated as of March 19, 2013, by and among MetroPCS Wireless, Inc., the Initial Guarantors (as defined therein), and Deutsche Bank Securities, as representative of the Initial Purchasers (as defined therein).	8-K	3/22/2013	10.1	
10.17	Registration Rights Agreement, dated as of August 21, 2013, by and among T-Mobile USA, Inc., the Guarantors (as defined therein), and Deutsche Bank Securities Inc., as Initial Purchaser (as defined therein).	8-K	8/21/2013	10.1	
10.18	License Exchange Agreement, dated January 5, 2014, among T-Mobile USA, Inc., T-Mobile License LLC, Celco Partnership d/b/a Verizon Wireless, Verizon Wireless (VAW) LLC, Athens Cellular, Inc. and Verizon Wireless of the East LP.	8-K	1/6/2014	10.1	
10.19	License Purchase Agreement, dated January 5, 2014, among T-Mobile USA, Inc., T-Mobile License LLC and Celco Partnership d/b/a Verizon Wireless.	8-K	1/6/2014	10.2	
10.20	Receivables Sale and Conveyancing Agreement, dated as of February 26, 2014, among T-Mobile West LLC, T-Mobile Central LLC, T-Mobile Northeast LLC and T-Mobile South LLC, as sellers, and T-Mobile PCS Holdings LLC, as purchaser.	8-K	3/4/2014	10.1	
10.21	Receivables Sale and Contribution Agreement, dated as of February 26, 2014, between T-Mobile PCS Holdings LLC, as seller, and T-Mobile Airtime Funding LLC, as purchaser.	8-K	3/4/2014	10.2	
10.22	Master Receivables Purchase Agreement, dated as of February 26, 2014, among T-Mobile Airtime Funding LLC, as funding seller, Billing Gate One LLC, as purchaser, Landesbank Hessen-Thüringen Girozentrale, as bank purchasing agent, T-Mobile PCS Holdings LLC, as servicer, and T-Mobile US, Inc., as performance guarantor.	8-K	3/4/2014	10.3	
10.23	Omnibus Amendment to the Master Receivables Purchase Agreement and Fee Letter, dated as of April 11, 2014, by and among T-Mobile Airtime Funding LLC, as funding seller, Billing Gate One LLC, as purchaser, Landesbank Hessen-Thüringen	10-Q	5/1/2014	10.7	

Girozentrale, as bank purchasing agent and a bank purchaser, T-Mobile PCS Holdings LLC, as servicer, T-Mobile US, Inc. as performance guarantor, and the Bank of Tokyo-Mitsubishi UFJ, Ltd., as a bank purchaser.

Table of Contents

Exhibit No.	Exhibit Description	Incorporated by Reference			Filed Herein
		Form	Date of Filing	Exhibit Number	
10.24	Second Amendment to the Master Receivables Purchase Agreement dated as of June 12, 2014, by and among T-Mobile Airtime Funding LLC, as funding seller, Billing Gate One LLC, as purchaser, Landesbank Hessen-Thüringen Girozentrale, as bank purchasing agent and a bank purchaser, T-Mobile PCS Holdings LLC, as servicer and T-Mobile US, Inc. as performance guarantor.	10-Q	7/31/2014	10.2	
10.25	Third Amendment to the Master Receivables Purchase Agreement, dated as of September 29, 2014, by and among T-Mobile Airtime Funding LLC, as funding seller, Billing Gate One LLC, as purchaser, Landesbank Hessen-Thüringen Girozentrale, as bank purchasing agent and a bank purchaser, T-Mobile PCS Holdings LLC, as servicer and T-Mobile US, Inc. as performance guarantor.	10-Q	10/28/2014	10.2	
10.26	Fourth Amendment to the Master Receivables Purchase Agreement, dated as of November 28, 2014, by and among T-Mobile Airtime Funding LLC, as funding seller, Billing Gate One LLC, as purchaser, Landesbank Hessen-Thüringen Girozentrale, as bank purchasing agent and a bank purchaser, T-Mobile PCS Holdings LLC, as servicer and T-Mobile US, Inc. as performance guarantor.	10-K	2/19/2015	10.54	
10.27	Joinder and First Amendment to the Receivables Sale and Conveyancing Agreement, dated as of November 28, 2014, among Powertel/Memphis, Inc., Triton PCS Holdings Company L.L.C., T-Mobile West LLC, T-Mobile Central LLC, T-Mobile Northeast LLC and T-Mobile South LLC, as sellers, and T-Mobile PCS Holdings LLC, as purchaser.	10-K	2/19/2015	10.55	
10.28	First Amendment to the Receivables Sale and Contribution Agreement, dated as of November 28, 2014, between T-Mobile PCS Holdings LLC, as seller, and T-Mobile Airtime Funding LLC, as purchaser.	10-K	2/19/2015	10.56	
10.29	November 2016 Amended and Restated Guarantee Facility Agreement, dated as of December 5, 2016, among T-Mobile US, Inc., as the company, T-Mobile Airtime Funding LLC, as the funding seller, and KfW IPEX-Bank GmbH, as the bank.				X
10.30	Fifth Amendment to the Master Receivables Purchase Agreement, dated as of January 9, 2015, by and among T-Mobile Airtime Funding LLC, as funding seller, Billing Gate One LLC, as purchaser, Landesbank Hessen-Thüringen Girozentrale, as bank purchasing agent and a bank purchaser, T-Mobile PCS Holdings LLC, as servicer and T-Mobile US, Inc. as performance guarantor.	10-Q	4/28/2015	10.4	
10.31	Joinder and Second Amendment to the Receivables Sale and Conveyancing Agreement, dated as of January 9, 2015, among SunCom Wireless Operating Company, LLC, Powertel/Memphis, Inc., Triton PCS Holdings Company L.L.C., T-Mobile West LLC, T-Mobile Central LLC, T-Mobile Northeast LLC and T-Mobile South LLC, as sellers, and T-Mobile PCS Holdings LLC, as purchaser.	10-Q	4/28/2015	10.5	
10.32	Second Amendment to the Receivables Sale and Contribution Agreement, dated as of January 9, 2015, by and among T-Mobile PCS Holdings LLC, as seller, and T-Mobile Airtime Funding LLC, as purchaser.	10-Q	4/28/2015	10.6	
10.33	Third Amendment to the Receivables Sale and Contribution Agreement, dated as of November 30, 2016, by and among T-				X

Mobile PCS Holdings LLC, as seller, and T-Mobile Airtime  
Funding LLC, as purchaser.

Table of Contents

Exhibit No.	Exhibit Description	Incorporated by Reference			Filed Herein
		Form	Date of First Filing	Exhibit Number	
10.34	October 2015 Amendment to the Master Receivables Purchase Agreement, dated as of October 30, 2015, among T-Mobile Airtime Funding LLC, as funding seller, Billing Gate One LLC, as purchaser, Landesbank Hessen-Thüringen Girozentrale, as bank purchasing agent, T-Mobile PCS Holdings LLC, as servicer, and T-Mobile US, Inc., as performance guarantor.	8-K	11/5/2015	10.1	
10.35	First Amended and Restated Master Receivables Purchase Agreement, dated as of June 6, 2016, among T-Mobile Airtime Funding LLC, as funding seller, Billing Gate One LLC, as purchaser, Landesbank Hessen-Thüringen Girozentrale, as bank purchasing agent, the Bank of Tokyo-Mitsubishi UFJ, Ltd., Düsseldorf Branch, as bank collections agent, T-Mobile PCS Holdings LLC, as servicer, and T-Mobile US, Inc., as performance guarantor.	10-Q	7/27/2016	10.5	
10.36	Second Amended and Restated Master Receivables Purchase Agreement, dated as of November 30, 2016, among T-Mobile Airtime Funding LLC, as funding seller, Billing Gate One LLC, as purchaser, Landesbank Hessen-Thüringen Girozentrale, as bank purchasing agent, The Bank of Tokyo Mitsubishi UFJ, Ltd., as bank collection agent, T-Mobile PCS Holdings LLC, as servicer, and T-Mobile US, Inc., as performance guarantor.	8-K	12/6/2016	10.1	
10.37	Term Loan Credit Agreement, dated as of November 9, 2015, among T-Mobile USA, Inc., the lenders party thereto and Deutsche Bank AG New York Branch, as administrative agent and collateral agent.	8-K	11/12/2015	10.1	
10.38	Receivables Sale Agreement, dated as of November 18, 2015, by and between T-Mobile Financial LLC, as seller, and T-Mobile Handset Funding LLC, as purchaser.	8-K	11/20/2015	10.1	
10.39	First Amendment to the Receivables Sale Agreement, dated as of March 18, 2016, by and between T-Mobile Financial LLC, as seller, and T-Mobile Handset Funding LLC, as purchaser.	10-Q	4/26/2016	10.3	
10.40	Amended and Restated Receivables Sale Agreement, dated as of June 6, 2016, by and between T-Mobile Financial LLC, as seller, and T-Mobile Handset Funding LLC, as purchaser.	8-K	6/8/2016	10.1	
10.41	First Amendment, dated as of December 23, 2016, to the Amended and Restated Receivables Sale Agreement, dated as of June 6, 2016, by and between T-Mobile Financial LLC, as seller, and T-Mobile Handset Funding LLC, as purchaser.				X
10.42	Receivables Purchase and Administration Agreement, dated as of November 18, 2015, by and among T-Mobile Handset Funding LLC, as transferor, T-Mobile Financial LLC, as servicer, T-Mobile US, Inc. as performance guarantor, Royal Bank of Canada, as administrative agent, and certain financial institutions party thereto from time to time.	8-K	11/20/2015	10.2	
10.43	Omnibus First Amendment to the Receivables Purchase and Administration Agreement and Administrative Agent Fee Letter, dated as of March 18, 2016, by and among T-Mobile Handset Funding LLC, as transferor, T-Mobile Financial LLC, individually and as servicer, T-Mobile US, Inc., as guarantor, Royal Bank of Canada, as administrative agent, and certain financial institutions from time to time party thereto.	10-Q	4/26/2016	10.2	
10.44	Amended and Restated Receivables Purchase and Administration	8-K	6/8/2016	10.2	

Agreement, dated as of June 6, 2016, by and among T-Mobile Handset Funding LLC, as transferor, T-Mobile Financial LLC, as servicer, T-Mobile US, Inc., as performance guarantor, Royal Bank of Canada, as administrative agent, and certain financial institutions party thereto from time to time.

Table of Contents

Exhibit No.	Exhibit Description	Incorporated by Reference			Filed Herein
		Form	Date of Filing	Exhibit Number	
10.45	First Amendment, dated as of July 27, 2016, to the Amended and Restated Receivables Purchase and Administration Agreement, dated as of June 6, 2016, by and among T-Mobile Handset Funding LLC, as transferor, T-Mobile Financial LLC, as servicer, T-Mobile US, Inc., as performance guarantor, Royal Bank of Canada, as administrative agent, and certain financial institutions party thereto.	10-Q	10/24/2016	10.1	
10.46	Second Amendment, dated as of October 31, 2016, to the Amended and Restated Receivables Purchase and Administration Agreement, dated as of June 6, 2016, by and among T-Mobile Handset Funding LLC, as transferor, T-Mobile Financial LLC, as servicer, T-Mobile US, Inc., as performance guarantor, Royal Bank of Canada, as administrative agent, and certain financial institutions party thereto.				X
10.47	Third Amendment, dated as of December 23, 2016, to the Amended and Restated Receivables Purchase and Administration Agreement, dated as of June 6, 2016, by and among T-Mobile Handset Funding LLC, as transferor, T-Mobile Financial LLC, as servicer, T-Mobile US, Inc., as performance guarantor, Royal Bank of Canada, as administrative agent, and certain financial institutions party thereto.				X
10.48	Purchase Agreement, dated as of March 6, 2016, among T-Mobile USA, Inc., the guarantor party thereto and Deutsche Telekom AG.	8-K	3/7/2016	1.1	
10.49	Amendment No. 1 to Purchase Agreement, dated as of October 28, 2016, to Purchase Agreement, dated as of March 6, 2016, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Telekom AG.	8-K	11/2/2016	10.1	
10.50	Purchase Agreement, dated as of April 25, 2016, among T-Mobile USA, Inc., the guarantor party thereto and Deutsche Telekom AG.	8-K	4/26/2016	1.1	
10.51	Amendment No. 1 to Purchase Agreement, dated as of October 28, 2016, to Purchase Agreement, dated as of April 25, 2016, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Telekom AG.	8-K	11/2/2016	10.2	
10.52	Purchase Agreement, dated as of April 29, 2016, among T-Mobile USA, Inc., the guarantor party thereto and Deutsche Telekom AG.	8-K	4/29/2016	1.1	
10.53	Amendment No. 1 to Purchase Agreement, dated as of October 28, 2016, to Purchase Agreement, dated as of April 29, 2016, by and among T-Mobile USA, Inc., the guarantors party thereto and Deutsche Telekom AG.	8-K	11/2/2016	10.3	
10.54	Unsecured Revolving Credit Agreement, dated as of December 29, 2016, by and among T-Mobile US, Inc., T-Mobile USA, Inc., the several banks and other financial institutions or entities from time to time party thereto as lenders, and Deutsche Telekom AG, as administrative agent.	8-K	12/30/2016	10.1	
10.55	Secured Revolving Credit Agreement, dated as of December 29, 2016, by and among T-Mobile US, Inc., T-Mobile USA, Inc., the several banks and other financial institutions or entities from time to time party thereto as lenders, and Deutsche Telekom AG, as administrative agent.	8-K	12/30/2016	10.2	
10.56	First Incremental Facility Amendment, dated as of December 29, 2016, to the Term Loan Credit Agreement, dated as of November 9, 2015, by and among T-Mobile USA, Inc., the several banks and other financial institutions or entities from time to time parties	8-K	12/30/2016	10.3	

thereto as lenders, and Deutsche Bank AG New York Branch, as administrative agent.

Table of Contents

Exhibit No.	Exhibit Description	Incorporated by Reference			Filed Herein
		Form	Date of Filing	Exhibit Number	
10.57	Second Incremental Facility Amendment, dated as of January 25, 2017, to the Term Loan Credit Agreement, dated as of November 9, 2015, as amended by that certain First Incremental Facility Amendment dated as of December 29, 2016, by and among T-Mobile USA, Inc., the several banks and other financial institutions or entities from time to time parties thereto as lenders, and Deutsche Bank AG New York Branch, as administrative agent.	8-K	1/25/2017	10.1	
10.58*	Amended and Restated MetroPCS Communications, Inc. 2004 Equity Incentive Compensation Plan.	S-1/A	2/27/2007	10.1(a)	
10.59*	MetroPCS Communications, Inc. 2010 Equity Incentive Compensation Plan.	Schedule 14A	4/19/2010	Annex A	
10.60*	Form Change in Control Agreement for MetroPCS Communications, Inc.	10-Q	8/9/2010	10.2	
10.61*	Form Change in Control Agreement Amendment for MetroPCS Communications, Inc.	10-Q	10/30/2012	10.1	
10.62*	MetroPCS Communications, Inc. Employee Non-qualified Stock Option Award Agreement relating to the MetroPCS Communications, Inc. Amended and Restated 2004 Equity Incentive Compensation Plan.	10-K	3/1/2013	10.9(a)	
10.63*	MetroPCS Communications, Inc. Non-Employee Director Non-qualified Stock Option Award Agreement relating to the MetroPCS Communications, Inc. Amended and Restated 2004 Equity Incentive Compensation Plan.	10-K	3/1/2013	10.9(b)	
10.64*	Form Amendment to the MetroPCS Communications, Inc. Notice of Grant of Stock Option relating to the Second Amended and Restated 1995 Stock Option Plan of MetroPCS, Inc.	10-Q	8/9/2010	10.5	
10.65*	Form MetroPCS Communications, Inc. 2010 Equity Incentive Compensation Plan Employee Non-Qualified Stock Option Award Agreement.	10-K	2/29/2012	10.12	
10.66*	Form MetroPCS Communications, Inc. 2010 Equity Incentive Compensation Plan Non-Employee Director Non-Qualified Stock Option Award Agreement.	10-K	3/1/2013	10.12(b)	
10.67*	Employment Agreement of J. Braxton Carter dated as of January 25, 2013.	8-K	5/2/2013	10.3	
10.68*	Employment Agreement of Thomas C. Keys dated as of January 25, 2013.	8-K	5/2/2013	10.4	
10.69*	Employment Agreement of John J. Legere dated as of September 22, 2012.	10-Q	8/8/2013	10.17	
10.70*	Amendment to Employment Agreement of John J. Legere dated as of October 23, 2013.	10-K	2/25/2014	10.35	
10.71*	Amendment No. 2 to Employment Agreement between T-Mobile US, Inc. and John J. Legere, dated as of February 25, 2015.	8-K	2/26/2015	10.1	
10.72*	T-Mobile US, Inc. Compensation Term Sheet for Michael Sievert Effective as of February 13, 2015.	10-Q	4/28/2015	10.3	
10.73*	Form of Indemnification Agreement.	8-K	5/2/2013	10.6	
10.74*	T-Mobile US, Inc. Non-Qualified Deferred Executive Compensation Plan (As Amended and Restated Effective as of January 1, 2014).	10-K	2/25/2014	10.39	
10.75*	T-Mobile US, Inc. Executive Continuity Plan as Amended and Restated Effective as of January 1, 2014.	8-K	10/25/2013	10.1	

7/20/2017

Document

10.76*	T-Mobile US, Inc. 2013 Omnibus Incentive Plan (as amended and restated on August 7, 2013).	10-Q	8/8/2013	10.20
10.77*	T-Mobile USA, Inc. 2011 Long-Term Incentive Plan.	10-Q	8/8/2013	10.21

Table of Contents

Exhibit No.	Exhibit Description	Incorporated by Reference			Filed Herein
		Form	Date of First Filing	Exhibit Number	
10.78*	Annual Incentive Award Notice under the 2013 Omnibus Incentive Plan.	10-K	2/25/2014	10.45	
10.79*	Form of Restricted Stock Unit Award Agreement for Non-Employee Directors under the T-Mobile US, Inc. 2013 Omnibus Incentive Plan.	8-K	6/4/2013	10.2	
10.80*	Form of Restricted Stock Unit Award Agreement (Time-Vesting) for Executive Officers under the T-Mobile US, Inc. 2013 Omnibus Incentive Plan.	10-Q	8/8/2013	10.24	
10.81*	Form of Restricted Stock Unit Award Agreement (Performance-Vesting) for Executive Officers under the T-Mobile US, Inc. 2013 Omnibus Incentive Plan.	10-Q	8/8/2013	10.25	
10.82*	Form of Restricted Stock Unit Award Agreement (Performance-Vesting) with Deferral Option for Executive Officers under the T-Mobile US, Inc. 2013 Omnibus Incentive Plan.	10-K	2/19/2015	10.43	
10.83*	Form of Restricted Stock Unit Award Agreement (Time-Vesting) with Deferral Option for Executive Officers under the T-Mobile US, Inc. 2013 Omnibus Incentive Plan.	10-K	2/19/2015	10.44	
10.84*	T-Mobile US, Inc. 2014 Employee Stock Purchase Plan.	S-8	2/19/2015	99.1	
10.85*	Amended Director Compensation Program effective as of May 1, 2013 (amended June 4, 2014 and further amended on June 1, 2015 and June 16, 2016).	10-Q	7/27/2016	10.6	
12.1	Computation of Ratio of Earnings to Fixed Charges.				X
21.1	Subsidiaries of Registrant.				X
23.1	Consent of PricewaterhouseCoopers LLP.				X
24.1	Power of Attorney, pursuant to which amendments to this Form 10-K may be filed (included on the signature page contained in Part IV of the Form 10-K).				X
31.1	Certifications of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				X
31.2	Certifications of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				X
32.1**	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				
32.2**	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				
101.INS	XBRL Instance Document.				X
101.SCH	XBRL Taxonomy Extension Schema Document.				X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.				X
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.				X
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.				X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.				X
*	Indicates a management contract or compensatory plan or arrangement.				
**	Furnished herein.				



10-K I USMform10k.htm 10-K

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

(Mark One)

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2016  
OR  
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 001-09712



**UNITED STATES CELLULAR CORPORATION**

(Exact name of Registrant as specified in its charter)

Delaware

62-1147325

(State or other jurisdiction of incorporation or organization)

(IRS Employer Identification No.)

8410 West Bryn Mawr, Chicago, Illinois 60631

(Address of principal executive offices) (Zip code)

Registrant's Telephone Number: (773) 399-8900

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Shares, \$1 par value	New York Stock Exchange
6.95% Senior Notes Due 2060	New York Stock Exchange
7.25% Senior Notes Due 2063	New York Stock Exchange
7.25% Senior Notes Due 2064	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes  No Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. 

Indicate by check mark 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.

7/20/2017

<https://www.sec.gov/Archives/edgar/data/821130/000082113017000010/USMform10k.htm>

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of June 30, 2016, the aggregate market value of the registrant's Common Shares held by non-affiliates was approximately \$545 million, based upon the closing price of the Common Shares on June 30, 2016 of \$39.27, as reported by the New York Stock Exchange. For purposes hereof, it was assumed that each director, executive officer and holder of 10% or more of any class of voting equity security of U.S. Cellular is an affiliate.

The number of shares outstanding of each of the registrant's classes of common stock, as of January 31, 2017, is 51,843,000 Common Shares, \$1 par value, and 33,006,000 Series A Common Shares, \$1 par value.

#### **DOCUMENTS INCORPORATED BY REFERENCE**

Those sections or portions of the registrant's 2016 Annual Report to Shareholders ("Annual Report"), filed as Exhibit 13 hereto, and of the registrant's Notice of Annual Meeting of Shareholders and Proxy Statement ("Proxy Statement") to be filed prior to April 30, 2017 for the 2017 Annual Meeting of Shareholders scheduled to be held May 23, 2017, are herein incorporated by reference into Parts II and III of this report.

---

---

**United States Cellular Corporation**  
**Annual Report on Form 10-K**  
**For the Period Ended December 31, 2016**

**TABLE OF CONTENTS**

<u>Part I</u>	<u>Page No.</u>
<u>Item 1.</u> <u>Business</u>	<u>1</u>
<u>Item 1A.</u> <u>Risk Factors</u>	<u>8</u>
<u>Item 1B.</u> <u>Unresolved Staff Comments</u>	<u>21</u>
<u>Item 2.</u> <u>Properties</u>	<u>21</u>
<u>Item 3.</u> <u>Legal Proceedings</u>	<u>21</u>
<u>Item 4.</u> <u>Mine Safety Disclosures</u>	<u>21</u>
 <u>Part II</u>	
<u>Item 5.</u> <u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>22</u>
<u>Item 6.</u> <u>Selected Financial Data</u>	<u>23</u>
<u>Item 7.</u> <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>23</u>
<u>Item 7A.</u> <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>23</u>
<u>Item 8.</u> <u>Financial Statements and Supplementary Data</u>	<u>23</u>
<u>Item 9.</u> <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>23</u>
<u>Item 9A.</u> <u>Controls and Procedures</u>	<u>24</u>
<u>Item 9B.</u> <u>Other Information</u>	<u>24</u>
 <u>Part III</u>	
<u>Item 10.</u> <u>Directors, Executive Officers and Corporate Governance</u>	<u>25</u>
<u>Item 11.</u> <u>Executive Compensation</u>	<u>25</u>
<u>Item 12.</u> <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>25</u>
<u>Item 13.</u> <u>Certain Relationships and Related Transactions, and Director Independence</u>	<u>25</u>
<u>Item 14.</u> <u>Principal Accountant Fees and Services</u>	<u>25</u>
 <u>Part IV</u>	
<u>Item 15.</u> <u>Exhibits and Financial Statement Schedules</u>	<u>26</u>
<u>Item 16.</u> <u>Form 10-K Summary</u>	<u>26</u>

Table of Contents**PART I****Item 1. Business****General**

United States Cellular Corporation ("U.S. Cellular") provides wireless telecommunications services to customers with approximately 5.0 million connections in 23 states collectively representing a total population of 32 million. U.S. Cellular operates in one reportable segment, and all of its wireless operating markets are in the United States.

- U.S. Cellular's strategy is to attract and retain wireless customers through a value proposition comprised of a high-quality network, outstanding customer service, and competitive devices, plans, and pricing, all provided with a local focus.
- U.S. Cellular Common Shares trade on the New York Stock Exchange ("NYSE") under the ticker symbol "USM."
- U.S. Cellular is a majority-owned subsidiary of Telephone and Data Systems, Inc. (NYSE: TDS). As of December 31, 2016, TDS owns 83% of U.S. Cellular common stock, has the voting power to elect all of the directors of U.S. Cellular and controls over 96% of the voting power in matters other than the election of directors of U.S. Cellular.
- U.S. Cellular was incorporated under the laws of the state of Delaware in 1983.

The map below highlights areas of operation of U.S. Cellular's consolidated operating markets.

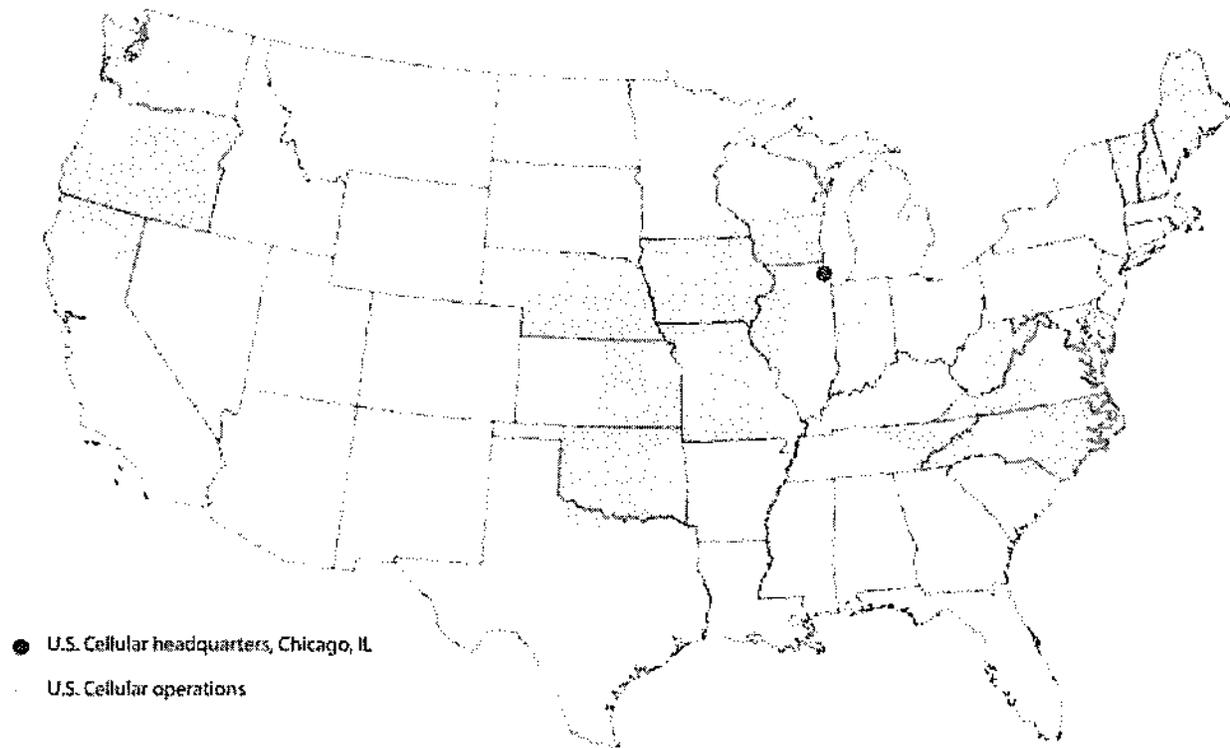


Table of Contents**Customers, Services and Products**

*Customers.* U.S. Cellular provides service to postpaid and prepaid customers from a variety of demographic segments. U.S. Cellular focuses on retail consumers, governments, and small-to-mid-size business customers in industries such as construction, retail, agriculture, professional services and real estate. These customers are served primarily through U.S. Cellular's retail and direct sales channels. U.S. Cellular builds customer loyalty by offering high-quality network services, outstanding customer-focused support services, competitive pricing, and other benefits as discussed further in "Marketing, Customer Service, and Sales and Distribution Channels."

*Services.* U.S. Cellular's postpaid customers are able to choose from a variety of national plans with voice, messaging and data usage options and pricing that are designed to fit different customer needs, usage patterns and budgets. Helping a customer find the right pricing plan is an important element of U.S. Cellular's brand positioning. U.S. Cellular offers Shared Connect data plans which allow customers to share data usage among all users and devices connected to the plan. Business rate plans are designed to meet the unique needs of the business customer. U.S. Cellular's national plans price all domestic calls as local calls, regardless of where they are made or received in the United States, with no long distance or roaming charges, made possible by roaming agreements with other wireless carriers. See "System Usage" section below for further discussion related to roaming. U.S. Cellular also offers monthly prepaid service plans, which provide customers unlimited voice and unlimited messaging with a specified amount of high-speed data and unlimited data at lower speeds once the high-speed data limit is reached to ensure customers are never without data access.

U.S. Cellular's portfolio of smartphones, tablets and other connected devices is a key part of its strategy to deliver wireless devices which allow customers to stay productive, entertained and connected on the go; these devices are backed by U.S. Cellular's high-speed networks, including a fourth generation ("4G") Long-Term Evolution ("LTE") network, which covers 99% of its postpaid connections and supports nationwide roaming. U.S. Cellular's 4G LTE network features smartphone messaging, data and internet services that allow customers to access the web and social network sites, e-mail, text, picture and video message, utilize turn-by-turn GPS navigation, and browse and download thousands of applications to customize their wireless devices to fit their lifestyles.

U.S. Cellular also offers advanced wireless solutions to consumers and business and government customers, including a growing suite of connected machine to machine solutions and software applications across the categories of monitor and control (e.g., sensors and cameras), business automation/operations (e.g., e-forms), communication (e.g., enterprise messaging, back-up router for business continuity services) and asset management (e.g., telematics, fleet management). U.S. Cellular intends to continue to further enhance these offerings for consumer and business customers in 2017 and beyond.

*Devices and Products.* U.S. Cellular offers a comprehensive range of wireless devices such as handsets, tablets, mobile hotspots, home phones and routers for use by its customers. U.S. Cellular offers wireless devices that are compatible with its 4G LTE and third generation ("3G") networks and are compliant with the Federal Communications Commission ("FCC") enhanced wireless 911 requirements. In addition, U.S. Cellular also offers a wide range of accessories, including wireless basics such as cases, screen protectors, chargers, and memory cards as well as an ever growing assortment of consumer electronics such as headphones, speakers, and hands-free devices. In addition, U.S. Cellular recently introduced an assortment of home automation products (e.g., cameras, sensors, thermostats).

During 2016, U.S. Cellular offered customers the option to purchase devices under two alternatives: (1) through equipment installment contracts over a specified time period, where no annual service contract is signed and a discount is provided on their connection charge or (2) alternative plans that are subject to a service contract. Starting in September 2016, however, new postpaid handset sales to retail consumers are made under equipment installment plans only; business and government customers may continue to purchase equipment under either alternative. For certain installment plans, after a specified period of time, the customer may have the right to upgrade to a new device prior to reaching the end of the installment term, thus enabling customers to access the latest smartphones and provide a better overall customer experience.

U.S. Cellular continues to offer device service programs that provide customers a simple process to replace a damaged or defective device through a retail store or via direct mail. U.S. Cellular also offers its Device Protection+ program which includes overnight delivery of a replacement device for lost and stolen devices. In 2016, U.S. Cellular launched Device Protection+ Advanced, which includes 100GB of data backup, TechSupport+, and AppleCare services for Apple iOS customers.

U.S. Cellular offers a full array of both iconic and value smartphones with options for both Android and iOS customers. U.S. Cellular continues to bolster its expanding smartphone portfolio with the Samsung Galaxy S@ 7 and S@ 7 Edge, the iPhone@ 7 and 7 Plus, the LG V20 and K8, and the Motorola G4 Play. Along with the iconic devices, U.S. Cellular supports the larger ecosystem of Samsung and Apple devices, such as the Samsung Gear VR, the Samsung Gear S2 and the Apple Watch. For tablets, U.S. Cellular offers the full complement of iPads, the Samsung Galaxy Tab S2, the LG G Pad F™ 8.0 LTE, and the ZTE ZPad™. U.S. Cellular's smartphone offerings play a significant role in attracting customers and driving data service usage and revenues. U.S. Cellular also offers additional products and services that utilize the company's network, including feature phones, mobile hotspots, LTE wireless routers and home phones.



Table of Contents

U.S. Cellular purchases wireless devices and accessory products from a number of original equipment manufacturers, including Samsung, Apple, Motorola, LG, Kyocera, ZTE, and Tescos. U.S. Cellular also has relationships with its suppliers to ensure best possible pricing and identifies opportunities for promotional support. Additionally, in 2016 U.S. Cellular completed multiple auctions to optimize pricing from accessories suppliers and was able to realize lower costs as a result. U.S. Cellular does not own significant product warehousing and distribution infrastructure; rather, it contracts with third party providers for the majority of its product warehousing, distribution and direct customer fulfillment activities. U.S. Cellular also contracts with third party providers for services related to its device service programs.

U.S. Cellular continuously monitors the financial condition of its wireless device and accessory suppliers. Since U.S. Cellular has a diversified portfolio of products from more than one supplier, U.S. Cellular does not expect the financial condition of any single supplier to affect its ability to offer a competitive portfolio of wireless devices and accessories for sale to customers.

**Marketing, Customer Service, and Sales and Distribution Channels**

*Marketing and Advertising.* U.S. Cellular's marketing plan is focused on acquiring, retaining and growing customer relationships by maintaining a high-quality wireless network, providing outstanding customer service, and offering a comprehensive portfolio of products and services built around customer needs at fair prices with a local focus.

U.S. Cellular believes that creating positive relationships with its customers enhances their wireless experience and builds customer loyalty. U.S. Cellular currently offers several customer-centric programs and services to customers. The Overage Protection service provides customers peace of mind by sending them text message alerts when they come close to reaching their allowable monthly plan minutes, text messages or data usage in order to avoid overage charges. U.S. Cellular also offers a service to customers on Shared Connect data plans to allow them to limit data usage on specific lines – or for the entire account – thereby providing controls to manage account overages. This service, Data Usage Controls, allows customers an easy way to divide their data bucket by line.

U.S. Cellular's advertising is directed at increasing the public awareness of the U.S. Cellular brand and understanding of the wireless services it offers, to attract potential customers, retain existing customers and increase their usage of U.S. Cellular's services. U.S. Cellular supplements its advertising with a focused public relations program that drives store traffic, supports sales of products and services, and builds brand awareness and preference. The approach combines national and local media relations in mainstream and social media channels with market-wide activities, events, and sponsorships.

U.S. Cellular focuses its charitable giving strategy on supporting initiatives relevant to consumers in its service areas. These initiatives include support of programs that focus on youth in the communities U.S. Cellular serves, such as the Boys and Girls Clubs and 4H Societies of America.

*Customer Service.* U.S. Cellular manages customer retention by focusing on outstanding customer service through the development of processes that are customer-friendly, extensive training of frontline sales and support associates and the implementation of retention programs.

U.S. Cellular currently operates four regional customer care centers in its operating markets with personnel who are responsible for customer service activities, and a national financial services center with personnel who perform credit and other customer payment activities. U.S. Cellular also contracts with third parties that provide additional customer care and financial services support.

*Sales and Distribution Channels.* U.S. Cellular supports a multi-faceted distribution program, including retail sales, direct sales, third-party national retailers, and independent agents, plus a website and telesales.

Company retail store locations are designed to market wireless products and services to the consumer and small business segments in a setting familiar to these types of customers. As of December 31, 2016, retail sales associates work in 267 U.S. Cellular-operated retail stores and kiosks. Direct sales consultants market wireless services to mid-size business and government customers. Additionally, the U.S. Cellular website enables customers to activate service and purchase wireless devices online.

U.S. Cellular maintains an ongoing training program to improve the effectiveness of retail sales associates and direct sales consultants by focusing their efforts on obtaining customers by facilitating the sale of appropriate packages for the customer's expected usage and value-added services that meet the individual needs of the customer.

U.S. Cellular has relationships with exclusive and non-exclusive agents (collectively "agents"). Those agents are independent businesses that obtain customers for U.S. Cellular on a commission basis. At December 31, 2016, U.S. Cellular had contracts with these businesses aggregating 523 locations. U.S. Cellular provides additional support and training to its agents to increase customer satisfaction and to ensure a consistent customer experience. U.S. Cellular's agents are generally in the business of selling wireless devices, wireless service packages and other related products. No single agent accounted for 10% or more of U.S. Cellular's operating revenues during the past three years.

U.S. Cellular products and services are also offered through third-party national and on-line retailers. Wal-Mart, Sam's Club, and Dollar General offer U.S. Cellular products and services at select retail locations in U.S. Cellular's service areas. Further, Amazon offers U.S. Cellular's postpaid and prepaid services on-line. U.S. Cellular continues to explore new relationships with additional third-party retailers as part of its strategy to expand distribution.

*Seasonality.* Seasonality in operating expenses may cause operating income to vary from quarter to quarter. U.S. Cellular's operating expenses tend to be higher in the fourth quarter due to increased marketing and promotional activities during the holiday season.

## Table of Contents

### Competition

The wireless telecommunication industry is highly competitive. U.S. Cellular competes directly with several wireless service providers in each of its markets. In general, there are between two and four competitors in each wireless market in which U.S. Cellular provides service, excluding resellers and mobile virtual network operators. In its footprint, U.S. Cellular competes to varying degrees against each of the national wireless companies: Verizon Wireless, AT&T Mobility, Sprint, and T-Mobile USA, in addition to a few smaller regional carriers in specific areas of its footprint. All of the national competitors have substantially greater financial and other resources than U.S. Cellular. Additionally, U.S. Cellular competes with other companies that use alternative communication technology and services to provide similar products and services.

Since each of these wireless competitors operates on systems using spectrum licensed by the FCC and has comparable technology and facilities, competition among wireless service providers for customers is principally on the basis of types of products and services, price, size of area covered, network quality, network speed and responsiveness of customer service. U.S. Cellular employs a customer satisfaction strategy that includes maintaining an outstanding wireless network throughout its markets. U.S. Cellular owns and operates low-band spectrum (less than 1 GHz) that covers the majority of its footprint and enables more efficient coverage in rural areas (compared to spectrum above 1 GHz), which strengthens its network quality positioning. As discussed below, the FCC is currently completing the auction process for a new tranche of low-band spectrum, the 600 MHz band. To the extent existing competitors or new entrants acquire such spectrum in U.S. Cellular markets, U.S. Cellular could face increased competition over time from competitors that hold such more-efficient low-band spectrum.

The use of national advertising and promotional programs by the top four wireless service providers is a source of additional competitive and pricing pressures in all U.S. Cellular markets, even if those operators do not provide direct service in a particular market. Over the past year, competition among top carriers has continued to be aggressive, with the top four carriers engaging in rich promotional initiatives including contract buyouts and limited-time and permanent price reductions. In addition, in the current wireless environment, U.S. Cellular's ability to compete depends on its ability to continue to offer national voice and data plans. U.S. Cellular provides wireless services comparable to the national competitors, but the national wireless companies operate in a wider geographic area and are able to provide such services over a wider area on their own networks than U.S. Cellular can offer on its network. Although U.S. Cellular offers similar coverage area as these competitors, U.S. Cellular incurs roaming charges for data sessions and calls made in portions of the coverage area which are not part of its network, thereby increasing its cost of operations. U.S. Cellular depends on roaming agreements with other wireless carriers to provide voice and data roaming capabilities in areas not covered by U.S. Cellular's network. Similarly, U.S. Cellular provides roaming services on its network to other wireless carriers' customers who travel within U.S. Cellular's coverage areas and receives revenue from other carriers for the provision of these services.

Convergence of connectivity is taking place on many levels, including wireless devices that can act as wireless or wireline replacement devices and the incorporation of wireless "hot spot" technology in wireless devices making internet access seamless regardless of location. Although less directly a substitute for other wireless services, wireless data services such as Wi-Fi may be adequate for those who do not need mobile wide-area roaming or full two-way voice services. Technological advances or regulatory changes in the future, such as the rollout and consumer adoption of Wi-Fi calling and Voice over Long-Term Evolution ("VoLTE") capabilities, may make available other alternatives to current wireless service, thereby creating additional sources of competition that shift consumers' perceptions and preferences of network strength, speed and reliability. If the trend toward convergence continues, U.S. Cellular is at a competitive disadvantage to larger competitors, including the national wireless carriers, traditional cable companies, mobile virtual network operators ("MVNO") and other potential large new entrants with much greater financial and other resources in adapting to such convergence.

U.S. Cellular's approach in 2017 and in future years will be to focus on the unique needs and attitudes of its customers towards wireless service. U.S. Cellular will deliver high-quality products and services at competitive prices and intends to continue to differentiate itself by seeking to provide an overall outstanding customer experience, founded on a high-quality network. U.S. Cellular's ability to compete successfully in the future will depend upon its ability to anticipate and respond to changes related to new service offerings, consumer preferences, competitors' pricing strategies and new product offerings, technology, demographic trends, economic conditions and its access to adequate spectrum resources.

### System Usage

U.S. Cellular's main sources of revenues are from its own customers and from customers of other wireless operators who roam on its network. An inter-carrier roaming agreement is negotiated between the wireless operators to enable customers who are in a wireless service area other than the customer's home service area to place or receive a call, SMS or use data in that service area. U.S. Cellular has entered into reciprocal roaming agreements with operators of other wireless systems covering virtually all systems with Code Division Multiple Access ("CDMA") technology in the United States, Canada and Mexico. In addition, U.S. Cellular has entered into 4G LTE roaming agreements with national wireless companies and, as a result, a majority of U.S. Cellular customers currently have access to nationwide 4G LTE service.

When roaming on another wireless carrier's network, customers will automatically pre-register on the serving carrier's network allowing customers to make or receive calls, SMS or use data. The charge for this service is negotiated as part of the roaming agreement between U.S. Cellular and the roaming customer's carrier. U.S. Cellular bills this charge to the customer's home carrier, which then may bill the customer. In many instances, based on competitive factors, carriers, including U.S. Cellular, may or may not charge their customers for roaming. Since 2010, U.S. Cellular has offered nationwide 3G data roaming services, allowing its customers to access high-speed data across the country.



[Table of Contents](#)**Access Technology and System Design**

*Technology.* Wireless telecommunication systems transmit voice, data, graphics and video through the transmission of signals over networks of radio towers using radio spectrum licensed by the FCC. Access to local, regional, national and worldwide telecommunications networks is provided through system interconnections. A high-quality network, supported by continued investments in that network, will remain an important factor for U.S. Cellular to remain competitive.

4G LTE technology enables more network capacity for more data per user as well as faster access to data. U.S. Cellular continues to devote efforts to enhance its network capabilities with the deployment of VoLTE technology and plans a multi-year roll out with one market in early 2017. VoLTE will allow U.S. Cellular's customers and customers of other wireless carriers that have roaming agreements with U.S. Cellular to utilize U.S. Cellular's LTE network for voice and data services. U.S. Cellular continues to offer services based on 3G technology and CDMA digital technology across its networks.

Through roaming agreements with other U.S. based wireless carriers, U.S. Cellular's customers may access CDMA and 4G LTE services in virtually all areas of the United States, as well as CDMA in parts of Canada and Mexico. Another digital technology, Global System for Mobile Communication ("GSM"), has a larger installed base of customers worldwide. U.S. Cellular customers now have the ability to roam on GSM carriers with voice, data and SMS in Canada, Mexico and internationally. Both CDMA and GSM technologies are being succeeded by 4G LTE technology.

*System Design and Construction.* U.S. Cellular designs and constructs its systems in a manner it believes will permit it to provide high-quality service to substantially all types of compatible wireless devices. Designs are based on engineering studies which relate to specific markets, in support of the larger network. Network reliability is given careful consideration and extensive backup redundancy is employed in many aspects of U.S. Cellular's network design. Route diversity, redundant equipment, ring topology and extensive use of emergency standby power also are used to enhance network reliability and minimize service disruption from any particular network element failure.

In accordance with its strategy of building and strengthening its operating market areas, U.S. Cellular has selected high-capacity, carrier-class digital wireless switching systems that are capable of serving multiple markets through a single mobile telephone switching office. Centralized equipment, used for network and data management, is located in high-availability facilities supported by multiple levels of power and network redundancy. U.S. Cellular's systems are designed to incorporate Internet Protocol ("IP") packet-based Ethernet technology, which allows for increased data capacity and a more efficient network. Interconnection between the mobile telephone switching office and the cell sites utilizes Ethernet technology for nearly all 4G LTE sites, over fiber or microwave links.

U.S. Cellular believes that currently available technologies and appropriate capital additions will allow sufficient capacity on its networks to meet anticipated demand for voice and data services over the next few years. However, increasing demand for high-speed data may require the acquisition of additional spectrum licenses to provide sufficient capacity and throughput.

Construction of wireless systems is capital-intensive, requiring substantial investment for land and improvements, buildings, towers, mobile telephone switching offices, cell site equipment, transport equipment, engineering and installation. U.S. Cellular primarily uses its own personnel to engineer each wireless system it owns and operates, and engages contractors to construct the facilities.

The costs (inclusive of the costs to acquire licenses) to develop the systems which U.S. Cellular operates have historically been financed primarily through proceeds from debt and equity offerings, with cash generated by operations, and proceeds from the sales of wireless interests and other non-strategic assets.

**Business Development Strategy**

U.S. Cellular groups its individual markets (geographic service areas as defined by the FCC in which wireless carriers are licensed, for fixed terms, to provide service) into broader geographic market areas to offer customers large service areas that primarily utilize U.S. Cellular's network. U.S. Cellular's ownership interests in wireless licenses include both consolidated and investment interests in operating and non-operating licenses covering portions of 32 states and a total population of 50 million at December 31, 2016.

U.S. Cellular's business development strategy is to obtain interests in and access to wireless licenses in its current operating markets and in areas that are adjacent to or in close proximity to its other wireless licenses, thereby building contiguous operating market areas. U.S. Cellular believes that the acquisition of additional licenses within its current operating markets will enhance its network capacity and speed to meet its customers' growing demand for data services. U.S. Cellular may continue to make opportunistic acquisitions or exchanges that further strengthen its current operating markets. From time to time, U.S. Cellular has divested outright or included in exchanges for other wireless interests certain consolidated and investment interests that were considered less essential to its current and expected future operations. As part of its business development strategy, U.S. Cellular may periodically be engaged in negotiations relating to the acquisition, exchange or disposition of companies, strategic properties or wireless spectrum. See Note 6 — Acquisitions, Divestitures and Exchanges in the Notes to Consolidated Financial Statements for a description of significant acquisitions, divestitures and exchanges in the years 2014 through 2016.



Table of Contents

Occasionally, the FCC conducts auctions through which additional spectrum is made available for the provision of wireless services. Historically, U.S. Cellular has participated in certain prior FCC auctions indirectly through its limited partnership interests. Each entity that qualified as a "designated entity" was eligible for bidding credits with respect to most licenses purchased in accordance with the rules defined by the FCC for each auction. In most cases, the bidding credits resulted in a 25% discount from the gross winning bid. In January 2015, the FCC released the results of Auction 97. U.S. Cellular participated in Auction 97 indirectly through its limited partnership interest in Advantage Spectrum L.P. Advantage Spectrum L.P. applied as a "designated entity" and received bid credits resulting in a 25% discount with respect to spectrum purchased in Auction 97. See Note 13 — Variable Interest Entities in the Notes to Consolidated Financial Statements for additional information. U.S. Cellular may participate as a bidder, or member of a bidding group, in future auctions.

In July 2016, the FCC announced U.S. Cellular as a qualified bidder in the FCC's forward auction of 600MHz spectrum licenses, referred to as Auction 1002. Due to changes in FCC rules, U.S. Cellular did not apply to participate in Auction 1002 by investing in a "designated entity" limited partnership which would have qualified for a discount of 25% on any licenses won in the auction. Instead, U.S. Cellular applied to participate in the auction directly and will not qualify for any discount on licenses that may be won in the auction. See Exhibit 13 to this Form 10-K, under "Regulatory Matters – FCC Auction 1002" for a summary of U.S. Cellular's participation in Auction 1002.

**Regulation**

U.S. Cellular's operations are subject to federal, state and local regulation. Key regulatory considerations are discussed below. Additional information relating to U.S. Cellular's regulatory environment is in Risk Factors and incorporated by reference from Exhibit 13 to this Form 10-K, Annual Report section "Regulatory Matters."

U.S. Cellular provides various wireless services, including voice and data services, pursuant to licenses granted by the FCC. The construction, operation and transfer of wireless systems in the United States are regulated to varying degrees by the FCC pursuant to the Communications Act of 1934, as amended ("Communications Act"). The FCC currently does not require wireless carriers to comply with a number of statutory provisions otherwise applicable to common carriers that provide, originate or terminate interstate or international telecommunications. However, the FCC has enacted regulations governing construction and operation of wireless systems, licensing (including renewal of licenses) and technical standards for the provision of wireless services under the Communications Act.

Wireless licenses segmented by geographic areas are granted by the FCC. The completion of acquisitions, involving the transfer of control of all or a portion of a wireless system, requires prior FCC approval. The FCC determines on a case-by-case basis whether an acquisition of wireless licenses is in the public interest. Wireless licenses are granted generally for a ten year term or, in some cases, for a fifteen year term. The FCC establishes the standards for conducting comparative renewal proceedings between a wireless license holder seeking renewal of its license and challengers filing competing applications. All of U.S. Cellular's licenses for which it applied for renewal since 1995 have been renewed. U.S. Cellular expects to continue to meet the criteria of the FCC's license renewal process.

As part of its data services, U.S. Cellular provides internet access. Such internet access services may be subject to different regulatory requirements than other wireless services.

Reference is made to Exhibit 13 to this Form 10-K under "Regulatory Matters" for information regarding any significant recent developments and proposals relating to the foregoing regulatory matters.

Although the Communications Act generally pre-empts state and local governments from regulating the entry of, or the rates charged by, wireless carriers, certain state and local governments regulate other terms and conditions of wireless services, including billing, termination of service arrangements, imposition of early termination fees, advertising, network outages, the use of handsets while driving, zoning and land use. Further, the Federal Aviation Administration also regulates the siting, lighting and construction of transmitter towers and antennae.

**Debt Securities**

The following securities trade on the NYSE: U.S. Cellular's 6.95% Senior Notes due 2060 trade under the symbol "UZA," U.S. Cellular's 7.25% Senior Notes due 2063 trade under the symbol "UZB," and U.S. Cellular's 7.25% Senior Notes due 2064 trade under the symbol "UZC." U.S. Cellular's 6.7% Senior Notes due 2033 are traded over the counter and are not listed on any stock exchange.

**Employees**

U.S. Cellular had approximately 6,300 full-time and part-time employees as of December 31, 2016. None of U.S. Cellular's employees are represented by labor organizations. U.S. Cellular considers its relationship with its employees to be good.



Table of Contents**Location and Company Information**

U.S. Cellular executive offices are located at 8410 West Bryn Mawr Avenue, Chicago, Illinois 60631. U.S. Cellular's telephone number is 773-399-8900. U.S. Cellular's website address is [www.uscellular.com](http://www.uscellular.com). U.S. Cellular files with, or furnishes to, the Securities and Exchange Commission ("SEC") annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, as well as various other information. Investors may access, free of charge, through the Investor Relations portion of the website, U.S. Cellular's annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to such reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practical after such material is filed electronically with the SEC. The public may read and copy any materials U.S. Cellular files with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington D.C. 20549. The public may obtain information on the operation of the Reference Room by calling the SEC at 1-800-732-0330. The public may also view electronic filings of U.S. Cellular by accessing SEC filings at [www.sec.gov](http://www.sec.gov).

[Table of Contents](#)

## Item 1A. Risk Factors

### PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995 SAFE HARBOR CAUTIONARY STATEMENT

This Annual Report on Form 10-K, 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 U.S. Cellular 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 are 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 under "Risk Factors" in this Form 10-K. Each of the following risks could have a material adverse effect on U.S. Cellular's business, financial condition or results of operations; 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. U.S. Cellular 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 following risk factors and other information contained in, or incorporated by reference into, this Form 10-K to understand the material risks relating to U.S. Cellular's business.

#### Risk Factors

**1. Intense competition in the markets in which U.S. Cellular operates could adversely affect U.S. Cellular's revenues or increase its costs to compete.**

Competition in the wireless industry is intense and is expected to intensify in the future due to multiple wireless industry factors such as increasing market penetration, decreasing customer churn rates, introduction of new products, new competitors and changing prices. There is competition in pricing; handsets and other devices; network quality, coverage, speed and technologies; distribution; new entrants; and other categories. In particular, wireless competition includes aggressive promotional pricing to induce customers to switch carriers, which could result in switching activity and churn; data network speed is a competitive differentiator; and there has been a resurgence of new entrants to wireless markets including prepaid brands that have been purchased by national carriers. U.S. Cellular's ability to compete effectively will depend, in part, on its ability to anticipate and respond to various competitive factors affecting the telecommunications industry. U.S. Cellular anticipates that competition will continue to cause the prices for products and services to decline and the costs to compete to increase. Most of U.S. Cellular's competitors are national or global telecommunications companies that are larger than U.S. Cellular, possess greater financial and other resources, possess more extensive coverage areas and more spectrum within their coverage areas, and market other services with their communications services that U.S. Cellular does not offer. Further, other companies that currently are less competitive may also add more efficient low-band spectrum to become more competitive in U.S. Cellular's primary markets. In particular, to the extent that existing competitors or new entrants acquire low-band (600 MHz) spectrum in FCC Auction 1002 in U.S. Cellular markets, U.S. Cellular could face increased competition over time from competitors which hold more efficient low-band spectrum. In addition, U.S. Cellular may face competition from technologies that may be introduced in the future. New technologies, services and products that are more commercially effective than the technologies, services and products offered by U.S. Cellular may be developed. Further, new technologies may be proprietary such that U.S. Cellular is not able to adopt such technologies. There can be no assurance that U.S. Cellular will be able to compete successfully in this environment.

Sources of competition to U.S. Cellular's business typically include two to four competing wireless telecommunications service providers in each market, wireline telecommunications service providers, cable companies, resellers (including MVNO), and providers of other alternate telecommunications services. Many of U.S. Cellular's wireless competitors and other competitors have substantially greater financial, technical, marketing, sales, purchasing and distribution resources than U.S. Cellular.

If U.S. Cellular does not adapt to compete effectively in such a highly competitive environment, such competitive factors could result in product, service, pricing or cost disadvantages and could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.

Table of Contents**2. A failure by U.S. Cellular to successfully execute its business strategy (including planned acquisitions, spectrum acquisitions, divestitures and exchanges) or allocate resources or capital could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular is a regional wireless carrier, but competes primarily against much larger national wireless carriers with much greater resources. Its business strategy in attempting to attract and retain wireless customers through a value proposition comprised of a high-quality network, outstanding customer service, and competitive devices, plans and pricing, all provided with a local focus has not resulted in, and in the future may not result in, performance that achieves returns in line with or above its cost of capital. U.S. Cellular's current forecast indicates that U.S. Cellular will not achieve a return on capital that exceeds its cost of capital in the foreseeable future. U.S. Cellular also might be unable to adopt technologies, products and services as fast as its larger competitors. As a result, consumers who are eager to adopt new technologies, products and services more quickly may select U.S. Cellular's competitors rather than U.S. Cellular as their service provider. To the extent that U.S. Cellular does not attract or retain these types of customers, U.S. Cellular could be at a competitive disadvantage and have a customer base that generates lower profit margins relative to its competition.

The successful execution of strategy and optimal capital allocation decisions depend on various internal and external factors, many of which are not in U.S. Cellular's control. U.S. Cellular's ability to achieve projected financial results by implementing and executing its business strategy and optimally allocating its assets and capital could be affected by such factors. Such factors include but are not limited to pricing practices by competitors, relative scale, purchasing power, roaming and other strategic agreements, wireless device availability, timing of introduction of wireless devices, access to spectrum, emerging technologies and other factors. In addition, there is no assurance that U.S. Cellular's strategy will be successful. Even if U.S. Cellular executes its business strategy as intended, such strategy may not be successful in the long term at achieving growth in customers, revenues, net income, or generating a return on capital greater than U.S. Cellular's cost of capital. A failure by U.S. Cellular to execute its business strategy successfully or to allocate resources or capital optimally could have an adverse effect on U.S. Cellular's wireless business, financial condition or results of operations.

**3. Uncertainty in U.S. Cellular's future cash flow and liquidity or in the ability to access capital, deterioration in the capital markets, other changes in U.S. Cellular's performance or market conditions, changes in U.S. Cellular's credit ratings or other factors could limit or restrict the availability of financing on terms and prices acceptable to U.S. Cellular, which could require U.S. Cellular to reduce its construction, development or acquisition programs, reduce the acquisition of spectrum licenses, and/or reduce or cease share repurchases.**

U.S. Cellular operates a capital-intensive business. U.S. Cellular has used internally-generated funds and also has obtained substantial funds from external sources for general corporate purposes. In the past, U.S. Cellular's existing cash and investment balances, funds available under its revolving credit facilities, funds from other financing sources, including a term loan and other long-term debt, and cash flows from operating, investing and financing activities, including sales of assets or businesses, provided sufficient liquidity and financial flexibility for U.S. Cellular to meet its normal day-to-day operating needs and debt service requirements, to finance the build-out and enhancement of markets and to fund acquisitions. There is no assurance that this will be the case in the future. It may be necessary from time to time to increase the size of the existing revolving credit facility, to put in place new credit facilities, or to obtain other forms of financing in order to fund potential expenditures. U.S. Cellular's liquidity would be adversely affected if, among other things, U.S. Cellular is unable to obtain short or long-term financing on acceptable terms, U.S. Cellular makes spectrum license purchases in FCC auctions or from other parties, the LA Partnership discontinues or reduces distributions compared to prior historical levels and/or Eligible Telecommunications Carrier ("ETC") and/or other regulatory support payments decline. In addition, although sales of assets or businesses by U.S. Cellular have been an important source of liquidity for U.S. Cellular in recent periods, U.S. Cellular does not expect a similar level of such sales in the future, which will reduce a source of liquidity for U.S. Cellular. In recent years, U.S. Cellular's credit rating has declined to sub-investment grade. In certain recent periods, U.S. Cellular has incurred negative free cash flow (defined as Cash flows from operating activities less Cash paid for additions to property, plant and equipment) and this will continue in the future if operating results do not improve or if capital expenditures do not decrease. U.S. Cellular currently expects to have negative free cash flow in 2017. U.S. Cellular may require substantial additional capital for, among other uses, funding day-to-day operating needs, working capital, acquisitions of providers of wireless telecommunications services, spectrum license or system acquisitions, system development and network capacity expansion, debt service requirements, the repurchase of shares, or making additional investments. There can be no assurance that sufficient funds will continue to be available to U.S. Cellular or its subsidiaries on terms or at prices acceptable to U.S. Cellular. Insufficient cash flows from operating activities, changes in its credit ratings, defaults of the terms of debt or credit agreements, uncertainty of access to capital, deterioration in the capital markets, reduced regulatory capital at banks which in turn limits their ability to borrow and lend, other changes in the performance of U.S. Cellular or in market conditions or other factors could limit or restrict the availability of financing on terms and prices acceptable to U.S. Cellular, which could require U.S. Cellular to reduce its acquisition, capital expenditure and business development programs, reduce the acquisition of spectrum licenses, and/or reduce or cease share repurchases. U.S. Cellular cannot provide assurances that circumstances that could have a material adverse effect on its liquidity or capital resources will not occur. Any of the foregoing would have an adverse impact on U.S. Cellular's business, financial condition or results of operations.



[Table of Contents](#)**4. U.S. Cellular has a significant amount of indebtedness which could adversely affect its financial performance and in turn adversely affect its ability to make payments on its indebtedness, comply with terms of debt covenants and incur additional debt.**

U.S. Cellular has a significant amount of indebtedness and may need to incur additional indebtedness. U.S. Cellular's level of indebtedness could have important consequences. For example, it (i) may limit U.S. Cellular's ability to obtain additional financing for working capital, capital expenditures or general corporate purposes, particularly if the ratings assigned to its debt securities by rating organizations are revised downward; (ii) will require U.S. Cellular to dedicate a substantial portion of its cash flow from operations to the payment of interest and principal on its debt, reducing the funds available to U.S. Cellular for other purposes including expansion through acquisitions, capital expenditures, marketing spending and expansion of its business; and (iii) may limit U.S. Cellular's flexibility to adjust to changing business and market conditions and make U.S. Cellular more vulnerable to a downturn in general economic conditions as compared to U.S. Cellular's competitors. U.S. Cellular's ability to make scheduled payments on its indebtedness or to refinance it will depend on its financial and operating performance, which, in turn, is subject to prevailing economic and competitive conditions and other factors beyond its control. In addition, U.S. Cellular's leverage may put it at a competitive disadvantage to some of its competitors that are not as leveraged. U.S. Cellular's revolving credit facility and the U.S. Cellular term loan facility require U.S. Cellular to comply with certain affirmative and negative covenants, including certain financial covenants. Depending on actual financial performance of U.S. Cellular, there is a risk that U.S. Cellular could fail to satisfy the required financial covenants. If U.S. Cellular breaches a financial or other covenant of any of these agreements, it would result in a default under that agreement, and could involve a cross-default under other debt instruments. This could in turn cause the affected lenders to accelerate the repayment of principal and accrued interest on any outstanding debt under such agreements and, if they choose, terminate the facility. If appropriate, U.S. Cellular may request the applicable lender for an amendment of financial covenants in the U.S. Cellular revolving credit facility and the U.S. Cellular term loan facility, in order to provide additional financial flexibility to U.S. Cellular, and may also seek other changes to such facilities. There is no assurance that the lenders will agree to any amendments. If the lenders agree to amendments, this may result in additional payments or higher interest rates payable to the lenders and/or additional restrictions. Restrictions in such debt instruments may limit U.S. Cellular's operating and financial flexibility.

As a result, U.S. Cellular's level of indebtedness, restrictions contained in debt instruments and/or possible breaches of covenants, defaults, and acceleration of indebtedness could have an adverse effect on U.S. Cellular's business, financial condition, revenues, results of operations and cash flows.

**5. Changes in roaming practices or other factors could cause U.S. Cellular's roaming revenues to decline from current levels, roaming expenses to increase from current levels and/or impact U.S. Cellular's ability to service its customers in geographic areas where U.S. Cellular does not have its own network, which could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular's service revenues include roaming revenues related to the use of U.S. Cellular's network by other carriers' customers who travel within U.S. Cellular's coverage areas. Changes in the network footprints of carriers due to mergers, acquisitions or network expansions could have an adverse effect on U.S. Cellular's roaming revenues. For example, consolidation among other carriers which have network footprints that currently overlap U.S. Cellular's network could decrease the amount of roaming revenues for U.S. Cellular.

Similarly, U.S. Cellular's customers can access another carrier's digital system automatically only if the other carrier allows U.S. Cellular's customers to roam on its network. U.S. Cellular relies on roaming agreements with other carriers to provide roaming capability to its customers in areas of the U.S. and internationally outside of its service areas, including Mexico and Canada, and to improve coverage within selected areas of U.S. Cellular's network footprint. Such agreements cover traditional voice services as well as data services. Although U.S. Cellular currently has long-term roaming agreements with certain other carriers, these agreements generally are subject to renewal and termination if certain events occur. FCC rules and orders impose certain requirements on wireless carriers to offer certain roaming arrangements to other carriers. However, carriers frequently disagree on what is required. Although U.S. Cellular has entered into 4G LTE roaming agreements with national carriers, there is no assurance that U.S. Cellular will be able to maintain these agreements and/or enter into new agreements with other carriers to provide roaming services using 4G LTE or other technologies or that it will be able to do so on reasonable or cost-effective terms.

Some competitors may be able to obtain lower roaming rates than U.S. Cellular is able to obtain because they have larger call volumes or may be able to reduce roaming charges by providing service principally over their own networks. In addition, the quality of service that a wireless carrier delivers during a roaming call may be inferior to the quality of service U.S. Cellular provides, the price of a roaming call may not be competitive with prices of other wireless carriers for such call, and U.S. Cellular's customers may not be able to use some of the advanced features, such as voicemail notification or data applications, that U.S. Cellular's customers enjoy when making calls on U.S. Cellular's network. U.S. Cellular's rate of adoption of new technologies, such as those enabling high-speed data and voice services, could affect its ability to enter into or maintain roaming agreements with other carriers. In addition, U.S. Cellular's wireless technology may not be compatible with technologies used by other carriers, which may limit the ability of U.S. Cellular to enter into voice or data roaming agreements with such other carriers. Carriers whose customers roam on U.S. Cellular's network could switch their business to new operators or, over time, to their own networks. Changes in roaming usage patterns, rates for roaming minutes or data usage or relationships with carriers whose customers generate roaming minutes or data use on U.S. Cellular's network could have an adverse effect on U.S. Cellular's revenues and revenue growth. Further, other carriers could negotiate higher roaming rates for accessing their networks, resulting in increased roaming expense for U.S. Cellular.



Table of Contents

To the extent that other carriers expand their networks in U.S. Cellular's service areas, the roaming arrangements between U.S. Cellular and these other carriers could become less strategic for them. That is, these other carriers will have fewer or less extensive geographic areas where roaming services are required by their customers and, as a result, the roaming arrangements could become less critical to serving their customer base. This presents a risk to U.S. Cellular in that, to the extent U.S. Cellular is not able to enter into economically viable roaming arrangements with these other carriers, this could impact U.S. Cellular's ability to service its customers in geographic areas where U.S. Cellular does not have its own network.

If U.S. Cellular's roaming revenues decline, roaming expenses increase, or if U.S. Cellular is unable to obtain or maintain roaming agreements with other carriers that contain pricing and other terms that are competitive and acceptable to U.S. Cellular, and that satisfy U.S. Cellular's quality and interoperability requirements, its business, financial condition or results of operations could be adversely affected.

**6. A failure by U.S. Cellular 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 U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular's business depends on the ability to use portions of the radio spectrum licensed by the FCC. U.S. Cellular could fail to obtain access to sufficient spectrum capacity in new or existing critical markets, whether through FCC auctions or other transactions, in order to meet the anticipated spectrum requirements associated with increased demand for existing services, especially increases in customer demand for data services, and to enable deployment of next-generation services. U.S. Cellular believes that this increased demand for data services reflects a trend that will continue for the foreseeable future. However, U.S. Cellular could fail to accurately forecast its future spectrum requirements considering changes in customer usage patterns, technology requirements and the expanded demands of new services. Such a failure could have an adverse impact on the quality of U.S. Cellular's services or U.S. Cellular's ability to roll out such future services in some markets, or could require that U.S. Cellular curtail existing services in order to make spectrum available for next-generation services. Spectrum constrained providers could be effectively capped in increasing market share. As spectrum constrained providers gain customers, they use up their network capacity. Since they lack spectrum, they can respond to demand only by adding cell sites, which is capital intensive, adds fixed operating costs, is limited by zoning considerations, and ultimately may not be cost effective.

U.S. Cellular may acquire access to spectrum through a number of alternatives, including acquisitions, exchanges and participation in spectrum auctions. U.S. Cellular may participate in spectrum auctions conducted by the FCC in the future. As required by law, the FCC has conducted auctions for licenses to use some parts of the radio spectrum. The decision to conduct auctions, and the determination of what spectrum frequencies will be made available for auction and the determination of geographic size of licenses, are made by the FCC pursuant to laws that it administers. The FCC may not be able to allocate spectrum sufficient to meet the demands of all those wishing to obtain licenses for new market entry or to expand their spectrum holdings to meet the expanding demand for data services or to address other spectrum constraints. Due to factors such as geographic size of licenses and auction bidders that may raise prices beyond acceptable levels, U.S. Cellular may not be successful in FCC auctions in obtaining access to the spectrum that it believes is necessary to implement its business and technology strategies.

In addition, newly auctioned spectrum may not be compatible with existing spectrum, and vendors may not create suitable products to use such spectrum. Further, access to spectrum licenses won in FCC auctions may not be available on a timely basis. Such access is dependent upon the FCC actually granting licenses won, which can be delayed for various reasons. Furthermore, newly licensed spectrum may not be available for immediate use since the radio operations of incumbent users, including in some cases government agencies, may need to be relocated to other portions of the radio spectrum, and/or the newly licensed spectrum may be subject to sharing and coordination obligations for a period of time. U.S. Cellular also may seek to acquire radio spectrum through purchases and exchanges with other spectrum licensees. However, U.S. Cellular may not be able to acquire sufficient spectrum through these types of transactions, and U.S. Cellular may not be able to complete any of these transactions on favorable terms.

**7. To the extent conducted by the FCC, U.S. Cellular may participate in FCC auctions of additional spectrum in the future directly or indirectly and, during certain periods, will be subject to the FCC's anti-collusion rules, which could have an adverse effect on U.S. Cellular.**

From time to time, the FCC conducts auctions through which additional spectrum is made available for the provision of wireless services. U.S. Cellular has participated in such auctions in the past and may participate in other auctions conducted by the FCC in the future. FCC anti-collusion rules place certain restrictions on business communications and disclosures by participants in an FCC auction. These anti-collusion rules may restrict the normal conduct of U.S. Cellular's business, U.S. Cellular's acquisition, divestiture, exchange and other corporate development activity and/or disclosures by U.S. Cellular relating to an FCC auction. The restrictions could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.

As a result of its application to participate in the FCC's forward auction of 600 MHz spectrum licenses, referred to as Auction 1002, since February 10, 2016, U.S. Cellular has been subject to FCC anti-collusion rules that place certain restrictions on public disclosures and business communications with other companies relating to U.S. Cellular's participation. As a result of the FCC's announcement of U.S. Cellular as a qualified bidder on July 15, 2016, these restrictions will continue until the down payment deadline for Auction 1002, which will be ten business days after release of the FCC's Channel Reassignment Public Notice, following the end of the auction. These anti-collusion rules may restrict the conduct of certain U.S. Cellular activities with other auction applicants as well as with nationwide providers of wireless services which are not applicants. The restrictions could have an adverse effect on U.S. Cellular's business, financial condition or results of operations. See Exhibit 13 to this Form 10-K, under "Regulatory Matters – FCC Auction 1002" for a summary of U.S. Cellular's participation in Auction 1002.

Table of Contents**8. Failure by U.S. Cellular to timely or fully comply with any existing applicable legislative and/or regulatory requirements or changes thereto could adversely affect U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular's operations are subject to varying degrees of regulation by the FCC, state public utility commissions and other federal, state and local regulatory agencies and legislative bodies. Changes in the administration of the various regulatory agencies and legislative bodies could result in different policies with respect to many federal laws and regulations, including but not limited to changes to fiscal and tax policies, which may include comprehensive tax reform. New or amended regulatory requirements could increase U.S. Cellular's costs and divert resources from other initiatives. Adverse decisions, increased regulation, or changes to existing regulation by regulatory bodies could negatively impact U.S. Cellular's operations by, among other things, changing the amount that can be charged for local, intrastate or interstate access rates, increasing U.S. Cellular's costs of doing business, permitting greater competition or limiting U.S. Cellular's ability to engage in certain sales or marketing activities. New regulatory mandates or enforcement may require unexpected or increased capital expenditures, lost revenues, higher operating expenses or other changes. Court decisions and rulemakings could have a substantial impact on U.S. Cellular's operations, including rulemakings on intercarrier access compensation and state and federal universal service. Litigation and different objectives among federal and state regulators could create uncertainty and delay U.S. Cellular's ability to respond to new regulations. Further, wireless licenses are subject to renewal by the FCC and could be revoked in the event of a violation of applicable laws or regulatory requirements. Also, FCC rules relating to net neutrality, broadband consumer privacy and other rules may result in additional costs for compliance and may limit opportunities to derive profits from certain business practices or resources, if not amended or rescinded.

U.S. Cellular attempts to timely and fully comply with all regulatory requirements. However, U.S. Cellular is unable to predict the future actions of the various legislative and regulatory bodies that govern U.S. Cellular, but such actions could have adverse effects on U.S. Cellular's business. Any failure by U.S. Cellular to timely or fully comply with any regulatory requirements could adversely affect U.S. Cellular's financial condition, results of operations or ability to do business.

For additional information about U.S. Cellular's regulatory environment, see Risk Factor Number 15 below and "Regulatory Matters" in Exhibit 13 to this Form 10-K.

**9. An inability to attract people of outstanding potential, to develop their potential through education and assignments, and to retain them by keeping them engaged, challenged and properly rewarded could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular's business is highly technical and competition for skilled talent in the wireless industry is aggressive. Due to competition for qualified management, technical, sales and other personnel, there can be no assurance that U.S. Cellular will be able to continue to attract and/or retain people of outstanding potential for the development of its business. The loss of the services of existing key personnel as well as the failure to recruit additional qualified personnel in a timely manner could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.

**10. U.S. Cellular's assets are concentrated in the U.S. wireless telecommunications industry. Consequently, its operating results may fluctuate based on factors related primarily to conditions in this industry.**

U.S. Cellular's assets and revenue streams are concentrated in the U.S. wireless telecommunications industry. The U.S. wireless telecommunications industry is facing significant change and an uncertain operating environment. U.S. Cellular's focus on the U.S. wireless telecommunications industry, together with its positioning relative to larger competitors with greater resources within the industry, may represent increased risk for investors due to the lack of diversification. This could have an adverse effect on U.S. Cellular's ability to attain and sustain long-term, profitable revenue growth and could have an adverse effect on its business, financial condition or results of operations.

**11. U.S. Cellular's smaller scale relative to larger competitors that may have greater financial and other resources than U.S. Cellular could cause U.S. Cellular to be unable to compete successfully, which could adversely affect its business, financial condition or results of operations.**

There has been a trend in the telecommunications and related industries in recent years towards consolidation of service providers through acquisitions, reorganizations and joint ventures. This trend could continue, leading to larger competitors over time. U.S. Cellular has smaller scale efficiencies compared to larger competitors. U.S. Cellular may be unable to compete successfully with larger companies that have substantially greater financial, technical, marketing, sales, purchasing and distribution resources or that offer more services than U.S. Cellular, which could adversely affect U.S. Cellular's revenues and costs of doing business. Specifically, U.S. Cellular's smaller scale relative to most of its competitors could have the following impacts, among others:

- Low profit margins and returns on investment that are below U.S. Cellular's cost of capital;
- Increased operating costs due to lack of leverage with vendors;
- Limited opportunities for strategic partnerships as potential partners are focused on wireless companies with greater scale and scope;
- Limited access to content;
- Limited ability to influence industry standards;
- Reduced ability to invest in research and development of new products and services;

- Vendors may deem U.S. Cellular non-strategic and not develop or sell products and services to U.S. Cellular, particularly where technical requirements differ from those of larger companies;
- Limited access to intellectual property; and
- Other limited opportunities such as for software development or third party distribution.

## Table of Contents

U.S. Cellular's business increasingly depends on access to content for data and access to new wireless devices being developed by vendors. U.S. Cellular's ability to obtain such access depends in part on other parties. If U.S. Cellular is unable to obtain timely access to new content or wireless devices being developed by vendors, its business, financial condition or results of operations could be adversely affected.

As a result of the foregoing, U.S. Cellular's smaller scale relative to larger competitors could adversely affect U.S. Cellular's business, financial condition or results of operations.

### **12. Changes in various business factors, including changes in demand, customer preferences and perceptions, price competition, churn from customer switching activity and other factors, could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

Changes in any of several factors could have an adverse effect on U.S. Cellular's business, financial condition or results of operations. These factors include, but are not limited to:

- Demand for or usage of services, particularly data services;
- Customer preferences, including type of wireless devices;
- Customer perceptions of network quality and performance;
- The pricing of services, including an increase in price-based competition;
- The overall size and growth rate of U.S. Cellular's customer base;
- Penetration rates;
- Churn rates;
- Selling expenses;
- Net customer acquisition and retention costs;
- Customers' ability to pay for wireless service and the potential impact on bad debts expense;
- Roaming agreements and rates;
- Third-party vendor support;
- The mix of products and services offered by U.S. Cellular and purchased by customers; and
- The costs of providing products and services.

### **13. Advances or changes in technology could render certain technologies used by U.S. Cellular obsolete, could put U.S. Cellular at a competitive disadvantage, could reduce U.S. Cellular's revenues or could increase its costs of doing business.**

The telecommunications industry is experiencing significant changes in technologies and services expected by customers, as evidenced by evolving industry standards, ongoing improvements in the capacity and quality of digital technology, shorter development cycles for new services and products, and enhancements and changes in end-user requirements and preferences. Widespread deployment of new technologies could cause the technology used on U.S. Cellular's wireless networks to become less competitive or obsolete. Further, fixed-mobile convergence services that combine wireline broadband services with mobile services represent a competitive threat. If the trend toward convergence continues, U.S. Cellular is at a competitive disadvantage to larger competitors, including the national wireless carriers and other potential large new entrants with much greater financial and other resources in adapting to such convergence. Future technological changes or advancements may enable other wireless technologies to equal or exceed U.S. Cellular's current levels of service and render its system infrastructure obsolete. For example, the timing, cost, and availability of CDMA enabled devices and other CDMA ecosystem support needs may inhibit U.S. Cellular's ability to maintain 3G wireless voice services until it is fully replaced by VoLTE. U.S. Cellular may not be able to respond to such changes and implement new technology on a timely or cost-effective basis, which could reduce its revenues or increase its costs of doing business. If U.S. Cellular cannot keep pace with these technological changes or other changes in the telecommunications industry over time, its financial condition, results of operations or ability to do business could be adversely affected.

### **14. Complexities associated with deploying new technologies present substantial risk and U.S. Cellular investments in unproven technologies may not produce the benefits that U.S. Cellular expects.**

U.S. Cellular has completed the transition to 4G LTE and has implemented 4G LTE roaming agreements with national carriers. U.S. Cellular will begin commercial deployment of VoLTE in early 2017 and has begun testing 5G technology. Transition to new technologies involves significant time and cost. Furthermore, the wireless business experiences rapid technology changes and new services and products. If U.S. Cellular fails to effectively deploy new wireless technologies, services or products on a timely basis, this could have an adverse impact on U.S. Cellular's business, financial condition and results of operations.

Furthermore, it is not certain that U.S. Cellular's investments in various new, unproven technologies and service and product offerings will be effective. The markets for some of these services, products and solutions may still be emerging and the overall potential for these markets may be uncertain. If customer demand for these new services, products and solutions does not develop as expected, U.S. Cellular's business, financial condition or results of operations could be adversely affected.



[Table of Contents](#)**15. U.S. Cellular receives regulatory support and is subject to numerous surcharges and fees from federal, state and local governments, and the applicability and the amount of the support and fees are subject to great uncertainty, which could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

Telecommunications companies may be designated by states, or in some cases by the FCC, as an ETC to receive universal service support payments if they provide specified services in "high cost" areas. U.S. Cellular has been designated as an ETC in certain states and received \$92 million in high cost support for service to high cost areas in 2016.

In 2011, the FCC released an order ("Reform Order") to: reform its universal service and intercarrier compensation mechanisms; establish a new, broadband-focused support mechanism; and propose further rules to advance reform. Pursuant to the Reform Order, U.S. Cellular's ETC support has been phased down by 40% since July 1, 2012. As provided by the Reform Order, the phasedown is currently suspended and U.S. Cellular will continue to receive 60% of its baseline support until a new fund proposed in the Reform Order is operational. On February 23, 2017, the FCC adopted an order concerning the Mobility Fund II and the resumption of the phase down. The text of the order has not been released but the press release issued by the FCC following adoption of the order indicates that the order will establish a Mobility Fund II support mechanism of \$453 million annually for ten years to be distributed through a market-based, multi-round reverse auction and that the phase down of unnecessary legacy support from the Federal USF will commence on the first day of the month following the completion of the auction and will conclude two years later. U.S. Cellular cannot predict at this time when the Mobility Fund II auction will occur, when the phase down period for its existing legacy support from the Federal USF will commence, or whether the Mobility Fund II auction will provide opportunities to the Company to offset any loss in existing support. However, U.S. Cellular currently expects that its legacy support will continue at the existing level for 2017. If the foregoing regulatory support is reduced from current levels, this could have an adverse effect on U.S. Cellular's business, financial condition or operating results. With respect to intercarrier compensation, the Reform Order provides for a reduction in the charges that U.S. Cellular pays to wireline phone companies to transport and terminate calls that originate on their networks, which will reduce U.S. Cellular's operating expenses. The reductions in intercarrier charges are to increase over the next five to ten years, further reducing U.S. Cellular's operating expenses.

Telecommunications providers pay a variety of surcharges and fees on their gross revenues from interstate and intrastate services, including USF fees and common carrier regulatory fees.

The division of services between interstate services and intrastate services, including the divisions associated with the Federal USF fees, is a matter of interpretation and may in the future be contested by the FCC or state authorities. The FCC also may change in the future the basis on which Federal USF fees are charged. The Federal government and many states also apply transaction-based taxes to sales of telecommunications products and services and to purchases of telecommunications services from various carriers. In addition, state regulators and local governments have imposed and may continue to impose various surcharges, taxes and fees on telecommunications services. The applicability of these surcharges and fees to its services is uncertain in many cases and jurisdictions may contest whether U.S. Cellular has assessed and remitted those monies correctly. Periodically, state and federal regulators may increase or change the surcharges and fees U.S. Cellular currently pays. In some instances, U.S. Cellular passes through these charges to its customers. However, Congress, the FCC, state regulatory agencies or state legislatures may limit the ability to pass through transaction-based tax liabilities, regulatory surcharges and regulatory fees imposed on U.S. Cellular to customers. U.S. Cellular may or may not be able to recover some or all of those taxes from its customers and the amount of taxes may deter demand for its services or increase its cost to provide service which could have an adverse effect on its business, financial condition or operating results.

**16. Performance under device purchase agreements could have a material adverse impact on U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular has entered into purchase commitments with certain vendors and may enter into similar purchase commitments with other vendors in the future. If U.S. Cellular is unable to sell all of the devices that it is required to purchase under such agreements, or if it is unable to sell them at the prices it projects, its business, financial condition or results of operations could be adversely affected.

**17. Changes in U.S. Cellular's enterprise value, changes in the market supply or demand for wireless licenses, adverse developments in the business or the industry in which U.S. Cellular is involved and/or other factors could require U.S. Cellular to recognize impairments in the carrying value of its licenses, goodwill and/or physical assets.**

A large portion of U.S. Cellular's assets consists of indefinite-lived intangible assets in the form of licenses and goodwill. U.S. Cellular also has substantial investments in long-lived assets such as property, plant and equipment. U.S. Cellular reviews its licenses, goodwill and other long-lived assets for impairment annually or whenever events or circumstances indicate that the carrying amount of such assets may not be fully recoverable. An impairment loss may need to be recognized to the extent the carrying value of the assets exceeds the fair value of such assets. The amount of any such impairment loss could be significant and could have an adverse effect on U.S. Cellular's reported financial results for the period in which the loss is recognized. The estimation of fair values requires assumptions by management about factors that are uncertain including such things as future cash flows and the appropriate discount rate. Different assumptions for these factors could create materially different results.



Table of Contents**18. Costs, integration problems or other factors associated with acquisitions, divestitures or exchanges of properties or licenses and/or expansion of U.S. Cellular's business could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

As part of U.S. Cellular's operating strategy, U.S. Cellular from time to time may be engaged in the acquisition, divestiture or exchange of companies, businesses, strategic properties, wireless spectrum or other assets. U.S. Cellular may change the markets in which it operates and the services that it provides through such acquisitions, divestitures and/or exchanges. In general, U.S. Cellular may not disclose the negotiation of such transactions until a definitive agreement has been reached.

These transactions commonly involve a number of risks, including:

- Identification of attractive companies, businesses, properties, spectrum or other assets for acquisition or exchange, and/or the selection of U.S. Cellular's businesses or assets for divestiture or exchange;
- Competition for acquisition targets and the ability to acquire or exchange businesses at reasonable prices;
- Inability to make acquisitions that would achieve sufficient scale to be competitive with competitors with greater scale;
- Possible lack of buyers for businesses or assets that U.S. Cellular desires to divest and the ability to divest or exchange such businesses or assets at reasonable prices;
- Ability to negotiate favorable terms and conditions for acquisitions, divestitures and exchanges;
- Significant expenditures associated with acquisitions, divestitures and exchanges;
- Legal and regulatory risks associated with new businesses or markets;
- Ability to enter markets in which U.S. Cellular has limited or no direct prior experience and competitors have stronger positions;
- Ability to integrate and manage businesses that are engaged in activities other than traditional wireless service;
- Uncertain revenues and expenses associated with acquisitions, with the result that U.S. Cellular may not realize the growth in revenues, anticipated cost structure, profitability, or return on investment that it expects;
- Difficulty of integrating the technologies, services, products, operations and personnel of the acquired businesses, or of separating such matters for divested businesses or assets;
- Diversion of management's attention;
- Disruption of ongoing business;
- Impact on U.S. Cellular's cash and available credit lines for use in financing future growth and working capital needs;
- Inability to retain key personnel;
- Inability to successfully incorporate acquired assets and rights into U.S. Cellular's service offerings;
- Inability to maintain uniform standards, controls, procedures and policies;
- Possible conditions to approval by the FCC, the Federal Trade Commission and/or the Department of Justice; and
- Impairment of relationships with employees, customers or vendors.

No assurance can be given that U.S. Cellular will be successful with respect to its acquisition, divestiture or exchange strategies or initiatives. If U.S. Cellular is not successful with respect to its acquisitions, divestitures or exchanges, its business, financial condition or results of operations could be adversely affected.

**19. U.S. Cellular offers customers the option to purchase certain devices under installment contracts which, compared to fixed-term service contracts, includes risks that U.S. Cellular may possibly incur greater churn, lower cash flows, increased costs and/or increased bad debts expense due to differences in contract terms, which could have an adverse impact on U.S. Cellular's financial condition or results of operations.**

U.S. Cellular sells devices to customers under installment contracts over a specified period of time. Customers with installment contracts are not required to sign a fixed-term service contract to obtain postpaid service; rather, their service is provided on a month to month basis with no early termination fee. These device installment contract plans may not meet U.S. Cellular's customers' or potential customers' needs, expectations or demands. In addition, customers on these device installment contract plans can discontinue their service at any time without penalty, other than the obligation of any residual commitment they may have for unpaid service or for amounts due under the installment contract for the device. U.S. Cellular could experience a higher churn rate than it expects due to the ability of customers to more easily change service providers, which could adversely affect its results of operations. U.S. Cellular's operational and financial performance may be adversely affected if it is unable to grow its customer base and achieve the customer penetration levels that it anticipates with this business model.

Customers who have financed their devices through these device installment contracts pay for their devices in installments over a specified period of time. Compared to fixed-term service contracts, such plans result in lower cash flows from operating activities in the near term and could have an adverse effect on U.S. Cellular's liquidity or capital resources. In addition, such device installment contracts subject U.S. Cellular to increased risks relating to consumer credit issues, which could result in increased costs, including increases to its bad debts expense. These device installment contracts may be particularly sensitive to changes in general economic conditions, and any declines in the credit quality of U.S. Cellular's customer base could have a material adverse effect on U.S. Cellular's financial condition or results of operations.



Table of Contents**20. A failure by U.S. Cellular to complete significant network construction and systems implementation activities as part of its plans to improve the quality, coverage, capabilities and capacity of its network, support and other systems and infrastructure could have an adverse effect on its operations.**

U.S. Cellular's business plan includes significant construction activities and enhancements to its network, support and other systems and infrastructure. As U.S. Cellular deploys, expands and enhances its network, it may need to acquire additional spectrum. Also, as U.S. Cellular continues to build out and enhance its network, U.S. Cellular must, among other things, continue to:

- Lease, acquire or otherwise obtain rights to cell and switch sites;
- Obtain zoning variances or other local governmental or third-party approvals or permits for network construction;
- Complete and update the radio frequency design, including cell site design, frequency planning and network optimization, for each of U.S. Cellular's markets; and
- Improve, expand and maintain customer care, network management, billing and other financial and management systems.

Any difficulties encountered in completing these activities, as well as problems in vendor equipment availability, technical resources, system performance or system adequacy, could delay expansion of operations and product capabilities in new or existing markets or result in increased costs. Failure to successfully build-out and enhance U.S. Cellular's network and necessary support facilities and systems in a cost-effective manner, and in a manner that satisfies customer expectations for quality and coverage, could have an adverse effect on U.S. Cellular's business, business prospects, financial condition or results of operations.

**21. Difficulties involving third parties with which U.S. Cellular does business, including changes in U.S. Cellular's relationships with or financial or operational difficulties of key suppliers or independent agents and third party national retailers who market U.S. Cellular's services, could adversely affect U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular has relationships with independent agents and third party national retailers who market U.S. Cellular services. If such relationships are seriously harmed or if such parties experience financial difficulties, including bankruptcy, U.S. Cellular's business, financial condition or results of operations could be adversely affected.

U.S. Cellular depends upon certain vendors to provide it with equipment (including wireless devices), services or content to continue its network construction and upgrades and to operate its business. U.S. Cellular does not have operational or financial control over such key suppliers and has limited influence with respect to the manner in which these key suppliers conduct their businesses. If these key suppliers experience financial difficulties or file for bankruptcy or experience other operational difficulties, they may be unable to provide equipment, services or content to U.S. Cellular on a timely basis, or at all, or they may otherwise fail to honor their obligations to U.S. Cellular.

Regulations regarding the use of "conflict minerals" mined from the Democratic Republic of Congo and adjoining countries may affect some of U.S. Cellular's suppliers. These regulations may limit the availability of conflict free minerals and, as a result, U.S. Cellular may not be able to obtain products in sufficient quantities or at competitive prices from its vendors who utilize such minerals in the manufacture of products. In such cases, U.S. Cellular may be unable to maintain and upgrade its network or provide products and services to its customers in a competitive manner, or could suffer other disruptions to its business. In that event, U.S. Cellular's business, financial condition or results of operations could be adversely affected.

In addition, operation of U.S. Cellular's supply chain and management of its inventory require accurate forecasting of customer growth and demand, which has become increasingly challenging. If overall demand for wireless devices or the mix of demand for wireless devices is significantly different than U.S. Cellular's expectations, U.S. Cellular could face inadequate or excess supplies of particular models of wireless devices. This could result in lost sales opportunities or an excess supply of inventory. Either of these situations could adversely affect U.S. Cellular's revenues, costs of doing business, results of operations or financial condition.

Also, U.S. Cellular has other arrangements with third parties, including arrangements pursuant to which U.S. Cellular now outsources certain support functions to third party vendors. Operational problems associated with such functions, including any failure by the vendor to provide the required level of service under the outsourcing arrangements, could have adverse effects on U.S. Cellular's business, financial condition or results of operations.

**22. U.S. Cellular has significant investments in entities that it does not control. Losses in the value of such investments could have an adverse effect on U.S. Cellular's financial condition or results of operations.**

U.S. Cellular has significant investments in entities that it does not control, including equity investments and interests in certain variable interest entities. U.S. Cellular's interests in such entities do not provide U.S. Cellular with control over the business strategy, financial goals, network build-out plans or other operational aspects of these entities. U.S. Cellular cannot provide assurance that these entities will operate in a manner that will increase or maintain the value of U.S. Cellular's investments, that U.S. Cellular's proportionate share of income from these investments will continue at the current level in the future or that U.S. Cellular will not incur losses from the holding of such investments. Losses in the values of such investments or a reduction in income from these investments could adversely affect U.S. Cellular's financial condition or results of operations. In addition, certain investments have historically contributed significant cash flows to U.S. Cellular and a reduction or suspension of such cash flows could adversely affect U.S. Cellular's financial condition.



Table of Contents**23. A failure by U.S. Cellular to maintain flexible and capable telecommunication networks or information technology, or a material disruption thereof, could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular relies extensively on its telecommunication networks and information technology to operate and manage its business, process transactions and summarize and report results. These networks and technology become obsolete over time and must be upgraded, replaced and/or otherwise enhanced over time. Enhancements must be more flexible and dependable than ever before. All of this is capital intensive and challenging. A failure by U.S. Cellular to maintain flexible and capable telecommunication networks or information technology could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.

The increased provision of data services has introduced significant new demands on U.S. Cellular's network and also has increased complexities related to network management. Further, the increased provision of data services on U.S. Cellular's networks has created an increased level of risk related to quality of service. This is due to the fact that many customers increasingly rely on data communications to execute and validate transactions. As a result, redundancy and geographical diversity of U.S. Cellular's network facilities are critical to providing uninterrupted service. Also, the speed of repair and maintenance procedures in the event of network interruptions is critical to maintaining customer satisfaction. U.S. Cellular's ability to maintain high-quality, uninterrupted service to its customers is critical, particularly given the increasingly competitive environment and customers' ability to choose other service providers.

In addition, U.S. Cellular's networks and information technology and the networks and information technology of vendors on which U.S. Cellular relies are subject to damage or interruption due to various events, including power outages, computer, network and telecommunications failures, computer viruses, security breaches, hackers and other cyber security risks, catastrophic events, natural disasters, errors or unauthorized actions by employees and vendors, flawed conversion of systems, disruptive technologies and technology changes.

**24. U.S. Cellular has experienced and, in the future, expects to experience cyber-attacks or other breaches of network or information technology security of varying degrees on a regular basis, which could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular experiences cyber-attacks of varying degrees on a regular basis. U.S. Cellular maintains administrative, technical and physical controls, as well as other preventative actions, to reduce the risk of security breaches. Although to date U.S. Cellular has not experienced a material security breach, these efforts may be insufficient to prevent a security breach stemming from future cyber-attacks. If U.S. Cellular's or its vendors' networks and information technology are not adequately adapted to changes in technology or are damaged or fail to function properly, and/or if U.S. Cellular's or its vendors' security is breached or otherwise compromised, U.S. Cellular could suffer adverse consequences, including theft, destruction or other loss of critical and private data, including customer and/or employee data, interruptions or delays in its operations, inaccurate billings, inaccurate financial reporting, and significant costs to remedy the problems. If U.S. Cellular's or its vendors' systems become unavailable or suffer a security breach of customer or other data, U.S. Cellular may be required to expend significant resources and take various actions to address the problems, including notification under data privacy laws and regulations, may be subject to fines, sanctions and litigation, and its reputation and operating results could be adversely affected. Any material disruption in U.S. Cellular's networks or information technology, including security breaches, could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.

**25. The market price of U.S. Cellular's Common Shares is subject to fluctuations due to a variety of factors.**

Factors that may affect the future market price of U.S. Cellular's Common Shares include:

- General economic conditions, including conditions in the credit and financial markets;
- Industry conditions;
- Fluctuations in U.S. Cellular's quarterly customer additions, churn rate, revenues, results of operations or cash flows;
- Variations between U.S. Cellular's actual financial and operating results and those expected by analysts and investors; and
- Announcements by U.S. Cellular's competitors.

Any of these or other factors could adversely affect the future market price of U.S. Cellular's Common Shares, or could cause the future market price of U.S. Cellular's Common Shares to fluctuate from time to time.

**26. Changes in facts or circumstances, including new or additional information, could require U.S. Cellular to record charges in excess of amounts accrued in the financial statements, which could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

The preparation of financial statements requires U.S. Cellular to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. U.S. Cellular bases its estimates on historical experience and on various other assumptions and information that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results may differ from estimates under different assumptions or conditions. Changes in facts or circumstances, including new or additional information, could require U.S. Cellular to record charges in excess of amounts accrued in the financial statements, if any, which could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.



Table of Contents

**27. Disruption in credit or other financial markets, a deterioration of U.S. or global economic conditions or other events could, among other things, impede U.S. Cellular's 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 U.S. Cellular's business, financial condition or results of operations.**

Disruptions in the credit and financial markets, declines in consumer confidence, increases in unemployment, declines in economic growth and uncertainty about corporate earnings could have a significant negative impact on the U.S. and global financial and credit markets and the overall economy. Such events could have an adverse impact on financial institutions resulting in limited access to capital and credit for many companies. Furthermore, economic uncertainties make it very difficult to accurately forecast and plan future business activities. Changes in economic conditions, changes in financial markets, deterioration in the capital markets or other factors could have an adverse effect on U.S. Cellular's business, financial condition, revenues, results of operations and cash flows.

**28. 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 U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular is regularly involved in a number of legal and policy proceedings before the FCC and various state and federal courts. Such legal and policy proceedings can be complex, costly, protracted and highly disruptive to business operations by diverting the attention and energies of management and other key personnel.

The assessment of legal and policy proceedings is a highly subjective process that requires judgments about future events. Additionally, amounts ultimately received or paid upon settlement or resolution of litigation and other contingencies may differ materially from amounts accrued in the financial statements. Depending on a range of factors, these or similar proceedings could impose restraints on U.S. Cellular's current or future manner of doing business. Such potential outcomes could have an adverse effect on U.S. Cellular's financial condition, results of operations or ability to do business.

**29. 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 U.S. Cellular's business, financial condition or results of operations.**

Media reports and certain professional studies have suggested that certain radio frequency emissions from wireless devices may be linked to various health problems, including cancer or tumors, and may interfere with various electronic medical devices, including hearing aids and pacemakers. U.S. Cellular is a party to and may in the future be a party to lawsuits against wireless carriers and other parties claiming damages for alleged health effects, including cancer or tumors, arising from wireless phones or radio frequency transmitters. Concerns over radio frequency emissions may discourage use of wireless devices or expose U.S. Cellular to potential litigation. In addition, the FCC or other regulatory authorities may adopt regulations in response to concerns about radio frequency emissions. Any resulting decrease in demand for wireless services, costs of litigation and damage awards or regulation could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.

In addition, some studies have indicated that some aspects of using wireless devices while driving may impair drivers' attention in certain circumstances, making accidents more likely. These concerns could lead to potential litigation relating to accidents, deaths or serious bodily injuries, any of which could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.

Numerous state and local legislative bodies have enacted or proposed legislation restricting or prohibiting the use of wireless devices while driving motor vehicles. These enacted or proposed laws or other similar laws, if passed, could have the effect of reducing customer usage and/or increasing costs, which could have an adverse effect on U.S. Cellular's business, financial condition, or results of operations.

Table of Contents

**30. Claims of infringement of intellectual property and proprietary rights of others, primarily involving patent infringement claims, could prevent U.S. Cellular from using necessary technology to provide products or services or subject U.S. Cellular to expensive intellectual property litigation or monetary penalties, which could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.**

U.S. Cellular faces possible effects of industry litigation relating to patents, other intellectual property or otherwise, that may restrict U.S. Cellular's access to devices for sale to customers. If technology that U.S. Cellular uses in products or services were determined by a court to infringe a patent or other intellectual property right held by another person, U.S. Cellular could be precluded from using that technology and could be required to pay significant monetary damages. U.S. Cellular also may be required to pay significant royalties to such person to continue to use such technology in the future. The successful enforcement of any intellectual property rights, or U.S. Cellular's inability to negotiate a license for such rights on acceptable terms, could force U.S. Cellular to cease using the relevant technology and offering services incorporating the technology. Any litigation to determine the validity of claims that U.S. Cellular's products or services infringe or may infringe intellectual property rights of another, regardless of their merit or resolution, could be costly and divert the effort and attention of U.S. Cellular's management and technical personnel. Regardless of the merits of any specific claim, U.S. Cellular cannot give assurance that it would prevail in litigation because of the complex technical issues and inherent uncertainties in intellectual property litigation. Although U.S. Cellular generally seeks to obtain indemnification agreements from vendors that provide it with technology, there can be no assurance that any claim of infringement will be covered by an indemnity or that U.S. Cellular will be able to recover all or any of its losses and costs under any available indemnity agreements. Any claims of infringement of intellectual property and proprietary rights of others could prevent U.S. Cellular from using necessary technology to provide its services or subject U.S. Cellular to expensive intellectual property litigation or monetary penalties, which could have an adverse effect on U.S. Cellular's business, financial condition or results of operations.

**31. There are potential conflicts of interests between TDS and U.S. Cellular.**

TDS owns over 80% of the combined total of both classes of common stock of U.S. Cellular, including a majority of the outstanding Common Shares and 100% of the Series A Common Shares, and controls over 96% of their combined voting power. As a result, TDS is effectively able to elect all of U.S. Cellular's fourteen directors and otherwise control the management and operations of U.S. Cellular. Seven of the fourteen directors of U.S. Cellular are also directors of TDS and/or executive officers of TDS and/or U.S. Cellular. Directors and officers of TDS who are also directors or officers of U.S. Cellular, and TDS as U.S. Cellular's controlling shareholder, are in positions involving the possibility of conflicts of interest with respect to certain transactions concerning U.S. Cellular. When the interests of TDS and U.S. Cellular diverge, TDS may exercise its influence in its own best interests.

U.S. Cellular and TDS have entered into contractual arrangements governing certain transactions and relationships between them. These agreements were executed prior to the initial public offering of U.S. Cellular's Common Shares and were not the result of arm's-length negotiations. Accordingly, there is no assurance that the terms and conditions of these agreements are as favorable to U.S. Cellular as could have been obtained from unaffiliated third parties. See "Certain Relationships and Related Transactions" in this Form 10-K.

Conflicts of interest may arise between TDS and U.S. Cellular when faced with decisions that could have different implications for U.S. Cellular and TDS, including technology decisions, financial budgets, the payment of distributions by U.S. Cellular, agreements or transactions between TDS and U.S. Cellular, business activities and other matters. TDS also may take action that favors its other businesses and the interests of its shareholders over U.S. Cellular's wireless business and the interests of U.S. Cellular shareholders and debt holders. Because TDS controls U.S. Cellular, conflicts of interest could be resolved in a manner adverse to U.S. Cellular and its other shareholders or its debt holders.

The U.S. Cellular Restated Certificate of Incorporation provides that, so long as not less than 500,000 Series A Common Shares are outstanding, U.S. Cellular, without the written consent of TDS, shall not, directly or indirectly own, invest or otherwise have an interest in, lease, operate or manage any business other than a business engaged solely in the construction of, the ownership of interests in and/or the management of wireless telephone systems. This limitation on the scope of U.S. Cellular's potential business could hurt the growth of U.S. Cellular's business. This restriction would preclude U.S. Cellular from pursuing attractive related or unrelated business opportunities unless TDS consents in writing. TDS has no obligation to consent to any business opportunities proposed by U.S. Cellular and may withhold its consent in its own best interests.

**32. Certain matters, such as control by TDS and provisions in the U.S. Cellular Restated Certificate of Incorporation, may serve to discourage or make more difficult a change in control of U.S. Cellular.**

The control of U.S. Cellular by TDS may tend to deter non-negotiated tender offers or other efforts to obtain control of U.S. Cellular and thereby deprive shareholders of opportunities to sell shares at prices higher than those prevailing in the market.

The U.S. Cellular Restated Certificate of Incorporation also contains provisions which may serve to discourage or make more difficult a change in control of U.S. Cellular without the support of TDS or without meeting various other conditions. In particular, the authorization of multiple classes of capital stock with different voting rights could prevent shareholders from profiting from an increase in the market value of their shares as a result of a change in control of U.S. Cellular by delaying or preventing such change in control.

The U.S. Cellular Restated Certificate of Incorporation also authorizes the U.S. Cellular Board of Directors to designate and issue Preferred Shares in one or more classes or series from time to time. Generally, no further action or authorization by the shareholders is necessary prior to the designation or issuance of the additional Preferred Shares authorized pursuant to the U.S. Cellular Restated Certificate of Incorporation unless applicable laws or regulations would require such approval in a given instance. Such Preferred Shares could be issued in circumstances that would serve to preserve TDS' control of U.S. Cellular.

Table of Contents**33. 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 U.S. Cellular's forward-looking estimates by a material amount.**

From time to time, U.S. Cellular may disclose forward-looking information, including estimates of future operating revenues; various measures of income before income taxes; and/or capital expenditures. Any such forward-looking information includes consideration of known or anticipated changes to the extent disclosed, but dynamic market conditions and/or other unknown or unanticipated events, including but not limited to the risks discussed above, could cause such estimates to differ materially from the actual amounts.

[Table of Contents](#)

## Item 1B. Unresolved Staff Comments

None.

## Item 2. Properties

U.S. Cellular has properties located throughout the United States. U.S. Cellular's mobile telephone switching offices, cell sites, call centers and retail stores are located primarily in U.S. Cellular's operating markets and are either owned or leased by U.S. Cellular, one of its subsidiaries, or the partnership, limited liability company or corporation which holds the license issued by the FCC.

As of December 31, 2016, U.S. Cellular's Property, plant and equipment, net of accumulated depreciation, totaled \$2,470 million.

U.S. Cellular considers the properties owned or leased by it and its subsidiaries to be maintained in good operating condition and suitable and adequate for its business operations.

## Item 3. Legal Proceedings

U.S. Cellular is involved or may be involved from time to time in legal proceedings before the FCC, other regulatory authorities, and/or various state and federal courts. If U.S. Cellular believes that a loss arising from such legal proceedings is probable and can be reasonably estimated, an amount is accrued in the financial statements for the estimated loss. If only a range of loss can be determined, the best estimate within that range is accrued; if none of the estimates within that range is better than another, the low end of the range is accrued. The assessment of the expected outcomes of legal proceedings is a highly subjective process that requires judgments about future events. The legal proceedings are reviewed at least quarterly to determine the adequacy of accruals and related financial statement disclosures. The ultimate outcomes of legal proceedings could differ materially from amounts accrued in the financial statements. See Note 12 --- Commitments and Contingencies in the Notes to Consolidated Financial Statements for further information.

## Item 4. Mine Safety Disclosures

Not applicable.

[Table of Contents](#)**PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

Market, holder, dividend and performance graph information is incorporated by reference from Exhibit 13 to this Form 10-K, Annual Report sections entitled "Shareholder Information" and "Consolidated Quarterly Information (Unaudited)."

U.S. Cellular has not paid any cash dividends in recent periods and currently intends to retain all earnings for use in U.S. Cellular's business.

Information relating to Issuer Purchases of Equity Securities is set forth below.

In November 2009, U.S. Cellular announced by Form 8-K that 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. In December 2016, the U.S. Cellular Board amended this authorization to provide that such amount will be any amount from zero to 1,300,000 beginning on January 1, 2017, as determined by the Pricing Committee, and that if the Pricing Committee did not specify an amount for any year, such amount would be zero for such year. The Pricing Committee did not specify any increase as of January 1, 2017. The Pricing Committee was also authorized to decrease the cumulative amount of the authorization at any time, but has not taken any action to do so at this time. As a result, there was no change to the cumulative amount of the share repurchase authorization as of January 1, 2017. The authorization provides that share repurchases 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. U.S. Cellular did not determine to terminate the foregoing Common Share repurchase program, as amended, or cease making further purchases thereunder, during the fourth quarter of 2016.

The following table provides certain information with respect to all purchases made by or on behalf of U.S. Cellular, and any open market purchases made by any "affiliated purchaser" (as defined by the SEC) of U.S. Cellular, of U.S. Cellular Common Shares during the fourth quarter of 2016.

Period	Total Number of Common Shares Purchased	Average Price Paid per Common Share	Total Number of Common Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Common Shares that May Yet Be Purchased Under the Plans or Programs
October 1 – 31, 2016	4,135	\$ 35.01	4,135	6,004,302
November 1 – 30, 2016	103,453	34.43	103,453	5,900,849
December 1 – 31, 2016	—	—	—	5,900,849
Total as of or for the quarter ended December 31, 2016	107,588	\$ 34.45	107,588	5,900,849

Table of Contents**Item 6. Selected Financial Data**

Incorporated by reference from Exhibit 13 to this Form 10-K, Annual Report section entitled "Selected Consolidated Financial Data," except for Ratio of earnings to fixed charges, which is incorporated herein by reference from Exhibit 12 to this Form 10-K.

**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

Incorporated by reference from Exhibit 13 to this Form 10-K, Annual Report section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations."

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

Incorporated by reference from Exhibit 13 to this Form 10-K, Annual Report section entitled "Market Risk."

**Item 8. Financial Statements and Supplementary Data**

Incorporated by reference from Exhibit 13 to this Form 10-K, Annual Report sections entitled "Consolidated Statement of Operations," "Consolidated Statement of Cash Flows," "Consolidated Balance Sheet," "Consolidated Statement of Changes in Equity," "Notes to Consolidated Financial Statements," "Management's Report on Internal Control Over Financial Reporting," "Report of Independent Registered Public Accounting Firm," and "Consolidated Quarterly Information (Unaudited)." The Consolidated Statement of Comprehensive Income was not included because comprehensive income for the years ended December 31, 2016, 2015 and 2014 equaled net income.

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

Table of Contents

## Item 9A. Controls and Procedures

### Evaluation of Disclosure Controls and Procedures

U.S. Cellular maintains disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under 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 SEC's rules and forms, and that such information is accumulated and communicated to U.S. Cellular's 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), U.S. Cellular 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 U.S. Cellular's disclosure controls and procedures as of the end of the period covered by this Annual Report. Based on this evaluation, the principal executive officer and principal financial officer have concluded that U.S. Cellular's disclosure controls and procedures were effective as of December 31, 2016, at the reasonable assurance level.

### Management's Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. U.S. Cellular's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America ("GAAP"). U.S. Cellular's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and, where required, the board of directors of the issuer; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the issuer's assets that could have a material effect on the interim or annual consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of U.S. Cellular's management, including its principal executive officer and principal financial officer, U.S. Cellular conducted an evaluation of the effectiveness of its internal control over financial reporting as of December 31, 2016, based on the criteria established in the 2013 version of *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Management has concluded that U.S. Cellular maintained effective internal control over financial reporting as of December 31, 2016 based on criteria established in the 2013 version of *Internal Control — Integrated Framework* issued by the COSO.

The effectiveness of U.S. Cellular's internal control over financial reporting as of December 31, 2016 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in the firm's report which is incorporated by reference into Item 8 of this Annual Report on Form 10-K from Exhibit 13 filed herewith.

### Changes in Internal Control over Financial Reporting

There were no changes in U.S. Cellular's internal control over financial reporting during the fourth quarter of 2016 that have materially affected, or are reasonably likely to materially affect, U.S. Cellular's internal control over financial reporting.

## Item 9B. Other Information

None.

[Table of Contents](#)

## **PART III**

### **Item 10. Directors, Executive Officers and Corporate Governance**

Incorporated by reference from Proxy Statement sections entitled "Election of Directors," "Corporate Governance," "Executive Officers" and "Section 16(a) Beneficial Ownership Reporting Compliance."

### **Item 11. Executive Compensation**

Incorporated by reference from Proxy Statement section entitled "Executive and Director Compensation."

### **Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

Incorporated by reference from Proxy Statement sections entitled "Security Ownership of Certain Beneficial Owners and Management" and "Securities Authorized for Issuance under Equity Compensation Plans."

### **Item 13. Certain Relationships and Related Transactions, and Director Independence**

Incorporated by reference from Proxy Statement sections entitled "Corporate Governance" and "Certain Relationships and Related Transactions."

### **Item 14. Principal Accountant Fees and Services**

Incorporated by reference from Proxy Statement section entitled "Fees Paid to Principal Accountants."

Table of Contents**PART IV****Item 15. Exhibits and Financial Statement Schedules**

(a) The following documents are filed as part of this report:

(1) Financial Statements

Consolidated Statement of Operations	Annual Report*
Consolidated Statement of Cash Flows	Annual Report*
Consolidated Balance Sheet	Annual Report*
Consolidated Statement of Changes in Equity	Annual Report*
Notes to Consolidated Financial Statements	Annual Report*
Management's Report on Internal Control Over Financial Reporting	Annual Report*
Report of Independent Registered Public Accounting Firm — PricewaterhouseCoopers LLP	Annual Report*
Consolidated Quarterly Information (Unaudited)	Annual Report*

\*Incorporated by reference from Exhibit 13.

(2) Financial Statement Schedules

	<u>Location</u>
Los Angeles SMSA Limited Partnership and Subsidiary Financial Statements	S-1
Report of Independent Registered Public Accounting Firm — Ernst & Young LLP	S-2
Consolidated Balance Sheets	S-3
Consolidated Statements of Income and Comprehensive Income	S-4
Consolidated Statements of Changes in Partners' Capital	S-5
Consolidated Statements of Cash Flows	S-6
Notes to Consolidated Financial Statements	S-7

All other schedules have been omitted because they are not applicable or not required or because the required information is shown in the financial statements or notes thereto.

(3) Exhibits

The exhibits set forth in the accompanying Index to Exhibits are filed as a part of this Report. Compensatory plans or arrangements are identified in the Index to Exhibits with an asterisk.

**Item 16. Form 10-K Summary**

None.

[Table of Contents](#)

## **LOS ANGELES SMSA LIMITED PARTNERSHIP AND SUBSIDIARY FINANCIAL STATEMENTS**

U.S. Cellular owns a 5.5% limited partnership interest in the Los Angeles SMSA Limited Partnership and accounts for such interest by the equity method. The partnership's consolidated financial statements were obtained by U.S. Cellular as a limited partner.

---

S-1

Table of Contents

## Report of Independent Registered Public Accounting Firm

## The Partners of Los Angeles SMSA Limited Partnership

We have audited the accompanying consolidated balance sheets of Los Angeles SMSA Limited Partnership and Subsidiary (the Partnership) as of December 31, 2016 and 2015, and the related consolidated statements of income and comprehensive income, changes in partners' capital and cash flows for each of the three years in the period ended December 31, 2016. These financial statements are the responsibility of the Partnership's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our December 31, 2016 audit in accordance with the standards of the Public Company Accounting Oversight Board (United States) and in accordance with auditing standards generally accepted in the United States of America. We conducted our December 31, 2015 and 2014 audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Partnership at December 31, 2016 and 2015, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

/s/ Ernst & Young LLP  
Certified Public Accountants

Orlando, Florida  
February 22, 2017

Table of Contents**Los Angeles SMSA Partnership and Subsidiary**

Consolidated Balance Sheets - As of December 31, 2016 and 2015

(Dollars in Thousands)

	2016	2015
<b>ASSETS</b>		
CURRENT ASSETS:		
Due from affiliate	\$ 281,846	\$ -
Accounts receivable, net of allowances of \$31,093 and \$37,090	489,043	407,622
Unbilled revenue	23,190	22,883
Prepaid expenses	18,716	11,785
Total current assets	<u>812,795</u>	<u>442,290</u>
PROPERTY, PLANT AND EQUIPMENT - NET	1,862,892	1,804,877
WIRELESS LICENSES	2,075,448	2,073,751
OTHER ASSETS	<u>228,770</u>	<u>252,751</u>
TOTAL ASSETS	<u>\$ 4,979,905</u>	<u>\$ 4,573,669</u>
<b>LIABILITIES AND PARTNERS' CAPITAL</b>		
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	\$ 202,284	\$ 190,807
Advance billings and other	160,434	166,533
Financing obligation	12,744	12,494
Deferred rent	8,382	8,382
Due to affiliate	-	348,724
Total current liabilities	<u>383,844</u>	<u>726,940</u>
LONG TERM LIABILITIES:		
Financing obligation	112,552	113,016
Deferred rent	146,547	150,557
Other liabilities	158	117
Total long term liabilities	<u>259,257</u>	<u>263,690</u>
Total liabilities	643,101	990,630
PARTNERS' CAPITAL		
General Partner's interest	1,734,722	1,433,215
Limited Partners' interest	<u>2,602,082</u>	<u>2,149,824</u>
Total partners' capital	<u>4,336,804</u>	<u>3,583,039</u>
TOTAL LIABILITIES AND PARTNERS' CAPITAL	<u>\$ 4,979,905</u>	<u>\$ 4,573,669</u>

See notes to consolidated financial statements.

Table of Contents**Los Angeles SMSA Limited Partnership and Subsidiary**

Consolidated Statements of Income and Comprehensive Income - For the Years Ended December 31, 2016, 2015 and 2014

(Dollars in Thousands)	2016	2015	2014
<b>OPERATING REVENUES:</b>			
Service revenues	\$ 3,996,989	\$ 4,181,377	\$ 4,317,377
Equipment revenues	930,690	943,419	650,130
Other	256,917	221,918	201,427
Total operating revenues	<u>5,184,596</u>	<u>5,346,714</u>	<u>5,168,934</u>
<b>OPERATING EXPENSES:</b>			
Cost of service (exclusive of depreciation and amortization)	1,070,302	968,132	863,031
Cost of equipment	1,193,924	1,267,801	1,195,874
Depreciation and amortization	356,848	360,463	344,887
Selling, general and administrative	1,278,205	1,397,856	1,470,669
Total operating expenses	<u>3,899,279</u>	<u>3,994,252</u>	<u>3,874,461</u>
<b>OPERATING INCOME</b>	<u>1,285,317</u>	<u>1,352,462</u>	<u>1,294,473</u>
<b>INTEREST (EXPENSE) INCOME, NET</b>	(6,552)	(3,197)	4,199
<b>NET INCOME AND COMPREHENSIVE INCOME</b>	<u>\$ 1,278,765</u>	<u>\$ 1,349,265</u>	<u>\$ 1,298,672</u>
Allocation of Net Income:			
General Partner	\$ 511,507	\$ 539,706	\$ 519,468
Limited Partners	\$ 767,258	\$ 809,559	\$ 779,204

See notes to consolidated financial statements.

Table of Contents**Los Angeles SMSA Limited Partnership and Subsidiary**

Consolidated Statements of Changes in Partners' Capital - For the Years Ended December 31, 2016, 2015 and 2014

(Dollars in Thousands)

	General Partner	Limited Partners			Total Partners' Capital
	AirTouch Cellular Inc.	AirTouch Cellular Inc.	Cellico Partnership	United States Cellular Investment Corporation of Los Angeles	
BALANCE - January 1, 2014	\$ 814,041	\$ 860,848	\$ 248,282	\$ 111,931	\$ 2,035,102
Distributions	(440,000)	(465,300)	(134,200)	(60,500)	(1,100,000)
Net Income	519,468	549,338	158,438	71,428	1,298,672
BALANCE - December 31, 2014	\$ 893,509	\$ 944,886	\$ 272,520	\$ 122,859	\$ 2,233,774
Net Income	539,706	570,740	164,611	74,208	1,349,265
BALANCE - December 31, 2015	\$ 1,433,215	\$ 1,515,626	\$ 437,131	\$ 197,067	\$ 3,583,039
Distributions	(210,000)	(222,075)	(64,050)	(28,875)	(525,000)
Net Income	511,507	540,917	156,009	70,332	1,278,765
BALANCE - December 31, 2016	\$ 1,734,722	\$ 1,834,468	\$ 529,090	\$ 238,524	\$ 4,336,804

See notes to consolidated financial statements.

Table of Contents**Los Angeles SMSA Limited Partnership and Subsidiary**

Consolidated Statements of Cash Flows - For the Years Ended December 31, 2016, 2015 and 2014

(Dollars in Thousands)	2016	2015	2014
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net Income	\$ 1,278,765	\$ 1,349,265	\$ 1,298,672
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	356,848	360,463	344,887
Imputed interest on financing obligation	12,284	9,135	-
Provision for losses on accounts receivable	71,925	79,063	34,370
Gain on device installment plan receivables sold	-	(7,632)	-
Changes in certain assets and liabilities:			
Accounts receivable	(153,704)	42,964	(200,950)
Unbilled revenue	(307)	1,628	(4,441)
Prepaid expenses	(6,931)	1,403	(8,831)
Other assets	20,037	(151,954)	(91,809)
Accounts payable and accrued liabilities	24,685	24,105	32,591
Advance billings and other	(6,099)	(31,182)	45,017
Deferred rent	(4,010)	88,115	(4,942)
Other liabilities	41	4,046	3,610
Net cash provided by operating activities	<u>1,593,534</u>	<u>1,769,419</u>	<u>1,448,174</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Capital expenditures	(449,005)	(470,954)	(487,511)
Fixed asset transfers out	23,453	25,371	27,816
Acquisition of wireless licenses (including capitalized interest)	(1,697)	(1,994,208)	-
Collections on deferred purchase price	1,783	-	-
Change in due from affiliate	(281,846)	(583,060)	111,521
Net cash used in investing activities	<u>(707,312)</u>	<u>(3,022,851)</u>	<u>(348,174)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Change in due to affiliate	(348,724)	1,137,057	-
Proceeds from financing obligation	-	126,635	-
Repayments of financing obligation	(12,498)	(10,260)	-
Distributions	(525,000)	-	(1,100,000)
Net cash (used in) provided by financing activities	<u>(886,222)</u>	<u>1,253,432</u>	<u>(1,100,000)</u>
CHANGE IN CASH	-	-	-
CASH - Beginning of year	-	-	-
CASH - End of year	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
CASH PAID FOR INTEREST	<u>\$ 2,576</u>	<u>\$ 24,269</u>	<u>\$ -</u>
<b>NONCASH TRANSACTIONS FROM INVESTING ACTIVITIES:</b>			
Accruals for capital expenditures	<u>\$ 15,621</u>	<u>\$ 28,829</u>	<u>\$ 31,019</u>

See notes to consolidated financial statements.



Table of Contents**Los Angeles SMSA Limited Partnership and Subsidiary**

Notes to Consolidated Financial Statements – For the Years Ended December 31, 2016, 2015 and 2014.

(Dollars in Thousands)

**1. ORGANIZATION AND MANAGEMENT**

The Consolidated Financial Statements include the accounts of the Los Angeles SMSA Limited Partnership ("Los Angeles SMSA") and Los Angeles Edge LLC, a wholly owned subsidiary of Los Angeles SMSA (collectively, the "Partnership"). The principal activity of Los Angeles SMSA, formed in 1984, is to provide cellular service in the Los Angeles metropolitan service area. Los Angeles Edge LLC was formed during 2015 and is a bankruptcy remote special purpose entity, created for the purpose of selling wireless device payment plan receivables to third parties (see Note 3).

In accordance with the partnership agreement, AirTouch Cellular Inc. an indirect wholly owned subsidiary of Cellco Partnership ("Cellco"), doing business as Verizon Wireless, and general partner of the Partnership is responsible for managing the operations of the Partnership (see Note 8).

The partners and their respective ownership percentages of the Partnership as of December 31, 2016, 2015 and 2014 are as follows:

## General Partner:

AirTouch Cellular Inc.	40.0%
------------------------	-------

## Limited Partners:

AirTouch Cellular Inc.	42.3%
Cellco Partnership	12.2%
United States Cellular Investment Corporation of Los Angeles	5.5%

**2. SIGNIFICANT ACCOUNTING POLICIES**

**Consolidation** – The method of accounting applied to consolidated investments involves an evaluation of all significant terms of the investments that explicitly grant or suggest evidence of control or influence over the operations of the investee. The consolidated financial statements include our subsidiary which is a variable interest entity (VIE) where Los Angeles SMSA is deemed to be the primary beneficiary. All significant intercompany accounts and transactions have been eliminated (see Note 3).

**Use of estimates** – The financial statements are prepared using U.S. generally accepted accounting principles (GAAP), which requires management to make estimates and assumptions that affect reported amounts and disclosures. Actual results could differ from those estimates.

Examples of significant estimates include: the allowance for doubtful accounts, the recoverability of property, plant and equipment, the recoverability of intangible assets and other long-lived assets, unbilled revenues, fair values of financial instruments, deferred purchase price, beneficial interest, accrued expenses and contingencies.

**Revenue recognition** – The Partnership offers products and services to customers through bundled arrangements. These arrangements involve multiple deliverables which may include products, services, or a combination of products and services.

The Partnership earns revenue primarily by providing access to and usage of its network as well as the sale of equipment. In general, access revenue is billed one month in advance and recognized when earned. Usage revenue is generally billed in arrears and recognized when service is rendered. Equipment revenue associated with the sale of wireless devices and accessories is generally recognized when the products are delivered to and accepted by the customer, as equipment sales is considered to be a separate earnings process from providing wireless services. For agreements involving the resale of third-party services in which the Partnership is considered the primary obligor in the arrangements, the revenue is recorded gross at the time of sale.

Under the Verizon device payment program, eligible wireless customers purchase wireless devices under a device payment plan agreement. On select devices, certain marketing promotions have been revocably offered to customers to upgrade to a new device after paying down a certain specified portion of the required device payment plan agreement amount as well as trading in their device in good working order. When a customer enters into a device payment plan agreement with the right to upgrade to a new device, the Partnership accounts for this trade-in right as a guarantee obligation. The full amount of the trade-in right's fair value (not an allocated value) is recognized as a guarantee liability and the remaining allocable consideration is allocated to the device. The value of the guarantee liability effectively results in a reduction to the revenue recognized for the sale of the device. The Partnership may offer customers certain promotions where a customer can trade-in his or her owned device in connection with the purchase of a new device. Under these types of promotions, the customer will receive trade-in credits that are applied to the customer's monthly bill. As a result, the Partnership recognizes a trade-in obligation measured at fair value using weighted-average selling prices obtained in recent resales of devices eligible for trade-in.



Table of Contents

In multiple element arrangements that bundle devices and monthly wireless service, revenue is allocated to each unit of accounting using a relative selling price method. At the inception of the arrangement, the amount allocable to the delivered units of accounting is limited to the amount that is not contingent upon the delivery of the monthly wireless service (the noncontingent amount). The Partnership effectively recognizes revenue on the delivered device at the lesser of the amount allocated based on the relative selling price of the device or the noncontingent amount owed when the device is sold.

Roaming revenue reflects service revenue earned by the Partnership when customers not associated with the Partnership operate in the service area of the Partnership and use the Partnership's network. The roaming rates with third party carriers associated with those customers are based on agreements with such carriers. The roaming rates charged by the Partnership to Cellco are established by Cellco on a periodic basis and may not reflect current market rates (see Note 8).

Other revenues primarily consist of certain fees billed to customers for surcharges and elected services as well as non-customer related revenues. The Partnership reports taxes imposed by governmental authorities on revenue producing transactions between the Partnership and its customers which is passed through to the customers on a net basis. Other revenues also include switch revenue. This revenue represents revenue earned by the Partnership for switch services provided to other Cellco owned entities by the Partnership. The switch revenue rates charged by the Partnership to Cellco are established by Cellco on a periodic basis and may not reflect current market rates (see Note 8).

**Operating expenses** – Operating expenses include expenses incurred directly by the Partnership, as well as an allocation of selling, general and administrative, and operating costs incurred by Cellco or its affiliates on behalf of the Partnership. Employees of Cellco provide services on behalf of the Partnership. These employees are not employees of the Partnership, therefore operating expenses include direct and allocated charges of salary and employee benefit costs for the services provided to the Partnership. Cellco believes such allocations, principally based on the Partnership's percentage of certain revenue streams, total customers, customer gross additions or minutes-of-use, are calculated in accordance with the Partnership agreement and are a reasonable method of allocating such costs (see Note 8).

Cost of roaming reflects costs incurred by the Partnership when customers associated with the Partnership operate in a service area not associated with the Partnership and use a network not associated with the Partnership. The roaming rates with third party carriers are based on agreements with such carriers. The roaming rates charged to the Partnership by Cellco are established by Cellco on a periodic basis and may not reflect current market rates (see Note 8).

Cost of equipment is recorded upon sale of the related equipment at Cellco's cost basis. Inventory is wholly owned by Cellco and is not recorded in the financial statements of the Partnership.

**Maintenance and repairs** – The cost of maintenance and repairs, including the cost of replacing minor items not constituting substantial betterments, is charged principally to Cost of service as these costs are incurred.

**Advertising costs** – Costs for advertising products and services as well as other promotional and sponsorship costs are charged to Selling, general and administrative expense in the periods in which they are incurred.

**Comprehensive income** – Comprehensive income is the same as net income as presented in the accompanying statements of income and comprehensive income.

**Income taxes** – The Partnership is treated as a pass through entity for income tax purposes and, therefore, is not subject to federal, state or local income taxes. Accordingly, no provision has been recorded for income taxes in the Partnership's financial statements. The results of operations, including taxable income, gains, losses, deductions and credits, are allocated to and reflected on the income tax returns of the respective partners.

The Partnership files federal and state tax returns. The 2013 through 2016 tax years for the Partnership remain subject to examination by the Internal Revenue Service and state tax jurisdiction. Because the application of tax laws and regulations to many types of transactions is susceptible to varying interpretations, amounts reported in the financial statements could be changed at a later date upon final determination by taxing authorities.

**Due to/from affiliate** – Due to/from affiliate principally represents the Partnership's cash position with Cellco. Cellco manages, on behalf of the Partnership, all cash, investing and financing activities, including all transactions associated with the sales of wireless device payment plan agreement receivables, of the Partnership. As such, the change in due to/from affiliate is reflected as an investing activity or a financing activity in the statements of cash flows depending on whether it represents a net asset or net liability for the Partnership.

Additionally, cost of equipment, administrative and operating costs incurred by Cellco on behalf of the Partnership, as well as property, plant and equipment and wireless license transactions with affiliates, are charged to the Partnership through this account. Interest income on due from affiliate is based on the Applicable Federal Rate which was approximately 0.7%, 0.5% and 0.3% for the years ended December 31, 2016, 2015 and 2014, respectively. Interest expense on due to affiliate is calculated by applying Cellco's average cost of borrowing from Verizon Communications Inc., which was approximately 4.8%, 4.8% and 5.0% for the years ended December 31, 2016, 2015 and 2014, respectively to the outstanding due to/from affiliate balance. Included in interest (expense) income, net is interest income of \$1,390, \$0 and \$1,706 for the years ended December 31, 2016, 2015 and 2014, respectively, related to due to/from affiliate. Interest expense of \$2,683 and \$23,878 was incurred during the years ended December 31, 2016 and 2015 respectively, of which all was capitalized.



Table of Contents

**Accounts receivable and allowance for doubtful accounts** – Accounts receivable are recorded in the financial statements at cost net of allowance for credit losses, with the exception of device payment plan agreement receivables which are initially recorded at fair value. The Partnership maintains allowances for uncollectible accounts receivable, including device payment plan agreement receivables, for estimated losses resulting from the failure or inability of customers to make required payments. The allowance for uncollectible accounts receivable is based on Cellco's assessment of the collectability of each Partnership's specific customer accounts and includes consideration of the credit worthiness and financial condition of those customers. The Partnership records an allowance to reduce the receivables to the amount that is reasonably believed to be collectible. The Partnership also records an allowance for all other receivables based on multiple factors including historical experience with bad debts, the general economic environment, and the aging of such receivables. Similar to traditional service revenue accounting treatment, bad debt expense related to device payment plan agreement receivables is recorded based on an estimate of the percentage of device payment plan agreement receivables that will not be collected. This estimate is based on a number of factors including historical write-off experience, credit quality of the customer base and other factors such as macro-economic conditions. Due to the device payment plan agreement receivables being incorporated in the standard Verizon Wireless bill, the collection and risk strategies continue to follow historical practices. The Partnership monitors the aging of accounts receivable, including device payment plan agreement receivables, and writes off account balances if collection efforts are unsuccessful and future collection is unlikely.

**Property, plant and equipment** – Property, plant and equipment is recorded at cost. Property, plant and equipment are generally depreciated on a straight-line basis.

Leasehold improvements are amortized over the shorter of the estimated life of the improvement or the remaining term of the related lease, calculated from the time the asset was placed in service.

When the depreciable assets are retired or otherwise disposed of, the related cost and accumulated depreciation are deducted from the property, plant and equipment accounts and any gains or losses on disposition are recognized in income. Transfers of property, plant and equipment between Cellco and affiliates are recorded at net book value on the date of the transfer with an offsetting entry included in due to/from affiliate.

Interest associated with the acquisition or construction of network-related assets is capitalized. Capitalized interest is reported as a reduction in interest expense and depreciated as part of the cost of the network-related assets.

In connection with the ongoing review of estimated useful lives of property, plant and equipment during 2016, Cellco determined that the average useful lives of certain leasehold improvements would be increased from 5 to 7 years. This change was immaterial in 2016. While the timing and extent of current deployment plans are subject to ongoing analysis and modification, Cellco and the Partnership believes the current estimates of useful lives are reasonable.

**Other assets** – Other assets primarily include long term device payment plan agreement receivables, net of allowances of \$16,545 and \$8,661 at December 31, 2016 and 2015, respectively.

**Impairment** – All long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. If any indications were to become present, the Partnership would test for recoverability by comparing the carrying amount of the asset group to the net undiscounted cash flows expected to be generated from the asset group. If those net undiscounted cash flows do not exceed the carrying amount, the next step would be to determine the fair value of the asset and record an impairment, if any. The Partnership reevaluates the useful life determinations for these long-lived assets each year to determine whether events and circumstances warrant a revision to their remaining useful lives.

**Wireless licenses** – Intangible assets are wireless licenses that provide the Partnership wireless operations with the exclusive right to utilize designated radio frequency spectrum to provide wireless communications services. In addition, Cellco maintains wireless licenses that provide the Partnership's operations with the exclusive right to utilize designated radio frequency spectrum to provide wireless communications services. While licenses are issued for only a fixed time, generally ten years, such licenses are subject to renewal by the Federal Communications Commission (FCC). License renewals, which are managed by Cellco, have historically occurred routinely and at nominal cost. Moreover, the Partnership determined that there are currently no legal, regulatory, contractual, competitive, economic or other factors that limit the useful life of wireless licenses. As a result, wireless licenses are treated as an indefinite-lived intangible asset. The useful life determination for wireless licenses is reevaluated each year to determine whether events and circumstances continue to support an indefinite useful life. The Partnership aggregates wireless licenses into one single unit of accounting, as they are utilized on an integrated basis.

Cellco and the Partnership test the wireless licenses balance for potential impairment annually or more frequently if impairment indicators are present. In 2016 and 2015, the Partnership performed a qualitative assessment to determine whether it is more likely than not that the fair value of wireless licenses was less than the carrying amount. As part of the assessment, several qualitative factors were considered including market transactions, the business enterprise value, macroeconomic conditions (including changes in interest rates and discount rates), industry and market considerations (including industry revenue and EBITDA (Earnings before interest, taxes, depreciation and amortization) margin projections), the projected financial performance, as well as other factors. In 2016, Cellco also performed a qualitative assessment similar to that described for the Partnership. In 2015, Cellco performed a quantitative assessment which consisted of comparing the estimated fair value of its aggregate wireless licenses to the aggregated carrying amount as of the test date.



Table of Contents

Interest expense incurred while qualifying activities are performed to ready wireless licenses for their intended use is capitalized as part of wireless licenses (see Note 4). The capitalization period ends when the development is discontinued or substantially complete and the license is ready for its intended use.

In addition, Cellco believes that under the Partnership agreement it has the right to allocate, based on a reasonable methodology, any impairment loss recognized by Cellco for licenses included in Cellco's national footprint. Cellco and the Partnership evaluated their wireless licenses for potential impairment as of December 15, 2016 and 2015. These evaluations resulted in no impairment of wireless licenses.

**Financial instruments** – The Partnership's trade receivables and payables are short-term in nature, and accordingly, their carrying value as well as the carrying value of the deferred purchase price and beneficial interest approximates fair value. The Partnership receives a beneficial interest, which is the residual amount on the device payment plan agreement receivables in excess of proceeds from the sale of these receivables to Cellco. The Partnership records a deferred purchase price, which is the residual amount on the device payment plan agreement receivables in excess of proceeds from the sale of these receivables to a third party. The deferred purchase price and the beneficial interest is recorded at fair value based on the remaining device payment amounts expected to be collected, adjusted, as applicable, for the time value of money and by the timing and estimated value of the device trade-in in connection with upgrades. The collection of the deferred purchase price and the beneficial interest is contingent on collections from customers.

**Fair value measurements** – Fair value of financial and non-financial assets and liabilities is defined as an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. The three-tier hierarchy for inputs used in measuring fair value, which prioritizes the inputs used in the methodologies of measuring fair value for assets and liabilities, is as follows:

Level 1 - Quoted prices in active markets for identical assets or liabilities

Level 2 - Observable inputs other than quoted prices in active markets for identical assets and liabilities

Level 3 - No observable pricing inputs in the market

Financial assets and financial liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurements. The assessment of the significance of a particular input to the fair value measurements requires judgment, and may affect the valuation of the assets and liabilities being measured and their categorization within the fair value hierarchy.

**Distributions** – The Partnership is required to make distributions to its partners based upon the Partnership's operating results, due to/from affiliate status, and financing needs as determined by the General Partner at the date of the distribution.

**Variable interest entities (VIEs)** – VIEs are entities which lack sufficient equity to permit the entity to finance its activities without additional subordinated financial support from other parties, have equity investors which do not have the ability to make significant decisions relating to the entity's operations through voting rights, do not have the obligation to absorb the expected losses, or do not have the right to receive the residual returns of the entity. The assets and liabilities of the VIEs are consolidated when the Partnership is deemed to be the primary beneficiary. The primary beneficiary is the party which has the power to make the decisions that most significantly affect the economic performance of the VIE and the obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE.

**Recent accounting standards** – In August 2016, the accounting standard update related to the classification of certain cash receipts and cash payments was issued. This standard update addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice for these issues. Among the updates, this standard update requires cash receipts from payments on a transferor's beneficial interests in securitized trade receivables to be classified as cash inflows from investing activities. This standard update is effective as of the first quarter of 2018; however, early adoption is permitted. The Partnership is currently evaluating the impact that this standard update will have on the consolidated financial statements. The Partnership expects the amendment relating to beneficial interests in securitization transactions will have an impact on the presentation of collections of the deferred purchase price from sales of wireless device payment plan agreement receivables in the consolidated statements of cash flows.

In June 2016, the standard update related to the measurement of credit losses on financial instruments was issued. This standard update requires that certain financial assets be measured at amortized cost reflecting an allowance for estimated credit losses expected to occur over the life of the assets. The estimate of credit losses must be based on all relevant information including historical information, current conditions and reasonable and supportable forecasts that affect the collectability of the amounts. This standard update is effective as of the first quarter of 2020; however early adoption is permitted. The Partnership is currently evaluating the impact that this standard update will have on the consolidated financial statements.

Table of Contents

In February 2016, the accounting standard update related to leases was issued. This standard update intends to increase transparency and improve comparability by requiring entities to recognize assets and liabilities on the balance sheet for all leases, with certain exceptions. In addition, through improved disclosure requirements, the standard update will enable users of financial statements to further understand the amount, timing, and uncertainty of cash flows arising from leases. This standard update is effective as of the first quarter of 2019; however early adoption is permitted. The Partnership's current operating lease portfolio is primarily comprised of spectrum, network, real estate, and equipment leases. Upon adoption of the standard, the balance sheet is expected to include a right of use asset and liability related to substantially all operating lease arrangements. At Cellco, a cross-functional coordinated implementation team has been established to implement the standard update related to leases. The Partnership is in the process of assessing the impact to its systems, processes and internal controls to meet the standard update's reporting and disclosure requirements.

In May 2014, the accounting standard update related to the recognition of revenue from contracts with customers was issued. This standard update along with related subsequently issued updates clarifies the principles for recognizing revenue and develops a common revenue standard for U.S. GAAP. The standard update also amends current guidance for the recognition of costs to obtain and fulfill contracts with customers such that incremental costs of obtaining and direct costs of fulfilling contracts with customers will be deferred and amortized consistent with the transfer of the related good or service. The standard update intends to provide a more robust framework for addressing revenue issues; improve comparability of revenue recognition practices across entities, industries, jurisdictions, and capital markets; and provide more useful information to users of financial statements through improved disclosure requirements. The two permitted transition methods under the new standard are the full retrospective method, in which case the standard would be applied to each prior reporting period presented and the cumulative effect of applying the standard would be recognized at the earliest period shown, or the modified retrospective method, in which case the standard is applied only to the most current period presented and the cumulative effect of applying the standard would be recognized at the date of initial application. In August 2015, an accounting standard update was issued that delays the effective date of this standard update until the first quarter of 2018, at which time the Partnership plans to adopt the standard.

The Partnership is in the process of evaluating the impact of the standard update. The ultimate impact on revenue resulting from the application of the new standard will be subject to assessments that are dependent on many variables, including, but not limited to, the terms of contractual arrangements and the mix of business. Upon adoption, the Partnership expects that the allocation of revenue between equipment and service for wireless fixed-term service plans will result in more revenue allocated to equipment and recognized earlier as compared with current GAAP. The timing of recognition of sales commission expenses is also expected to be impacted, as a substantial portion of these costs (which are currently expensed) will be capitalized and amortized as described above. The available transition methods will continue to be evaluated. The Partnership's considerations include, but are not limited to, the comparability of financial statements and the comparability within the industry from application of the new standard to contractual arrangements. The Partnership plans to select a transition method by the second half of 2017.

At Cellco, a cross-functional coordinated implementation team has been established to implement the standard update related to the recognition of revenue from contracts with customers. The Partnership has identified and is in the process of implementing changes to its systems, processes and internal controls to meet the standard update's reporting and disclosure requirements.

**Reclassifications** – The Partnership reclassified certain prior year amounts to conform to the current year presentation.

**Subsequent events** – Events subsequent to December 31, 2016 have been evaluated through February 22, 2017, the date the financial statements were issued.

Table of Contents**3. WIRELESS DEVICE PAYMENT PLANS**

Under the Verizon device payment program, eligible wireless customers purchase wireless devices under a device payment plan agreement. Customers that activate service on devices purchased under the device payment program pay lower service fees as compared to those under fixed-term service plans, and their device payment plan charge is included in their standard wireless monthly bill.

**Wireless device payment plan agreement receivables** – The following table displays device payment plan agreement receivables, net, recognized in the accompanying balance sheets:

	2016	2015
Device payment plan agreement receivables, gross	\$ 272,174	\$ 159,527
Unamortized imputed interest	(11,544)	(6,534)
Device payment plan agreement receivables, net of unamortized imputed interest	260,630	152,993
Allowance for credit losses	(36,026)	(25,873)
<b>Device payment plan agreement receivables, net</b>	<b>\$ 224,604</b>	<b>\$ 127,120</b>
<b>Classified on the consolidated balance sheets:</b>		
Accounts receivable, net	\$ 120,747	\$ 68,785
Other assets	\$ 103,857	\$ 58,335
<b>Device payment plan agreement receivables, net</b>	<b>\$ 224,604</b>	<b>\$ 127,120</b>

The Partnership may offer customers certain promotions where a customer can trade-in his or her owned device in connection with the purchase of a new device. Under these types of promotions, the customer will receive trade-in credits that are applied to the customer's monthly bill. As a result, the Partnership recognizes a trade-in obligation measured at fair value using weighted-average selling prices obtained in recent resales of devices eligible for trade-in. Device payment plan agreement receivables, net does not reflect this trade-in obligation. At December 31, 2016 and 2015, the amount of trade-in obligations was not material.

At the time of sale, the Partnership imputes risk adjusted interest on the device payment plan agreement receivables. Imputed interest is recorded as a reduction to the related accounts receivable. Interest income, which is included within Other revenues on the statements of income and comprehensive income, is recognized over the financed payment term.

When originating device payment plan agreements, the Partnership uses internal and external data sources to create a credit risk score to measure the credit quality of a customer and to determine eligibility for the device payment program. If a customer is either new to the Partnership or has less than 210 days of customer tenure (a new customer), the credit decision process relies more heavily on external data sources. For a small portion of new customer applications, a traditional credit report is not available from one of the national credit reporting agencies because the potential customer does not have sufficient credit history. In those instances, alternate credit data is used for the risk assessment. If the customer has 210 days or more of customer tenure (an existing customer), the credit decision process relies on internal data sources. The experience has been that the payment attributes of longer tenured customers are highly predictive when considering their ability to pay in the future. External data sources include obtaining a credit report from a national consumer credit reporting agency, if available. Internal data and/or credit data obtained from the credit reporting agencies is used to create a custom credit risk score. The custom credit risk score is generated automatically (except with respect to a small number of applications where the information needs manual intervention) from the applicant's credit data using Verizon's proprietary custom credit models, which are empirically derived and demonstrably and statistically sound. The credit risk score measures the likelihood that the potential customer will become severely delinquent and be disconnected for non-payment.

Based on the custom credit risk score, each customer is assigned to a credit class, each of which has a specified required down payment percentage and specified credit limits. Device payment plan agreement receivables originated from customers assigned to credit classes requiring no down payment represent the lowest risk. Device payment plan agreement receivables originated from customers assigned to credit classes requiring a down payment represent a higher risk.

Subsequent to origination, the Partnership monitors delinquency and write-off experience as key credit quality indicators for its portfolio of device payment plan agreements and fixed-term service plans. The extent of collection efforts with respect to a particular customer are based on the results of proprietary custom empirically derived internal behavioral scoring models which analyze the customer's past performance to predict the likelihood of the customer falling further delinquent. These customer scoring models assess a number of variables, including origination characteristics, customer account history and payment patterns. Based on the score derived from these models, accounts are grouped by risk category to determine the collection strategy to be applied to such accounts. The Partnership continuously monitors collection performance results and the credit quality of device payment plan agreement receivables based on a variety of metrics, including aging. The Partnership considers an account to be delinquent and in default status if there are unpaid charges remaining on the account on the day after the bill's due date.



Table of Contents

As of December 31, 2016, the balance and aging of the device payment plan agreement receivables on a gross basis was as follows:

Unbilled	\$	264,724
Billed:		
Current		5,885
Past Due		1,565
Device payment plan agreement receivables, gross		272,174

Activity in the allowance for credit losses for the device payment plan agreement receivables was as follows:

	2016	2015
Balance at January 1	\$ 25,873	\$ 3,205
Bad debt expenses	48,965	43,794
Write-offs	(24,482)	(14,319)
Allowance related to receivables sold	(16,829)	(8,758)
Other	2,499	1,951
Balance at December 31	<u>\$ 36,026</u>	<u>\$ 25,873</u>

Customers entering into device payment plan agreements prior to May 31, 2015, have the right to upgrade their device, subject to certain conditions, including making a stated portion of the required device payment plan agreement payments and trading in their device in good working condition. Generally, customers entering into device payment agreements on or after June 1, 2015 are required to repay all amounts due under their device payment agreement before being eligible to upgrade their device. However, on select devices, certain marketing promotions have been revocably offered to customers to upgrade to a new device after paying down a certain specified portion of the device payment plan agreement amount as well as trading in their device in good working order. When a customer enters into a device payment plan agreement with the right to upgrade to a new device or for a device that is subject to an upgrade promotion, the Partnership records a guarantee liability in accordance with the Partnership's accounting policy. The guarantee liability related to this program, which was \$2,840 at December 31, 2016 and \$11,526 at December 31, 2015, was included in Advance billings and other on the accompanying consolidated balance sheets.

**Sales of wireless device payment plan agreement receivables** -- During 2015 and 2016, Cellco established programs pursuant to a Receivables Purchase Agreement (RPA) to sell from time to time, on an uncommitted basis, eligible device payment plan receivables to a group of primarily relationship banks (Purchasers) on both a revolving (Revolving Program) and non-revolving (Non-Revolving Program) basis. Additionally, during September of 2016, Cellco entered into a device payment plan agreement receivables financing facility (the "ABS Financing Facility") with a number of financial institutions. The receivables sold under the RPA and ABS are no longer considered assets of the Partnership.

Cellco continues to bill and collect on the receivables on behalf of the Partnership. Eligible receivables under the RPA exclude device payment plan agreements where a new customer was required to provide a down payment. The sales of receivables under the RPA did not have a material impact on the consolidated statements of income and comprehensive income. The proceeds received from the Purchasers are recorded within cash flows provided by operating activities on the consolidated statements of cash flows.

**Receivables Purchase Agreement** -- Under the Non-Revolving Program, Los Angeles SMSA transfers the eligible receivables to Los Angeles Edge LLC (Seller or SPE). The Seller then sells the receivables to the Purchasers for upfront proceeds and additional consideration upon settlement of the receivables (the deferred purchase price). Under the Revolving Program, Los Angeles SMSA transfers the eligible device payment plan agreement receivables to the Seller. The Seller then sells the eligible receivables on a revolving basis, subject to a maximum funding limit, to the Purchasers. Sales of eligible receivables by the Sellers, once initiated, generally occur and are settled on a monthly basis. Customer payments made towards receivables sold under the Revolving Program will be available to purchase additional eligible device payment plan agreement receivables originated during the revolving period. Cellco elected to end the revolving period in July 2016.

During 2016, the Partnership sold \$178,981 of receivables, net of allowances and imputed interest under the Revolving Program. The Partnership received proceeds from new transfers of \$132,483 and proceeds from reinvested collections of \$36,855, and recorded a deferred purchase price of \$23,873.

During 2015, the Partnership sold \$418,615 of receivables, net of allowances and imputed interest, under the Non-Revolving Program. In connection with this sale, proceeds from new transfers of \$308,659 were received and a deferred purchase price of \$117,587 was recorded. During 2015, the Partnership also sold \$201,283 of receivables, net of allowances and imputed interest, under the Revolving Program. In connection with this sale, proceeds from new transfers of \$168,854 were received and a deferred purchase price of \$32,429 was recorded.



Table of Contents

**Deferred purchase price** – Under the RPA, the deferred purchase price was initially recorded at fair value, based on the remaining device payment amounts expected to be collected, adjusted, as applicable, for the time value of money and by the timing and estimated value of the device trade-in in connection with upgrades. The estimated value of the device trade-in considers prices expected to be offered to us by independent third parties. This estimate contemplates changes in value after the launch of a device. The initial fair value measurements are considered to be Level 3 measurements within the fair value hierarchy. The collection of the deferred purchase price is contingent on collections from customers. At December 31, 2016 and 2015, the Partnership's deferred purchase price receivable was \$95,827 and \$148,941, respectively, which is held by the SPE and is included within Other assets on the consolidated balance sheets.

**Variable interest entities (VIEs)** – Under the RPA, the SPE's sole business consists of the acquisition of the receivables from Los Angeles SMSA and the resale of the receivables to the Purchasers. The assets of the SPE are not available to be used to satisfy obligations of any Partnership entities other than the SPE's. It was determined that the SPE is a VIE as it lacks sufficient equity to finance its activities. Given that Los Angeles SMSA has the power to direct the activities of the SPE that most significantly impact the SPE's economic performance, Los Angeles SMSA is deemed to be the primary beneficiary of the SPE. As a result, the Los Angeles SMSA consolidates the assets and liabilities of the SPE into the consolidated financial statements (see Note 2). Under ABS, there is a Trust entity (the "Trust") whose sole business consists of holding collected receivables which were previously sold by the Partnership to Cellco affiliates under the terms of the ABS Financing Facility. The activity of servicing the receivables and distribution of the cash collected is the activity that has the most significant impact on the Trust. Cellco is the master and special servicer for the receivables but does not have a direct variable interest in the Trust. The Partnership holds a beneficial interest in the Trust which represents the residual interest in the Trust and as such are variable interests. Since Cellco maintains decision making rights as servicer and has an obligation to absorb losses, it is the primary beneficiary in the Trust.

**ABS Financing Facility** – Under the terms of the ABS Financing Facility, the counterparties to the facility made advances under asset-backed loans backed by device payment plan agreement receivables for proceeds. There is a two year revolving period, which may be extended, during which Cellco may transfer additional receivables to an ABS Entity. Subject to certain conditions, Cellco may also remove receivables from the ABS Entity. Cellco may prepay the outstanding amounts of the loans without penalty, but in certain cases, with breakage costs. During 2016, the Partnership sold \$389,800 of device payment plan agreement receivables, net of allowances and imputed interest to Cellco and received proceeds of \$331,454 and recorded a beneficial interest of \$58,346, which is included within Other assets on the consolidated balance sheets.

**Beneficial interest** – Under the ABS Financing Facility, the beneficial interest was initially recorded at fair value, based on the remaining device payment amounts expected to be collected, adjusted, as applicable, for the time value of money. This estimate contemplates changes in value after the launch of a device. The initial fair value measurements are considered to be Level 3 measurements within the fair value hierarchy. The collection of the beneficial interest is contingent on collections from customers. At December 31, 2016, the Partnership's beneficial interest was \$56,359.

**Continuing involvement** – The Partnership has continuing involvement related to the sold receivables as they may be responsible for absorbing additional credit losses pursuant to the RPA. The Partnership's maximum exposure to loss related to the sold receivables is limited to the amount of the deferred purchase price, which was \$95,827 and \$148,941 as of December 31, 2016 and 2015, respectively. The maximum exposure to loss represents an estimated loss that would be incurred under severe, hypothetical circumstances whereby the Partnership would not receive the total portion of the proceeds withheld by the Purchasers. As the Partnership believes the probability of these circumstances occurring is remote, the maximum exposure to loss is not an indication of the Partnership's expected loss. Additionally, Cellco has continuing involvement with the sold receivables as it services the receivables on behalf of the Partnership under the RPA and ABS Financing Facility. Cellco continues to service the customer and their related receivables, including facilitating customer payment collection. The Partnership has no continuing involvement related to the sold receivables and is not responsible for absorbing additional credit losses pursuant to the ABS Financing Facility. While servicing the receivables, the same policies and procedures are applied to the sold receivables that apply to owned receivables, and Cellco continues to maintain normal relationships with the customers. The credit quality of the customers served was consistent throughout the periods presented.

The outstanding device payment plan agreement receivables derecognized from the Partnership's consolidated balance sheets, but which Cellco continues to service, was \$609,990 and \$527,002 (1) at December 31, 2016 and 2015, respectively.

- (1) The Partnership corrected the 2015 information in the preceding Paragraph, which was identified during the preparation of the 2016 consolidated financial statements. Management believes such amounts are immaterial to the previously issued consolidated financial statements.

Table of Contents**4. WIRELESS LICENSES**

Changes in the carrying amount of wireless licenses are as follows:

Balance at January 1, 2015	\$	79,543
Acquisitions		1,972,824
Capitalized interest on wireless licenses		21,075
Reclassifications, adjustments and other		309
Balance at December 31, 2015	\$	2,073,751
Acquisitions		-
Capitalized interest on wireless licenses		1,697
Reclassifications, adjustments and other		-
<b>Balance at December 31, 2016</b>	<b>\$</b>	<b>2,075,448</b>

At December 31, 2016, \$1,972,824 of wireless licenses were under development for commercial service for which the Partnership was capitalizing interest costs.

The average remaining renewal period of the Partnership's wireless license portfolio was 7.0 years as of December 31, 2016.

**Spectrum license transaction** – On January 29, 2015, the FCC completed an auction of 65 MHz of spectrum, which it identified as the AWS-3 band. Cellco participated in that auction and was the high bidder on the licenses covering the Partnership service area. The licenses were deemed to be right to use assets and were allocated and recorded by the Partnership as wireless licenses. The cash payment made by the Partnership of \$1,972,824 is classified within Acquisition of wireless licenses on the statement of cash flows for the year ended December 31, 2015.

**5. PROPERTY, PLANT AND EQUIPMENT, NET**

Property, plant and equipment consist of the following as of December 31, 2016 and 2015:

	2016	2015
Land	\$ 7,716	\$ 7,716
Buildings and improvements (15-45 years)	940,411	836,428
Wireless plant and equipment (3-50 years)	4,165,458	3,973,684
Furniture, fixtures and equipment (3-10 years)	63,565	64,269
Leasehold improvements (5-7 years)	428,995	400,313
	<b>5,606,145</b>	5,282,410
Less: accumulated depreciation	<b>(3,743,253)</b>	(3,477,533)
Property, plant and equipment, net	<b>\$ 1,862,892</b>	\$ 1,804,877

Capitalized interest cost of \$772 and \$2,803, and capitalized network engineering costs of \$24,656 and \$26,754, were recorded during the years ended December 31, 2016 and 2015, respectively. Construction in progress included in certain classifications shown above, principally consists of wireless plant and equipment, amounted to \$127,758 and \$106,935, as of December 31, 2016 and 2015, respectively. Depreciation expense of \$354,329, \$353,975, and \$343,883 was incurred during the years ended December 31, 2016, 2015 and 2014.

Table of Contents**6. TOWER MONETIZATION TRANSACTION**

Prior to the acquisition of the Partnership interest by Celco in 2000, Vodafone Group PLC ("Vodafone"), then parent company of AirTouch Cellular, entered into agreements to sublease all of its unused space on up to 430 of its communications towers ("Sublease Agreement") to SpectraSite Holdings, Inc. ("SpectraSite") in exchange for \$155,000. At various closings in 2001 and 2000, SpectraSite leased 274 communications towers owned and operated by the Partnership for \$98,465. At December 31, 2016 and 2015, the Partnership has \$18,967 and \$23,932, respectively, recorded as deferred rent. The Sublease Agreement requires monthly maintenance fees for the existing physical space used by the Partnership's cellular equipment. The Partnership paid \$1,528, \$2,152 and \$3,944 to SpectraSite pursuant to the Sublease Agreement for the years ended December 31, 2016, 2015 and 2014, respectively, which is included in cost of service in the accompanying statements of income and comprehensive income.

During March 2015, Verizon Communications, the parent company of Celco, entered into an agreement with American Tower Corporation (ATC) giving ATC exclusive rights to lease and operate approximately 11,300 wireless towers owned and operated by Celco and its subsidiaries for an upfront payment of \$5.0 billion (not in thousands). Verizon Communications also sold 162 towers to ATC for an upfront payment of \$0.1 billion (not in thousands). Under the terms of the lease agreements, ATC has exclusive rights to lease and operate the towers over an average term of approximately 28 years. As the leases expire, ATC has fixed-price purchase options to acquire these towers based on their anticipated fair market values at the end of the lease terms. The Partnership has subleased capacity on the towers from ATC for a minimum of 10 years at current market rates, with options to renew. The Partnership participated in this arrangement and has leased 538 towers to ATC for an upfront payment of \$221,653 and has sold 1 tower to ATC for an upfront payment of \$616. The upfront payment, including the towers sold was \$222,269 and was accounted for as deferred rent and as a financing obligation. The \$95,634 accounted for as deferred rent was included in cash flows provided by operating activities and relates to the portion of the towers for which the right-of-use has passed to ATC. The deferred rent is being recognized on a straight-line basis over the Partnership's average lease term of 30 years. At December 31, 2015, a financing obligation in the amount of \$126,635 was included in cash flows provided by financing activities, which relates to the portion of the towers that continue to be occupied and used for the Partnership's network operations. The Partnership makes a sublease payment to ATC for \$1.9 per month per site, with annual increases of 2 percent. During 2016 and 2015, the Partnership made \$12,498 and \$10,260, respectively, of sublease payments to ATC, which is recorded as Repayments of financing obligation.

At December 31, 2016 and 2015, the balance of deferred rent was \$89,605 and \$93,057, respectively. At December 31, 2016 and 2015, the balance of the financing obligation was \$125,296 and \$125,510, respectively.

**7. CURRENT LIABILITIES**

Accounts payable and accrued liabilities consist of the following as of December 31, 2016 and 2015:

	2016	2015
Accounts payable	\$ 189,081	\$ 174,883
Accrued liabilities	13,203	15,924
Accounts payable and accrued liabilities	<u>\$ 202,284</u>	<u>\$ 190,807</u>

Advance billings and other consist of the following as of December 31, 2016 and 2015:

	2016	2015
Advance billings	\$ 139,714	\$ 142,652
Customer deposits	17,880	12,355
Guarantee liability	2,840	11,526
Advance billings and other	<u>\$ 160,434</u>	<u>\$ 166,533</u>

Table of Contents**8. TRANSACTIONS WITH AFFILIATES AND RELATED PARTIES**

In addition to fixed asset purchases and right to use licenses substantially all of service revenues, equipment revenues, other revenues, cost of service, cost of equipment, and selling, general and administrative expenses represent transactions processed by affiliates (Cellco and its related parties) on behalf of the Partnership or represent transactions with affiliates. These transactions consist of (1) revenues and expenses that pertain to the Partnership which are processed by Cellco and directly attributed to or directly charged to the Partnership; (2) roaming revenue by customers of other Cellco affiliated markets within the Partnership market or Partnership customers' cost when roaming in other Cellco affiliated markets; and (3) certain revenues and expenses that are processed or incurred by Cellco which are allocated to the Partnership based on factors such as the Partnership's percentage of revenue streams, customers, gross customer additions, or minutes of use. These transactions do not necessarily represent arm's length transactions and may not represent all revenues and costs that would be present if the Partnership operated on a standalone basis. Cellco periodically reviews the methodology and allocation bases for allocating certain revenues, operating costs, selling, general and administrative expenses to the Partnership. Resulting changes, if any, in the allocated amounts have historically not been significant.

**Service revenues** – Service revenues include monthly customer billings processed by Cellco on behalf of the Partnership and roaming revenues relating to customers of other affiliated markets that are specifically identified to the Partnership. For the years ended December 31, 2016, 2015, and 2014 roaming revenues were \$486,262, \$438,105 and \$369,731, respectively. Service revenues also include long distance, data, and certain revenue reductions including revenue concessions that are processed by Cellco and allocated to the Partnership based on certain factors deemed appropriate by Cellco.

**Equipment revenues** – Equipment revenues include equipment sales processed by Cellco and specifically identified to the Partnership, as well as certain handset and accessory revenues, contra-revenues including equipment concessions, and coupon rebates that are processed by Cellco and allocated to the Partnership based on certain factors deemed appropriate by Cellco.

**Other revenues** – Other revenues include switch revenue and other fees and surcharges charged to the customer that are specifically identified to the Partnership. For the years ended December 31, 2016, 2015, and 2014 switch revenues were \$8,570, \$9,234, and \$6,614, respectively.

**Cost of service** – Cost of service includes roaming costs relating to the Partnership's customers roaming in other affiliated markets. For the years ended December 31, 2016, 2015 and 2014 roaming costs were \$619,985, \$547,672, and \$477,949, respectively. Cost of service also includes cost of telecom, long distance and application content that are incurred by Cellco and allocated to the Partnership based on certain factors deemed appropriate by Cellco. The Partnership has lease agreements for the right to use additional spectrum owned by Cellco. See Note 2 for further information regarding this arrangement.

**Cost of equipment** – Cost of equipment is recorded at Cellco's cost basis (see Note 2). Cost of equipment also includes certain costs related to handsets, accessories and other costs incurred by Cellco and allocated to the Partnership based on certain factors deemed appropriate by Cellco.

**Selling, general and administrative** – Selling, general and administrative expenses include commissions, customer billing, office telecom, customer care, salaries, sales and marketing and advertising expenses that are specifically identified to the Partnership as well as incurred by Cellco and allocated to the Partnership based on certain factors deemed appropriate by Cellco. The Partnership recorded \$113,300, \$117,409 and \$118,342 in advertising costs for the years ended December 31, 2016, 2015 and 2014, respectively.

**Property, plant and equipment** – Property, plant and equipment includes assets purchased by Cellco and directly charged to the Partnership as well as assets transferred between Cellco and the Partnership (see Note 2).

**Wireless licenses** – Wireless licenses include the right to use assets that were allocated by Cellco and recorded by the Partnership in exchange for a \$1,972,824 payment (see Note 4).

Table of Contents**9. COMMITMENTS**

Cellco, on behalf of the Partnership, and the Partnership itself have entered into operating leases for facilities and equipment used in its operations. Lease contracts include renewal options that include rent expense adjustments based on the Consumer Price Index as well as annual and end-of-lease term adjustments. Rent expense is recorded on a straight-line basis. The noncancellable lease term used to calculate the amount of the straight-line rent expense is generally determined to be the initial lease term, including any optional renewal terms that are reasonably assured of occurring. Leasehold improvements related to these operating leases are amortized over the shorter of their estimated useful lives or the noncancellable lease term. For the years ended December 31, 2016, 2015 and 2014, the Partnership incurred a total of \$117,771, \$104,515 and \$97,285 respectively, as rent expense related to these operating leases, which was included in Cost of service and Selling, general and administrative expenses in the accompanying statements of income and comprehensive income. Aggregate future minimum rental commitments under noncancellable operating leases, excluding renewal options that are not reasonably assured of occurring and remaining tower maintenance fees of \$10,182 (see Note 6), for the years shown are as follows:

Years	Amount
2017	\$ 95,290
2018	84,812
2019	73,290
2020	49,838
2021	27,042
2022 and thereafter	<u>131,324</u>
Total minimum payments	<u>\$ 461,596</u>

The Partnership has also entered into certain agreements with Cellco, whereas the Partnership leases certain spectrum from Cellco that overlaps the Los Angeles metropolitan service area. Total rent expense under these spectrum leases amounted to \$124,943 in 2016, \$124,722 in 2015 and \$110,044 in 2014, respectively, which is included in Cost of service in the accompanying consolidated statements of income and comprehensive income.

Based on the terms of these leases as of December 31, 2016, future spectrum lease obligations are expected to be as follows:

Years	Amount
2017	\$ 103,919
2018	93,249
2019	82,781
2020	72,312
2021	72,312
2022 and thereafter	<u>882,177</u>
Total minimum payments	<u>\$ 1,306,750</u>

The General Partner currently expects that any renewal option in the leases will be exercised.

Table of Contents**10. CONTINGENCIES**

Cellco and the Partnership are subject to lawsuits and other claims including class actions, product liability, patent infringement, intellectual property, antitrust, partnership disputes, and claims involving relations with resellers and agents. Cellco is also currently defending lawsuits filed against it and other participants in the wireless industry alleging various adverse effects as a result of wireless phone usage. Various consumer class action lawsuits allege that Cellco violated certain state consumer protection laws and other statutes and defrauded customers through misleading billing practices or statements. These matters may involve indemnification obligations by third parties and/or affiliated parties covering all or part of any potential damage awards against Cellco and the Partnership and/or insurance coverage. All of the above matters are subject to many uncertainties, and the outcomes are not currently predictable.

The Partnership may be allocated a portion of the damages that may result upon adjudication of these matters if the claimants prevail in their actions. In none of the currently pending matters is the amount of accrual material to the Partnership. An estimate of the reasonably possible loss or range of loss with respect to these matters as of December 31, 2016 cannot be made at this time due to various factors typical in contested proceedings, including (1) uncertain damage theories and demands; (2) a less than complete factual record; (3) uncertainty concerning legal theories and their resolution by courts or regulators; and (4) the unpredictable nature of the opposing party and its demands. The Partnership continuously monitors these proceedings as they develop and will adjust any accrual or disclosure as needed. It is not expected that the ultimate resolution of any pending regulatory or legal matter in future periods will have a material effect on the financial condition of the Partnership, but it could have a material effect on the results of operations for a given reporting period.

**11. RECONCILIATION OF ALLOWANCE FOR DOUBTFUL ACCOUNTS**

	Balance at Beginning of the Year	Additions Charged to Operations	Write-offs Net of Recoveries	Balance at End of the Year
Accounts Receivable Allowances:				
2016	\$ 45,751	\$ 71,925	\$ (70,038)	\$ 47,638
2015	24,136	79,063	(57,448)	45,751
2014	21,600	34,370	(31,834)	24,136

\*\*\*\*\*

S-19



Table of Contents**Power of Attorney**

Each person whose signature appears below constitutes and appoints LeRoy T. Carlson, Jr. as his or her true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution for him or her and in his or her name, place, and stead, in any and all capacities to sign any and all amendments to this Annual Report on Form 10-K under the Securities Exchange Act of 1934, as amended, and to file the same, with all exhibits thereto, and other documents in connection therewith with the Securities and Exchange Commission, granting unto said attorney-in-fact and agent full power and authority to do so and perform each and every act and thing requisite or necessary to be done in and about the premises, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all the said attorney-in fact and agent or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ LeRoy T. Carlson, Jr.</u> LeRoy T. Carlson, Jr.	Director	February 24, 2017
<u>/s/ Kenneth R. Meyers</u> Kenneth R. Meyers	Director	February 24, 2017
<u>/s/ James Barr III</u> James Barr III	Director	February 24, 2017
<u>/s/ Steven T. Campbell</u> Steven T. Campbell	Director	February 24, 2017
<u>/s/ Walter C. D. Carlson</u> Walter C. D. Carlson	Director	February 24, 2017
<u>/s/ J. Samuel Crowley</u> J. Samuel Crowley	Director	February 24, 2017
<u>/s/ Ronald E. Daly</u> Ronald E. Daly	Director	February 24, 2017
<u>/s/ Paul-Henri Denuit</u> Paul-Henri Denuit	Director	February 24, 2017
<u>/s/ Harry J. Harczak, Jr.</u> Harry J. Harczak, Jr.	Director	February 24, 2017
<u>/s/ Gregory P. Josefowicz</u> Gregory P. Josefowicz	Director	February 24, 2017
<u>/s/ Peter L. Sereda</u> Peter L. Sereda	Director	February 24, 2017
<u>/s/ Douglas D. Shuma</u> Douglas D. Shuma	Director	February 24, 2017
<u>/s/ Cecelia D. Stewart</u> Cecelia D. Stewart	Director	February 24, 2017
<u>/s/ Kurt B. Thaus</u> Kurt B. Thaus	Director	February 24, 2017



[Table of Contents](#)**Index to Exhibits**

Exhibit Number	Description of Documents
3.1	Restated Certificate of Incorporation, is hereby incorporated by reference to Exhibit 3.1 to U.S. Cellular's Current Report on Form 8-K dated November 10, 2014.
3.2	Restated Bylaws are hereby incorporated by reference to Exhibit 3.1 to U.S. Cellular's Current Report on Form 8-K dated August 19, 2014.
4.1	Restated Certificate of Incorporation incorporated herein as Exhibit 3.1.
4.2	Restated Bylaws are incorporated herein as Exhibit 3.2.
4.3	Revolving Credit Agreement, among U.S. Cellular, Toronto Dominion (Texas) LLC, as administrative agent, and the other lenders thereto, dated as of June 15, 2016, including Schedules and Exhibits, including the form of the subsidiary Guaranty and Subordination Agreement, is hereby incorporated by reference to Exhibit 4.1 to U.S. Cellular's Form 8-K dated June 15, 2016.
4.4(a)	Indenture for Senior Debt Securities dated June 1, 2002 between U.S. Cellular and The Bank of New York Mellon Trust Company, N.A., formerly known as BNY Midwest Trust Company of New York ("BNY") is hereby incorporated by reference to Exhibit 4.1 to Form S-3 dated May 31, 2013 (File No. 333-188971).
4.4(b)	Form of Third Supplemental Indenture dated December 3, 2003 between U.S. Cellular and BNY Midwest Trust Company, relating to \$444,000,000 of U.S. Cellular's 6.7% Senior Notes due 2033, is hereby incorporated by reference to Exhibit 4.1 to U.S. Cellular's Current Report on Form 8-K dated December 3, 2003.
4.4(c)	Form of Fifth Supplemental Indenture dated June 21, 2004 between U.S. Cellular and BNY Midwest Trust Company, relating to \$100,000,000 of U.S. Cellular's 6.7% Senior Notes due 2033, is hereby incorporated by reference to Exhibit 4.1 to U.S. Cellular's Current Report on Form 8-K dated June 21, 2004.
4.4(d)	Form of Sixth Supplemental Indenture dated as of May 9, 2011 between U.S. Cellular and BNY Midwest Trust Company, related to \$342,000,000 of U.S. Cellular's 6.95% Senior Notes due 2060, is hereby incorporated by reference to Exhibit 4.1 to U.S. Cellular's Current Report on Form 8-K dated May 9, 2011.
4.4(e)	Form of Seventh Supplemental Indenture dated as of December 8, 2014 between U.S. Cellular and BNY Midwest Trust Company, related to \$275,000,000 of U.S. Cellular's 7.25% Senior Notes due 2063, is hereby incorporated by reference to Exhibit 2 to U.S. Cellular's Registration Statement on Form 8-A dated December 2, 2014.
4.4(f)	Form of Eighth Supplemental Indenture dated as of November 23, 2015 between U.S. Cellular and BNY Midwest Trust Company, related to \$300,000,000 of U.S. Cellular's 7.25% Senior Notes due 2064, is hereby incorporated by reference to Exhibit 2 to U.S. Cellular's Registration Statement on Form 8-A dated November 17, 2015.
4.5	Indenture for Subordinated Debt Securities between U.S. Cellular and BNY is hereby incorporated by reference to Exhibit 4.1 to U.S. Cellular's Current Report on Form 8-K dated September 16, 2013.
4.6	Amended and Restated Term Loan Credit Agreement, among U.S. Cellular and CoBank, ACB, as administrative agent, and the other lenders thereto, dated as of June 15, 2016, including Schedules and Exhibits, including the forms of the subsidiary Guaranty and Subordination Agreement, is hereby incorporated by reference to Exhibit 4.1 to U.S. Cellular's Form 8-K dated June 15, 2016.
9.1	Amendment and Restatement (dated April 22, 2005) of Voting Trust Agreement dated June 30, 1989 is hereby incorporated by reference to the Exhibit filed on Amendment No. 3 to the Schedule 13D dated May 2, 2005 filed by the trustees of such voting trust with respect to TDS Common Shares.
10.1	Tax Allocation Agreement between U.S. Cellular and TDS is hereby incorporated by reference to an exhibit to U.S. Cellular's Registration Statement on Form S-1 (Registration No. 33-16975).
10.2	Cash Management Agreement between U.S. Cellular and TDS is hereby incorporated by reference to an exhibit to U.S. Cellular's Registration Statement on Form S-1 (Registration No. 33-16975).
10.3	Registration Rights Agreement between U.S. Cellular and TDS is hereby incorporated by reference to an exhibit to U.S. Cellular's Registration Statement on Form S-1 (Registration No. 33-16975).

- 10.4 Exchange Agreement between U.S. Cellular and TDS, as amended, is hereby incorporated by reference to an exhibit to U.S. Cellular's Registration Statement on Form S-1 (Registration No. 33-16975).
- 10.5 Intercompany Agreement between U.S. Cellular and TDS is hereby incorporated by reference to an exhibit to U.S. Cellular's Registration Statement on Form S-1 (Registration No. 33-16975).
- 10.6 Employee Benefit Plans Agreement between U.S. Cellular and TDS is hereby incorporated by reference to an exhibit to U.S. Cellular's Registration Statement on Form S-1 (Registration No. 33-16975).
- 10.7 Insurance Cost Sharing Agreement between U.S. Cellular and TDS is hereby incorporated by reference to an exhibit to U.S. Cellular's Registration Statement on Form S-1 (Registration No. 33-16975).
- 10.8(a)\* TDS Supplemental Executive Retirement Plan, as amended and restated, effective January 1, 2009 is hereby incorporated by reference to Exhibit 10.1 to TDS' Current Report on Form 8-K dated August 27, 2008.
- 10.8(b)\* Amendment Number One to the TDS Supplemental Executive Retirement Plan, is hereby incorporated by reference to Exhibit 10.2 to TDS' Current Report on Form 8-K dated March 15, 2012.
- 10.8(c)\* Amendment Number Two to the TDS Supplemental Executive Retirement Plan, is hereby incorporated by reference to Exhibit 10.3 to TDS' Current Report on Form 8-K dated November 3, 2014.
- 10.9\* U.S. Cellular Restated Compensation Plan for Non-Employee Directors is hereby incorporated by reference to Exhibit B to the U.S. Cellular's Notice of Annual Meeting of Shareholders and Proxy Statement dated April 15, 2013, which was filed with the SEC on Schedule 14A on April 15, 2013.
-

Table of Contents

- 10.10\* U.S. Cellular 2005 Long-Term Incentive Plan is hereby incorporated by reference to Exhibit C to the U.S. Cellular Notice of Annual Meeting of Shareholders and Proxy Statement dated April 15, 2009, which was filed with the SEC on Schedule 14A on April 15, 2009.
- 10.11(a)\* U.S. Cellular 2013 Long-Term Incentive Plan is hereby incorporated by reference to Exhibit B to the U.S. Cellular Notice of Annual Meeting of Shareholders and Proxy Statement dated April 12, 2016, which was filed with the SEC on Schedule 14A on April 12, 2016.
- 10.11(b)\* Amendment No. 1 to U.S. Cellular 2013 Long-Term Incentive Plan is hereby incorporated by reference to Exhibit A to the U.S. Cellular Notice of Annual Meeting of Shareholders and Proxy Statement dated April 12, 2016, which was filed with the SEC on Schedule 14A on April 12, 2016.
- 10.12\* U.S. Cellular Form of Long-Term Incentive Plan Executive Deferred Compensation Agreement —Phantom Stock Account for officers is hereby incorporated by reference to Exhibit 10.5 to U.S. Cellular's Current Report on Form 8-K dated May 14, 2013.
- 10.13(a)\* U.S. Cellular Executive Deferred Compensation Interest Account Plan is hereby incorporated by reference to Exhibit 10.1 to U.S. Cellular's Current Report on Form 8-K dated December 10, 2007.
- 10.13(b)\* First Amendment to U.S. Cellular Executive Deferred Compensation Interest Account Plan is hereby incorporated by reference to Exhibit 10.6 to U.S. Cellular's Current Report on Form 8-K dated December 9, 2008.
- 10.13(c)\* Second Amendment to U.S. Cellular Executive Deferred Compensation Interest Account Plan is hereby incorporated by reference to Exhibit 10.12(c) to U.S. Cellular's Annual Report on Form 10-K for the year ended December 31, 2012.
- 10.13(d)\* Election Form for U.S. Cellular Executive Deferred Compensation Interest Account Plan is hereby incorporated by reference to Exhibit 10.12(d) to U.S. Cellular's Annual Report on Form 10-K for the year ended December 31, 2012.
- 10.14\* U.S. Cellular Form of Long-Term Incentive Plan Restricted Stock Unit Award Agreement for the President and CEO, is hereby incorporated by reference to Exhibit 10.4 to U.S. Cellular's Current Report on Form 8-K dated March 14, 2016.
- 10.15\* U.S. Cellular Form of Long-Term Incentive Plan Stock Option Award Agreement for the President and CEO, is hereby incorporated by reference to Exhibit 10.3 to U.S. Cellular's Current Report on Form 8-K dated March 14, 2016.
- 10.16\* Letter Agreement dated October 28, 2013 between U.S. Cellular and Jay Ellison, is hereby incorporated by reference to Exhibit 10.13 to U.S. Cellular's Annual Report on Form 10-K for the year ended December 31, 2013.
- 10.17\* U.S. Cellular Form of Long-Term Incentive Plan Stock Option Award Agreement for Officers other than the President and CEO, is hereby incorporated by reference to Exhibit 10.1 to U.S. Cellular's Current Report on Form 8-K dated March 14, 2016.
- 10.18\* U.S. Cellular Form of Long-Term Incentive Plan Restricted Stock Unit Award Agreement for Officers other than the President and CEO, is hereby incorporated by reference to Exhibit 10.2 to U.S. Cellular's Current Report on Form 8-K dated March 14, 2016.
- 10.19\* Letter Agreement between U.S. Cellular and Steven T. Campbell dated June 1, 2005 is hereby incorporated by reference to Exhibit 99.2 to U.S. Cellular's Current Report on Form 8-K dated June 1, 2005.
- 10.20\* Form of Retention Bonus Letter to "named executive officers" other than the President and CEO is hereby incorporated by reference to Exhibit 10.1 to U.S. Cellular's Current Report on Form 8-K dated April 12, 2011.
- 10.21\* U.S. Cellular 2016 Officer Annual Incentive Plan effective January 1, 2016 is hereby incorporated by reference to Exhibit 10.1 to U.S. Cellular's Current Report on Form 8-K dated June 7, 2016.
- 10.22\* Guidelines for the Determination of Annual Bonus for President and Chief Executive Officer of U.S. Cellular, are hereby incorporated by reference to Exhibit 10.2 to U.S. Cellular's Current Report on Form 8-K dated August 19, 2014.
- 10.23\* Letter Agreement dated July 25, 2013 between U.S. Cellular and Kenneth R. Meyers is hereby incorporated by reference to Exhibit 10.1 to U.S. Cellular's Current Report on Form 8-K dated July 25, 2013.
- 10.24\*\* Master Service Agreement entered into by United States Cellular Corporation and Amdocs Software Systems

Limited on August 17, 2010 to develop a Billing and Operational Support System ("B/OSS") with a new point-of-sale system to consolidate billing on one platform, is hereby incorporated by reference to Exhibit 10.8 to U.S. Cellular's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2010.

10.25\*\*

Software License and Maintenance Agreement entered into by United States Cellular Corporation and Amdocs Software Systems Limited on August 17, 2010 to develop a Billing and Operational Support System ("B/OSS") with a new point-of-sale system to consolidate billing on one platform, is hereby incorporated by reference to Exhibit 10.9 to U.S. Cellular's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2010.

---

Table of Contents

10.26**	Master Statement of Work, dated as of November 25, 2014, between U.S. Cellular and Amdocs Software Systems, Ltd., is hereby incorporated by reference from Exhibit 10.26 to U.S. Cellular's Annual Report on Form 10-K for the year ended December 31, 2014.
10.27*	Letter Agreement dated March 14, 2014 between U.S. Cellular and Deirdre Drake, is hereby incorporated by reference from Exhibit 10.27 to U.S. Cellular's Annual Report on Form 10-K for the year ended December 31, 2014.
11	Statement regarding computation of earnings per share (included in Note 5 — Earnings Per Share in the Notes to Consolidated Financial Statements in Exhibit 13).
12	Statement regarding computation of ratio of earnings to fixed charges for the years ended December 31, 2016, 2015, 2014, 2013, and 2012.
13	Incorporated portions of 2016 Annual Report to Shareholders.
21	Subsidiaries of U.S. Cellular.
23.1	Consent of Independent Registered Public Accounting Firm—PricewaterhouseCoopers LLP.
23.2	Consent of Independent Registered Public Accounting Firm—Ernst & Young LLP.
31.1	Principal executive officer certification pursuant to Rule 13a-14 of the Securities Exchange Act of 1934.
31.2	Principal financial officer certification pursuant to Rule 13a-14 of the Securities Exchange Act of 1934.
32.1	Principal executive officer certification pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code.
32.2	Principal financial officer certification pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
*	Indicates a management contract or compensatory plan or arrangement.
**	Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission as part of an application for confidential treatment pursuant to the Securities Exchange Act of 1934, as amended. The application for confidential treatment has been granted.

10-K 1 d296602d10k.htm 10-K

Table of Contents

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

(Mark one)

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2016

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: 1-8606

**Verizon Communications Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction  
of incorporation or organization)

**23-2259884**  
(I.R.S. Employer Identification No.)

**1095 Avenue of the Americas**  
**New York, New York**  
(Address of principal executive offices)

**10036**  
(Zip Code)

Registrant's telephone number, including area code: (212) 395-1000

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, \$.10 par value	New York Stock Exchange The NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes   
No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter)

during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark 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. (Check one):

Large accelerated filer       Accelerated filer       Non-accelerated filer       Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

At June 30, 2016, the aggregate market value of the registrant's voting stock held by non-affiliates was approximately \$227,584,340,225.

At January 31, 2017, 4,076,731,752 shares of the registrant's common stock were outstanding, after deducting 165,642,488 shares held in treasury.

#### Documents Incorporated By Reference:

Portions of the registrant's Annual Report to Shareowners for the year ended December 31, 2016 (Parts I and II).

---

Table of Contents

## TABLE OF CONTENTS

Item No.		Page
<b>PART I</b>		
Item 1.	<u>Business</u>	3
Item 1A.	<u>Risk Factors</u>	18
Item 1B.	<u>Unresolved Staff Comments</u>	21
Item 2.	<u>Properties</u>	21
Item 3.	<u>Legal Proceedings</u>	21
Item 4.	<u>Mine Safety Disclosures</u>	21
<b>PART II</b>		
Item 5.	<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	22
Item 6.	<u>Selected Financial Data</u>	22
Item 7.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	22
Item 7A.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	22
Item 8.	<u>Financial Statements and Supplementary Data</u>	22
Item 9.	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	22
Item 9A.	<u>Controls and Procedures</u>	23
Item 9B.	<u>Other Information</u>	23
<b>PART III</b>		
Item 10.	<u>Directors, Executive Officers and Corporate Governance</u>	23
Item 11.	<u>Executive Compensation</u>	24
Item 12.	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	24
Item 13.	<u>Certain Relationships and Related Transactions, and Director Independence</u>	24
Item 14.	<u>Principal Accounting Fees and Services</u>	24
<b>PART IV</b>		
Item 15.	<u>Exhibits, Financial Statement Schedules</u>	25
	<u>Signatures</u>	30

**Certifications**

## **Table of Contents**

### **PART I**

#### **Item 1 Business**

##### **General**

Verizon Communications Inc. (Verizon, or the Company) is a holding company that, acting through its subsidiaries, is one of the world's leading providers of communications, information and entertainment products and services to consumers, businesses and governmental agencies. With a presence around the world, we offer voice, data and video services and solutions on our wireless and wireline networks that are designed to meet customers' demand for mobility, reliable network connectivity, security and control. Formerly known as Bell Atlantic Corporation (Bell Atlantic), we were incorporated in 1983 under the laws of the State of Delaware. We began doing business as Verizon on June 30, 2000 following our merger with GTE Corporation. We have a highly diverse workforce of approximately 160,900 employees.

Our principal executive offices are located at 1095 Avenue of the Americas, New York, New York 10036 (telephone number 212-395-1000).

We have two reportable segments, Wireless and Wireline, which we operate and manage as strategic business segments and organize by products and services.

**Wireless** Wireless' communications products and services include wireless voice and data services and equipment sales, which are provided to consumer, business and government customers across the United States.

**Wireline** Wireline's voice, data and video communications products and enhanced services include broadband video and data, corporate networking solutions, data center and cloud services, security and managed network services and local and long distance voice services. We provide these products and services to consumers in the United States, as well as to carriers, businesses and government customers both in the United States and around the world.

Additional discussion of our reportable segments is included in the 2016 Verizon Annual Report to Shareowners under the headings "Management's Discussion and Analysis of Financial Condition and Results of Operations - Overview and - Segment Results of Operations" and in Note 12 to the consolidated financial statements of Verizon Communications Inc. and Subsidiaries, which are incorporated by reference into this report.

##### **Wireless**

###### **Background**

Our Wireless segment, doing business as Verizon Wireless, provides wireless communications services and products across one of the most extensive wireless networks in the United States (U.S.). Verizon Wireless is the largest wireless service provider in the United States as measured by retail connections and revenue. At December 31, 2016, Verizon Wireless had 114.2 million retail connections and 2016 revenues of approximately \$89.2 billion, representing approximately 71% of Verizon's aggregate revenues.

Cellco Partnership (Cellco), which originally held the wireless assets of Bell Atlantic, began operating as "Verizon Wireless" in April 2000 with both Vodafone Group Plc (Vodafone) and Bell Atlantic as partners, following Vodafone's contribution of its U.S. wireless assets into Cellco. On September 2, 2013, Verizon entered into a stock purchase agreement with Vodafone and Vodafone 4 Limited, pursuant to which Verizon agreed to acquire all of Vodafone's indirect 45% interest in Verizon Wireless for aggregate consideration of approximately \$130 billion (the Wireless Transaction). We completed the Wireless Transaction on February 21, 2014 and, as a result, we acquired 100% ownership of Verizon Wireless. The consideration paid was primarily comprised of cash and Verizon common stock.

We have the largest fourth-generation (4G) Long-Term Evolution (LTE) technology and third-generation (3G) Evolution - Data Optimized (EV-DO) networks of any U.S. wireless service provider. Our 4G LTE network is available to over 98% of the U.S. population in more than 500 markets covering approximately 314 million people, including those in areas served by our LTE in Rural America partners. Under this program, we are working with wireless carriers in rural areas to collaboratively build and operate a 4G LTE network using each carrier's network assets and our core 4G LTE equipment and 700 MHz C Block and Advanced Wireless Services (AWS) spectrum.

We are adding capacity and density to our 4G LTE network. We are committed to developing and deploying fifth-generation (5G) wireless technology and are working with key partners to ensure the aggressive pace of innovation, standards development and appropriate requirements for this next generation of wireless technology. Based on the outcome of our ongoing pre-commercial trials, we intend to be the first company to deploy a 5G fixed wireless broadband network in the United States. We expect to launch a fixed commercial wireless service supported by this network in 2018.

## Table of Contents

### **Wireless Service and Product Offerings**

Our wireless services are available to our customers receiving service under the Verizon Wireless brand. In addition, customers can obtain wireless products and services that operate on our network from resellers that purchase network access from us on a wholesale basis.

#### *Wireless Services*

We offer our wireless services on a postpaid and prepaid basis. Retail (non-wholesale) postpaid accounts primarily represent retail customers with Verizon Wireless that are directly served and managed by Verizon Wireless and use its branded services. A single account may include monthly wireless services for a variety of connected devices. A postpaid retail connection represents an individual line of service for a wireless device for which a customer is billed in advance a monthly access charge in return for a monthly network service allowance, and usage beyond the allowance is billed in arrears. Approximately 95% of our total retail connections were postpaid retail connections as of December 31, 2016. Our prepaid service enables individuals to obtain wireless services without credit verification by paying for all services in advance.

We offer various postpaid account service plans, including shared data plans, single connection plans and other plans tailored to the needs of our customers. Our shared data plans typically feature domestic unlimited voice minutes, unlimited domestic and international text, video and picture messaging, and a single data allowance that can be shared among the wireless devices on a customer's account. These allowances will vary from time to time as part of promotional offers or in response to market circumstances. On February 12, 2017, we announced an introductory plan, our new Verizon Unlimited plan, available to our consumer and small business customers, which offers among other things, unlimited domestic voice, data and texting. Both our shared data plans and the Verizon Unlimited plan include our HD (High Definition) Voice, Video Calling and Mobile Hotspot services on compatible devices. HD Voice is a suite of services enabled by Voice over LTE (VoLTE), which delivers calls over our 4G LTE network, and our Video Calling service combines an HD Voice call with real-time video. Our Mobile Hotspot service enables a customer to activate a personal Wi-Fi hotspot via their smartphone that can provide Internet access to multiple Wi-Fi enabled devices. We also offer various voice and shared data plans for small and large businesses.

Our simplified shared data plan, the new Verizon Plan, offers customers various sizes of data packages that can be shared among up to 10 devices on a consumer account or 25 devices on a business account. The plan features Carryover Data, which allows customers to carry over unused data to the next month, and Safety Mode, which enables customers to avoid data overage fees by allowing them to continue using data at a reduced data speed after using their data allowance. Certain plans, with higher account access amounts also include calling to and voice, text and data roaming in Mexico and Canada. Customers who wish to participate in this new plan can do so by purchasing a device from Verizon either under our device payment program or at full retail, or by using their own compatible device.

Customers on our fixed-term service plans have historically paid higher access fees for their wireless service in exchange for the ability to purchase their wireless devices at subsidized prices. We have largely discontinued this form of device subsidy. Under the Verizon device payment program, our eligible wireless customers purchase wireless devices under a device payment plan agreement. Customers that activate service on devices purchased under the device payment program or on a compatible device that they already own pay lower access fees (unsubsidized service pricing) as compared to those under our fixed-term service plans. Generally, customers entering into device payment plan agreements on or after June 1, 2015 are required to repay all amounts due under their device payment plan agreement before being eligible to upgrade their device. However, certain devices are subject to promotions that allow customers to upgrade to a new device after paying down a specified percentage of the balance on their device payment plan and trading in their device in good working condition.

We also offer prepaid single connection service plans that feature domestic unlimited voice minutes and unlimited domestic and international text. On compatible devices, certain of our prepaid plans also feature video and picture messaging, Carryover Data and Always-On Data, which allows a customer to stay online at reduced data speeds after using their data allowance. HD Voice, Video Calling and Mobile Hotspot service are available on compatible devices. Customers can manage their prepaid services on the device using their My Verizon Mobile application or logging in to the My Verizon website.

We offer our customers a wide variety of wireless services accessible on a broad range of devices. Access to the Internet is available on all smartphones and nearly all basic phones. We also offer service that enables our customers to access the Internet wirelessly at broadband speeds on notebook computers and tablets that either have embedded 4G LTE or 3G EV-DO modules or that are used in conjunction with separate devices that enable access to this service, such as USB modems, Jetpacks™ and other dedicated devices that provide a mobile Wi-Fi connection.

Our customers can access multimedia offerings, provided by Verizon and by third parties, consisting of applications providing music, video, gaming, news and other content. Our business-focused offerings, which are designed to increase productivity, include solutions that enable customers to access the Internet, their corporate intranets and e-mail across our diverse portfolio of wireless devices. Our location-based services provide our customers with directions to their destination and enable our business customers to locate, monitor and

communicate with their mobile field workers. Our global data services allow our customers to access data services and the Internet on all smartphones and many tablets and basic phones from hundreds of international destinations that we sell. A majority of the wireless devices used by our customers can run applications and services offered by Google (a subsidiary of Alphabet Inc.) via Google Play or Apple Inc. (Apple) via iTunes.

Our customers can also make and receive calls on their home phone handsets using our wireless network through our Home Phone Connect service or Verizon 4G LTE Broadband Router with Voice service. We also offer LTE Internet (Installed), a high-speed Internet service that provides customers with Internet connections in their homes using our 4G LTE network.

## **Table of Contents**

We provide network access and, in some cases, enhanced value-added services to support wireless connections for the Internet of Things (IoT). Our IoT services offer end-to-end solutions for various IoT vertical markets, such as:

- Fleet management and telematics – We provide in-vehicle solutions that enable vehicle navigation, GPS tracking, engine diagnostic monitoring and maintenance alerts;
- Energy – We offer solutions targeted to providing the energy sector with greater visibility into energy usage and the ability to remotely monitor devices used to track energy usage;
- Agricultural technology – We provide solutions that give farmers critical data they need to improve yields and save costs; and
- Smart Communities – Our solutions enable localities to collect data from IoT and connected machine technologies with the goal of improving public safety, managing traffic, reducing pollution, identifying revenue generation opportunities, making efficient use of limited resources and attracting businesses, residents and workers.

We also work with various companies that purchase network access from us to connect their Open Development certified devices, bundled together with their own solutions, which they sell to end-users.

### ***Wireless Devices***

We offer several categories of wireless devices, including smartphones and basic phones, tablets and other Internet access devices.

*Smartphones and Basic Phones.* All of the smartphones we offer are enabled to utilize our 4G LTE and 3G EV-DO high-speed data services. These devices run on various operating platforms, primarily Apple iOS and Google Android. The basic phones we offer are 3G EV-DO-enabled and have HTML-browsing capability.

*Tablets and Other Internet Devices.* We offer tablets from multiple manufacturers, all of which can access the Internet via our 4G LTE network or a Wi-Fi connection. The tablets run primarily on the Apple iOS and Google Android operating systems. In addition, we offer dedicated devices, which we refer to as Jetpacks that provide a mobile Wi-Fi 4G LTE and/or 3G EV-DO connection and are capable of connecting multiple Wi-Fi enabled devices to the Internet at one time. Our customers can also access the Internet wirelessly at broadband speeds on their computers via data cards, USB modems or through the use of certain laptop computers and netbooks enabled to access our wireless network.

We purchase a substantial majority of our wireless devices and accessories from Apple, Samsung, Motorola Mobility, Google, LG Electronics and HTC.

A key component of all wireless devices is the chipset, which contains the “intelligence” of the device. The LTE chipsets used in our 4G LTE-enabled devices are manufactured by various companies, each using its own 4G LTE chipset technology. To support Code Division Multiple Access (CDMA)-1XRTT and EV-DO technologies (with and without 4G LTE), most of our wireless device suppliers currently rely on Qualcomm Incorporated for the manufacture and supply of chipsets. In addition, there are a number of other components common to wireless devices provided by various electronic component manufacturers that we do not deal with directly.

### ***Network***

We have the largest 4G LTE and 3G EV-DO networks of any service provider in the United States, with licensed and operational coverage in all of the 100 most populous U.S. metropolitan areas. As of December 31, 2016, our 4G LTE network covered approximately 314 million people in the United States, including those in areas served by our LTE in Rural America partners. We currently have 21 LTE in Rural America partners that provide 4G LTE coverage to an area covering approximately three million people.

The reliability of our wireless network is a key factor for our continued success, and we strive to provide our customers with the highest network reliability for their wireless services. We believe that steady and consistent network and platform investments provide the foundation for innovative products and services that will fuel profitable growth. The depth and breadth of our network provides our fundamental strength and is the basis for our competitive advantage.

We design and deploy our network in an efficient manner that we believe maximizes the number of successful data sessions, including video, permitting the completion of large file downloads and uploads while delivering on our advertised throughput speeds, and maximizes the number of calls that are connected on the first attempt and completed without being dropped. We plan to continue to upgrade our network, primarily to increase its capacity and density, by utilizing small cell technology, in-building solutions and distributed antennae systems in addition to deploying existing AWS spectrum. We are also exploring strategic opportunities to increase our network capacity and efficiency through selective acquisitions of spectrum licenses.

Our network includes various elements of redundancy designed to enhance the reliability of our service. To mitigate the impact of power disruptions on our operations, we have battery backup at every switch and every macrocell in our network. We also utilize backup generators at a majority of our macrocells and at every switch location. In addition, we have a fleet of portable backup generators that can be deployed, if needed. We further enhance reliability by using a fully redundant Multiprotocol Label Switching backbone network in critical locations.

## Table of Contents

In addition to our own network coverage, we have roaming agreements with a number of wireless service providers to enable our customers to receive wireless service in nearly all other areas in the United States where wireless service is available. We also offer a variety of international wireless voice and data services to our customers through roaming arrangements with wireless service providers outside of the United States. Certain of our roaming agreements can be terminated at will by either party upon several months' notice; however, we do not believe that the termination of any of these at-will agreements would have a material adverse effect on our business.

### **Technology**

Our primary network technology platforms are 4G LTE and 3G CDMA. 4G LTE provides higher data throughput performance for data services at a lower cost compared to that offered by 3G technologies.

In 2014, we commercially launched our mobile VoLTE service. HD Calling, enabled by VoLTE, is now being used, in addition to CDMA technology, to provide voice calling services to our customers.

We are committed to developing and deploying 5G wireless technology. We are densifying our 4G LTE network to add capacity and pre-position us for 5G technology. We launched the Verizon 5G Technology Forum with key industry partners to develop 5G requirements and standards and conduct testing to accelerate the introduction of 5G technologies. We believe that 5G technology will provide higher throughput than the current 4G LTE technology, lower latency and the ability to handle more network traffic as the number of Internet-connected devices grows. Based on the outcome of our ongoing pre-commercial trials, we intend to be the first company to deploy a 5G fixed wireless broadband network in the United States. We expect to launch a fixed commercial wireless service supported by this network in 2018.

### **Spectrum**

The spectrum licenses we hold can be used for mobile wireless voice and data communications services. We have licenses to provide these wireless services on portions of the 800 MHz band, also known as cellular spectrum, the 1800-1900 MHz band, also known as Personal Communication Services (PCS) spectrum, portions of the 700 MHz upper C band and AWS spectrum in the 1700 and 2100 MHz bands, in areas that, collectively, cover nearly all of the population of the United States.

In January 2015, the Federal Communications Commission (FCC) completed an auction of 65 MHz of spectrum in the AWS-3 band. We participated in that auction and were the high bidder on 181 spectrum licenses, for which we paid cash of approximately \$10.4 billion. The FCC granted us these spectrum licenses in April 2015.

We anticipate we will need additional spectrum to meet future demand. This increasing demand is driven by growth in customer connections and the increased usage of wireless broadband services, that use more bandwidth and require ever faster rates of speed. Additional spectrum may also allow us to offer new products enabled by advances in technology, including emerging 5G and IoT services. We can meet our future spectrum needs by acquiring licenses or leasing spectrum from other licensees, or by acquiring new spectrum licenses from the FCC, if and when future FCC spectrum auctions occur. In March 2016, the FCC commenced a voluntary incentive auction of television broadcast spectrum in the 600 MHz frequency range. The auction has finished the reverse and forward clock phases. Any results will be disclosed by the FCC after the completion of the assignment phase and after the FCC announces the close of the auction by public notice.

Since we and competing wireless service providers have experienced spectrum shortages in certain markets and may have spectrum surpluses in others, from time to time we have exchanged spectrum licenses with other service providers through secondary market swap transactions. We expect to continue to pursue similar opportunities to trade spectrum licenses in order to meet certain of our capacity and expansion needs in the future. In other cases, we have entered into intra-market spectrum swaps designed to increase the amount of contiguous spectrum within frequency bands in a specific market. Contiguous spectrum improves network performance and efficiency. These swaps as well as any spectrum purchases are subject to obtaining governmental approvals for the transfer of spectrum licenses in each instance.

Additional information regarding spectrum license transactions is included in the 2016 Verizon Annual Report to Shareowners in Note 2 to the consolidated financial statements of Verizon Communications Inc. and Subsidiaries, which is incorporated by reference into this report.

### **Network Equipment and Build-out**

Nokia and Ericsson are currently our primary network vendors for our LTE network deployments for macro sites as well as small cells. Our primary CDMA cell site equipment infrastructure vendors are Nokia, which provides more than half of our CDMA cell site equipment, and Ericsson, which provides nearly all of our remaining cell site equipment. We also rely on Nokia and Ericsson for our switching equipment.

As we continue to build and upgrade our existing network, we must complete a variety of steps, including securing rights to a large number of sites as well as obtaining zoning and other governmental approvals and fiber facilities for both our macro and small cells. As we densify our network, we follow a similar process for small cells, in-building systems and antennas and related radio equipment that comprise distributed antenna systems. We utilize tower site management firms, such as Crown Castle International Corp. and American Tower Corporation (American Tower), as lessors or managers of a portion of our existing tower sites.

During March 2015, we completed a transaction with American Tower pursuant to which American Tower acquired the exclusive rights to lease and operate approximately 11,300 of our wireless towers for an upfront payment of \$5.0 billion. Under the terms of the lease agreements, American

## **Table of Contents**

Tower has exclusive rights to lease and operate towers over an average term of approximately 28 years. As the leases expire, American Tower has fixed-price purchase options to acquire these towers based on their anticipated fair market values at the end of the lease terms. As part of this transaction, we also sold 162 towers for \$0.1 billion. We have subleased capacity on the towers from American Tower for a minimum of 10 years at current market rates, with options to renew.

### **Marketing and Distribution**

Our marketing strategy is focused on offering solutions tailored to the needs of our various customer market groups; promoting our brand; leveraging our extensive distribution network; and jointly marketing our products and services to large business and government customers with Verizon's Wireline business units through the Wireless Business Group, a sales and marketing organization that encompasses all of Verizon Wireless' solutions for medium and large business and government customers. Our marketing plan includes a coordinated program of television, print, radio, outdoor signage, Internet and point-of-sale media promotions designed to present our corporate message consistently across all of our markets. We use a combination of direct, indirect and alternative distribution channels in order to increase customer growth while reducing customer acquisition costs.

Company-operated stores are a core component of our distribution strategy. We have Verizon Destination Stores in various major metropolitan areas, which focus on the mobile lifestyle and highlight the many ways consumers can use wireless technology in their daily lives. These stores are part of a broader initiative that includes the redesign of our retail stores nationwide into "Smart Stores," which showcase the same mobile lifestyle zones on a smaller scale. In addition, our direct channel includes our business-to-business sales operations and systems organization and is focused on supporting the wireless communications needs of consumers and local, regional and national business customers. In addition, we have a telemarketing sales force dedicated to handling incoming calls from customers, and we offer fully-automated, end-to-end web-based sales of wireless devices, accessories and service plans.

Our indirect channel includes agents that sell our postpaid and prepaid wireless products and services at retail locations throughout the United States, as well as through the Internet. The majority of these agents sell both our postpaid and prepaid products and services, and do so under exclusive selling arrangements with us. We also have relationships with high-profile national retailers, such as Best Buy, Wal-Mart and Target, to sell our postpaid and prepaid wireless products and services. Stores such as Dollar General and various drugstore chains sell our prepaid products and services.

### **Competition**

We operate in a highly competitive industry. We compete against other national wireless service providers, including AT&T Inc., Sprint Corporation and T-Mobile USA, Inc., as well as various regional wireless service providers. We also compete for retail activations with resellers that buy bulk wholesale service from facilities-based wireless service providers for resale, including resellers that buy from us. Competition is intense as a result of continuing increases in wireless market penetration levels, network investment by our competitors, the development and deployment of new technologies, the introduction of new products and services, new market entrants, the availability of additional spectrum, both licensed and unlicensed, and regulatory changes. Competition may also increase as smaller, stand-alone wireless service providers merge or transfer licenses to larger, better capitalized wireless service providers.

The wireless industry also faces competition from other communications and technology companies seeking to increase their brand recognition and capture customer revenue with respect to the provision of wireless products and services, in addition to non-traditional offerings in mobile data. For example, Microsoft, Google, Apple and others are offering alternative means for making wireless voice calls that, in certain cases, can be used in lieu of the wireless provider's voice service, as well as alternative means of accessing video content.

We believe that the following are the most important competitive factors in our industry:

- *Network reliability, capacity and coverage.* We believe that a wireless network that consistently provides high-quality and reliable service is a key differentiator in the U.S. market and driver of customer satisfaction. Lower prices, improved service quality and new wireless service offerings, which in many cases include video content, have led to increased customer usage of wireless services, which, in turn, puts pressure on network capacity. In order to compete effectively, wireless service providers must keep pace with network capacity needs and offer highly reliable national coverage through their networks. We believe that our investments in our 4G LTE network to increase network capacity will enable us to meet consumer demand.

- *Pricing.* Service and equipment pricing play an important role in the wireless competitive landscape. As the demand for wireless services continues to grow, we and other wireless service providers are offering service plans at competitive prices that include unlimited voice minutes and text messages and a specific amount of data access in varying megabyte or gigabyte sizes or, in some cases, on an unlimited basis subject to certain restrictions. These allowances will vary from time to time as part of promotional offers or in response to market circumstances. We and many other wireless service providers also allow customers on certain plans to carry over unused data allowances to the next billing period, or to stay online at a reduced data speed after using all of a data allowance for a billing period. In addition, some wireless service providers have bundled wireless service offerings with other products while others offer promotional pricing and incentives targeted specifically to customers of Verizon Wireless.

We and other wireless service providers, as well as equipment manufacturers, offer device payment options that distinguish service pricing from equipment pricing and blur the traditional boundary between prepaid and postpaid plans. These payment options include device payment plans.

## Table of Contents

which provide customers with the ability to pay for their device over a period of time, and device leasing arrangements. Historically, wireless service providers offered customers wireless plans whereby, in exchange for the customer entering into a fixed-term service agreement, the wireless service provider significantly, and in some cases fully, subsidized the customer's device purchase. Wireless providers recovered those subsidies through higher service fees as compared to those paid by customers on device payment plans. We and many other wireless providers have limited or discontinued this form of device subsidy.

- *Customer service.* We believe that high-quality customer service is a key factor in retaining customers and attracting new customers, including those of other wireless providers. Our customer service, retention and satisfaction programs are based on providing customers with convenient and easy-to-use products and services and focusing on their needs in order to promote long-term relationships and minimize churn. Our competitors also recognize the importance of customer service and are also focused on improving in this area. As part of our efforts to transform and simplify the customer experience, we launched a new My Verizon app, which allows customers to manage their price plan, data usage, account and billing from their device. As part of our efforts to promote long-term relationships with our customers, we offer Verizon Smart Rewards, which is a program that offers a wide variety of rewards to customers in exchange for points they earn in connection with their account-related interactions with Verizon Wireless. The program offers customers discounts and savings on merchandise from well-known brands, as well as discounts and other offers at local shopping and dining venues.
- *Product and service development.* As wireless technologies develop and wireless broadband networks proliferate, continued customer and revenue growth will be increasingly dependent on the development of new and enhanced data products and services. We continue to pursue the development and rapid deployment of new and innovative wireless products and services both independently and in collaboration with application and content providers. We also collaborate with various device manufacturers in the development of distinctive smartphones and other wireless devices that can access the growing array of data applications and content available over the Internet. We continue to focus on increasing the penetration of smartphones, tablets and other connected devices throughout our customer base.
- *Sales and distribution.* The key to achieving sales success in the wireless industry is the reach and quality of sales channels and distribution points. We believe that attaining the optimal combination of varying distribution channels is important to achieving industry-leading profitability, as measured by operating income. We endeavor to increase sales through our company-operated stores, outside sales teams and telemarketing, web-based sales and fulfillment capabilities, our extensive indirect distribution network of retail outlets and prepaid replenishment locations, and through manufacturers of laptops and netbooks with embedded 4G LTE and 3G modules that can access the Internet on our network at broadband speeds. In addition, we sell network access to both traditional resellers, which resell network services to their end-users, and to various companies to enable wireless communications for their IoT devices or services.
- *Capital resources.* In order to expand the capacity and coverage of their networks and introduce new products and services, wireless service providers require significant capital resources. We generate significant cash flow from operations, as do some of our competitors.

Our success will depend on our ability to anticipate and respond to various factors affecting the wireless industry, including the factors described above, as well as new technologies, new business models, changes in customer preferences, regulatory changes, demographic trends, economic conditions and pricing strategies of competitors.

### **Wireline**

#### **Background**

Our Wireline segment provides voice, data and video communications products and enhanced services. We provide these products and services to consumers in the United States, as well as to carriers, businesses and government customers both in the United States and around the world. In 2016, Wireline revenues were \$31.3 billion, representing approximately 25% of Verizon's aggregate revenues.

#### **Strategic Transactions**

On February 5, 2015, we entered into a definitive agreement with Frontier Communications Corporation (Frontier) pursuant to which Verizon sold its local exchange business and related landline activities in California, Florida and Texas, including Fios Internet and video customers, switched and special access lines and high-speed Internet service and long distance voice accounts in these three states, for approximately \$10.5 billion (approximately \$7.3 billion net of income taxes), subject to certain adjustments and including the assumption of \$0.6 billion of indebtedness from Verizon by Frontier. The transaction, which included the acquisition by Frontier of the equity interests of Verizon's incumbent local exchange carriers (ILECs) in California, Florida and Texas, did not involve any assets or liabilities of Verizon Wireless. The transaction closed on April 1, 2016.

The transaction resulted in Frontier acquiring approximately 3.3 million voice connections, 1.6 million Fios Internet subscribers, 1.2 million Fios video subscribers and the related ILEC businesses from Verizon. Approximately 9,300 Verizon employees who served customers in California, Florida and Texas continued employment with Frontier. The operating results of these businesses are excluded from our Wireline segment for all periods presented to reflect comparable segment operating results consistent with the information regularly reviewed by our chief operating decision maker.

## Table of Contents

On February 20, 2016, we entered into a purchase agreement to acquire XO Holdings' wireline business, which owns and operates one of the largest fiber-based IP and Ethernet networks, for approximately \$1.8 billion, subject to adjustment. We completed the acquisition on February 1, 2017. Separately, we entered into an agreement to lease certain wireless spectrum from a wholly-owned subsidiary of XO Holdings that holds its wireless spectrum. Verizon has an option, exercisable under certain circumstances, to buy that subsidiary.

We are reinventing our network architecture around a common fiber platform that will support both our wireless and wireline technologies. We expect that this new "One Fiber" architecture will improve our 4G LTE coverage, speed the deployment of 5G, deliver high-speed Fios broadband to homes and businesses and create new opportunities in the small and medium business market. In April 2016, we announced our One Fiber strategy for the city of Boston. We launched One Fiber for consumer and business services to customers in Boston late in 2016.

On December 6, 2016, we entered into a definitive agreement with Equinix, Inc. pursuant to which Verizon will sell 24 customer-facing data center sites in the United States and Latin America for approximately \$3.6 billion, subject to certain adjustments. The sale does not affect Verizon's data center services delivered from 27 sites in Europe, Asia-Pacific and Canada, or its managed hosting and cloud offerings. The transaction is subject to customary regulatory approvals and closing conditions, and is expected to close during the first half of 2017.

### **Wireline Service and Product Offerings**

We organize our service and product offerings by the primary customers targeted by these offerings – mass markets, global enterprise and global wholesale.

#### ***Mass Markets***

Mass Markets operations provide broadband Internet and video services (including high-speed Internet, Fios Internet and Fios video services), and local exchange (basic service and end-user access) and long distance (including regional toll) voice services to residential and small business subscribers. In 2016, Mass Markets revenues were \$14.4 billion, representing approximately 46% of Wireline's aggregate revenues.

*Internet services.* We offer Fios Internet and high-speed Internet services with varying throughput speeds. We believe that as consumers connect more devices and stream more video, they will require increased broadband speeds. With our Fios Quantum broadband service and certain other data services, our customers can achieve symmetrical upload and download speeds of up to 500 Mbps, and we recently launched our Instant Internet service, which allows customers in certain markets to achieve symmetrical upload and download speeds of 750 Mbps and higher. As more data storage and, in some cases, processing is moved to the cloud, we believe that customers will place an increasing value on upstream performance that matches what they already receive for downloads.

*Video services.* We offer video service over our fiber-optic network. As of December 31, 2016, Fios video services were available to approximately 14 million homes across 9 states, as well as the District of Columbia. We have several offerings available to our Fios TV customers, including:

- *Fios Quantum TV*, which provides customers the ability to record up to 12 shows at once and control live TV from any room in their home;
- *Fios Custom TV*, which provides customers local versions of the Fox, CBS, NBCU, and ABC broadcast stations and other similar local content and offers customers the option of purchasing an Essentials plan that includes a base set of lifestyle, entertainment, pop culture and content for children and national news networks, or a Sports and More plan that includes national and regional sports networks as well as non-sports national networks. Customers can add more sets of categorized channels to their Custom TV package for an additional monthly fee; and
- *Fios on Demand*, which gives Fios customers the ability to watch content virtually anytime and anywhere, on any compatible device. Customers who subscribe to Fios Internet and video service also have the ability to upload their photos, music and videos to their personal Fios on Demand Library, which gives them access to this content via various data-capable devices. With the Fios Mobile App, programming, such as ESPN, TNT, Nickelodeon, HBO and TBS, can be streamed to a customer's tablet or other mobile device.

We continue to partner with major corporations to offer further interoperability with various products such as video game consoles, smart televisions and tablets. This technology further expands our initiative to provide customers with the ability to watch content anytime and anywhere on any data-capable device.

*Voice services.* We offer voice services that include local exchange, regional and long distance calling and voice messaging services, as well as Voice over Internet protocol (VoIP) services, which use the Internet or private broadband networks to transmit voice

communications.

**Global Enterprise**

Global Enterprise offers strategic services and other core communications services to medium and large business customers, including multinational corporations, as well as state and federal government customers. Global Enterprise markets these services through Verizon Enterprise Solutions. In 2016, Global Enterprise revenues were \$11.6 billion, representing approximately 37% of Wireline's aggregate revenues.

Verizon Enterprise Solutions offers an array of advanced information and communication technology services, including Global Internet Protocol (IP) network, cloud and IT solutions, and business communications, IoT, data, security and mobility services.

- *Network products and solutions* – These products and solutions primarily include our Private IP, Public Internet, Ethernet and optical networking services. Our Private IP service enables customers around the world to communicate over a virtual private network using a variety of access methods, including Ethernet and Verizon Wireless 4G LTE. Our Public Internet services provide Internet connectivity through a variety of low and high-speed options. Our Ethernet portfolio includes access services that allow customers to connect network environments around the world and enable applications and technologies to work seamlessly and with little disruption, as well as local and long distance layer 2 services that include Metro local area network (LAN), long distance switched and dedicated architectures. Optical networking services include technologies that help customers handle bandwidth demands and control their costs.

## Table of Contents

- *IT solutions and cloud services* – Our IT solutions and cloud services are built to help our enterprise customers drive innovation and business growth. We offer IT infrastructure services that include colocation and managed hosting in data centers around the globe. Our cloud services include computing, storage, backup, recovery and application platforms our customers rely on to run their business operations.
- *Business communications services* – Business communications services primarily include IP communications services, which simplify network management and drive operational efficiencies by enabling the convergence of voice and data traffic on the same access connection; dedicated Internet access, which provides enterprise customers with high-bandwidth dedicated access to Verizon's global network; unified communications and collaboration capabilities, which enable customers to communicate in real-time through VoIP and IP conferencing, and emergency communication services, which allow customers to respond effectively to emergencies while maintaining business continuity.
- *Security services* – We offer a suite of data security services to help companies secure their networks, data, applications and infrastructure from security threats while building customer trust and confidence.
- *Core services* – Core services include core voice and data services, which consist of a comprehensive portfolio of global solutions utilizing traditional telecommunications technology, such as conferencing and contact center solutions, and private line and data access networks. Core services also include providing customer premise equipment, and installation, maintenance and site services. We are continuing to transition customers out of copper-based legacy voice and data services to fiber services, including IP and Ethernet.

### **Global Wholesale**

Global Wholesale provides communications services, including data, voice, local dial tone and broadband services, primarily to local, long distance, wireless and other carriers that use our facilities to provide services to their customers. In 2016, Global Wholesale revenues were \$5.0 billion, representing approximately 16% of Wireline's aggregate revenues. A portion of Global Wholesale revenues are generated by a few large telecommunications companies, most of which compete directly with us.

Global Wholesale provides the following services, which it jointly markets with Verizon's other business units through Verizon Enterprise Solutions:

- *Data services.* We offer a robust portfolio of data services with varying speeds and options to enhance our wholesale customers' networks and provide connections to their end-users and subscribers. Our data services include high-speed digital data offerings, such as Ethernet and Wavelength services, as well as core data circuits, such as DS1s and DS3s. In addition, we receive revenue from data services that is generated from carriers that buy dedicated local exchange capacity to support their private networks.

Data services also include certain value-added business services, which leverage many of the same offerings available in the Global Enterprise portfolio, including:

- *Managed services*, which offer wholesale customers security, remote access, web applications and the opportunity to outsource the management of their networks to Verizon;
  - *Mobility offerings*, which enable wholesale customers to enhance their portfolio to triple-play or quad-play capability by leveraging wireless devices and services offered through Verizon Wireless that can be packaged and resold under their own carrier brand; and
  - *Security services*, which provide wholesale customers integrated solutions to help their enterprise end-users secure their networks and data.
- *Voice services.* We provide switched access services that allow carriers to complete their end-user calls that originate or terminate within our territory. In addition, we provide originating and terminating voice services throughout the United States and globally utilizing our time-division multiplexing (TDM) and VoIP networks.
  - *Local services.* We offer an array of local dial tone and broadband services to competitive local exchange carriers, some of which are offered to comply with telecommunications regulations. In addition, we offer services such as colocation, resale and unbundled network elements in compliance with applicable regulations.

### **Network**

Verizon operates a large and advanced telecommunications network in the United States and around the world to provide services and solutions to its customers.

- *Fios.* Our fiber-to-the-home network through which we provide our Fios residential broadband service has passed over 16.9 million premises in the United States as of December 31, 2016. Residential broadband service has seen significant growth in bandwidth demand over the past several years, and we believe that demand will continue to grow. The continued emergence of new video services, new data applications and the proliferation of IP devices in the home will continue to drive new network requirements for increased data speeds and throughput. We believe that the Passive Optical Network (PON) technology underpinning Fios makes us well positioned to meet these demands in a cost effective and efficient manner. Our PON technology provides the flexibility to adapt our network to deliver increased data speeds and new services without major overhauls or replacements to the fiber-optic infrastructure.

## Table of Contents

While deployed initially as a consumer broadband network, the PON infrastructure is also finding more widespread application in the enterprise sector, especially as businesses increasingly migrate to Ethernet-based access services.

- *Global IP.* Verizon owns and operates one of the largest global fiber networks in the world, providing connectivity to business customers in more than 150 countries. Our global IP network includes long haul, metro and submarine assets that span over 800,000 route miles and enable and support far reaching international operations.

Global business is rapidly evolving to an “everything-as-a-service” model in which business customers seek cloud-based, converged enterprise solutions delivered securely via managed and professional services. With the continued deployment of packet optical transport strategy, Verizon is creating a single, high-capacity global network platform that combines optical transport with advanced packet switching technology. The result is a global IP network that can offer powerful solutions to these service demands.

We believe that our continued focus on enhancing our domestic and global fiber-based networks, and achieving cost efficient solutions through new technology deployments, will help Verizon advance its position as a provider of choice to residential and enterprise customers.

## **Competition**

The wireline telecommunications industry is highly competitive. We expect competition to intensify further with traditional, non-traditional and emerging players seeking increased market share. Current and potential competitors include cable companies, wireless service providers, domestic and foreign telecommunications providers, satellite television companies, Internet service providers and other companies that offer network services and managed enterprise solutions.

In addition, companies with a global presence increasingly compete with our wireline businesses. A relatively small number of telecommunications and integrated service providers with global operations serve customers in the global enterprise and, to a lesser extent, the global wholesale markets. We compete with these providers for large contracts to provide integrated services to global enterprises. Many of these companies have strong market presence, brand recognition and existing customer relationships, all of which contribute to intensifying competition that may affect our future revenue growth.

We believe the following are the most important competitive factors and trends in the wireline industry:

- *Bandwidth (speed) and network reliability:* Consumers and small business customers are seeking to leverage high-speed connections for entertainment, communications and productivity. As online and online-enabled activities increase, so will bandwidth requirements, both downstream and upstream. To succeed, we and other network-based providers must ensure that our networks can meet these increasing bandwidth requirements. In addition, network reliability and security are increasingly important competitive factors in the global enterprise market. We continue to invest in our network to be able to meet growing bandwidth demand and provide the most reliable and secure network.
- *Pricing:* Cable operators, telecommunications companies and integrated service providers use pricing to capture market share from incumbents. Pricing is also a significant factor as non-traditional modes of providing communication services emerge and new entrants compete for customers. For example, VoIP and portal-based calling is free or nearly free to customers and is often supported by advertising revenues.
- *Customer service:* Customers expect industry-leading service from their service providers. As technologies and services evolve, the ability to excel in this area is important for customer acquisition and retention. In Mass Markets, we compete in this area through our service representatives and online support. In Global Enterprise, we provide our customers with ready access to their system and performance information, and we conduct proactive testing of our network to identify issues before they affect customers. In the Global Wholesale business, we believe service improvement can be achieved through continued system automation initiatives.
- *Product differentiation:* As a result of pricing pressures, providers need to differentiate their products and services. Customers are shifting their focus from access to applications and are seeking ways to leverage their broadband and video connections. Converged features, such as integrated wireless and wireline functionality, are becoming similarly important, driven by both customer demand and technological advancement.
- *Innovation:* The delivery of new and innovative products and services has been accelerating. To compete effectively, providers need to continuously review, improve and refine their product portfolio and develop and rapidly deploy new products and services tailored to the needs of the customer.

## Table of Contents

In the Mass Markets business, cable operators are significant competitors. Cable operators have increased the size and capacity of their networks in order to offer digital products and services. We continue to market competitive bundled offerings that include high-speed Internet access, digital television and voice services. Several major cable operators also offer bundles with wireless services through strategic relationships.

We expect customer migration from traditional voice services to wireless services to continue as a growing number of customers place greater value on mobility and wireless companies position their service as a landline alternative. We also face increasing competition from cable companies and other providers of VoIP services as well as Internet portal providers. In addition, customers have more choices for obtaining video content from various online services and that content can be accessed on a TV, computer, tablet or mobile phone.

In the global enterprise market, the customer's need to reduce technical complexity coupled with the growth opportunity created by technology convergence is driving the expansion of the competitive landscape. Major competitors include system integrators, carriers and hardware and software providers. Some of the biggest companies in IT services are making strategic acquisitions, divesting non-strategic assets or forging new alliances to be better positioned for a rebound in technology spending. Many new alliances and acquisitions have focused on emerging fields such as cloud computing, software delivery, communication applications and other computing tasks via the network, rather than on in-house machines. Carriers have also utilized acquisitions to make significant inroads into enterprise outsourcing markets that have long been dominated by the major IT outsourcers.

Global Wholesale competes with traditional carriers for long-haul, voice and IP services. In addition, mobile video and data needs are driving a greater need for wireless backhaul. Network providers, cable companies and niche players are competitors for this new revenue opportunity.

We also compete with competitive local exchange carriers (CLECs). Our telephone operations generally have been required to sell their services to CLECs at significant discounts from the prices our telephone operations charge their retail customers.

### **New Product Development and Strategic Initiatives**

Technology developments, interconnected markets, shifting consumer needs and converging industry ecosystems are creating innovative opportunities for Verizon. We are transforming around the capabilities of our high-performing networks, with a goal of future growth based on delivering what customers want and need in the new digital world. Our three tier strategy is to lead at the network connectivity level in the markets we serve, develop new business models through global platforms in digital media and IoT and deliver solutions to key industry segments for incremental monetization. To execute this strategy, we have created an organization devoted to the development of new products and the cultivation of new businesses. This organization is focused on leveraging all of our assets to create innovative products and services that can provide our customers with integrated solutions that address their needs. Several strategic initiatives have been undertaken by this organization in the areas of digital media, interactive entertainment and IoT and telematics products and services.

As a market leader in offering differentiated solutions to our connected customers across their devices at home, at work and on the go, Verizon will continue to focus on strategic partnerships as an important pillar of our future strategy. Strategic partnerships are aimed at complementing and augmenting our strengths, expanding our addressable market, accelerating our pace of innovation, enabling faster delivery of solutions such as media and IoT to the marketplace and, where possible, lowering our market and execution risk. Strong partnerships are expected to further our efforts to offer comprehensive solutions for our customers. We look to formulate strategic partnerships and alliances with a global orientation, which we believe will benefit us in terms of technology sourcing, content acquisition, consumer insights and application ecosystems.

We believe these investments will assist us in bringing innovative next generation products and services to market and uncovering new sources of revenue, increasing revenue from existing projects and leveraging our strengths across the company.

### **Digital Media and Interactive Entertainment**

Verizon has been investing in emerging technology that taps into the market shift to digital content and advertising. We have been investing in video assets and capabilities with a goal of building a global platform and developing new business models for reaching the digital video customer. We believe the growth in video consumption using mobile devices provides us with an opportunity for revenue growth. Through various acquisitions and investments and the launch of video streaming products and services, we are expanding the ways in which we can deliver content to our customers, including the following:

- In June 2015, we completed our acquisition of AOL Inc. (AOL), a leader in digital content and advertising. AOL's business model aligns with our approach, and we believe that its combination of owned and operated content properties plus a digital advertising platform enhances our ability to further develop future revenue streams. During 2015, we also acquired Millennial Media, an advertising technology business.

- In July 2016, we entered into a stock purchase agreement (the Purchase Agreement) with Yahoo! Inc. (Yahoo). Pursuant to the Purchase Agreement, upon the terms and subject to the conditions thereof, we agreed to acquire the stock of one or more subsidiaries of Yahoo holding all of Yahoo's operating business, for approximately \$4.83 billion in cash, subject to certain adjustments (the Transaction). On February 20, 2017, we entered into an amendment to the Purchase Agreement, pursuant to which, among other things, the Transaction purchase price will be reduced by \$350 million to approximately \$4.48 billion in cash, subject to certain adjustments. The Transaction is expected to provide us with a valuable portfolio of online properties and mobile applications, including market leading content in sports, finance, news and email services, which have attracted over one billion monthly active consumer views. The Transaction is expected to also expand our analytics and ad tech capabilities and enhance our competitive position and value proposition to advertisers. Additional discussion of the Transaction is included in the 2016 Verizon Annual Report to Shareowners in Note 2 to the consolidated financial statements of Verizon Communications Inc. and Subsidiaries, which is incorporated by reference into this report.

## **Table of Contents**

- In 2015, we launched go90, a mobile-first social entertainment platform that provides the opportunity for ad-supported mobile video streaming as well as subscription-based services. Digital content available on the go90 platform includes live events, popular web and television content and original content. In 2016, we introduced StreamPass, which offers streaming of live sports through go90 free of data charges to Verizon Wireless customers on certain data plans. We also introduced FreeBee Data, a sponsored data service that enables content providers to provide our customers with access to some or all of the provider's mobile content or to sponsor specific consumer actions on a per-click basis, free of data charges to the customer.
- We have made investments in converging technologies and services involving content delivery networks (CDNs), video streaming and related consumer hardware to leverage new content models. Our wireless network enables us to move towards a unified video strategy that positions us to take advantage of this growth opportunity. We began using Multimedia Broadcast Multicast Service technology to develop our LTE Multicast service, which we use to deliver live events in go90. This service has the potential to enhance our network efficiency and provide our customers with access to live streaming video content with virtually no buffering, regardless of the number of devices using the service. We also believe it is important to have rights to deliver content over a wireless network that do not require an authentication back to a subscription agreement. For example, our NFL agreement allows our customers to access certain games live on our 4G LTE network without authenticating back to any subscription.
- We continue to invest in Verizon Digital Media Services, which offers a scalable platform for delivering content, including live broadcasts, video on demand, games, software and websites, to our customers on their devices at any time. As the digital platform reshapes the delivery of media and entertainment content, there is an increasing need for a stable, high-quality video delivery platform. We are focused on providing a simple end-to-end global platform for the delivery of media to customers, which we believe will be superior to that offered by the existing and highly fragmented media delivery ecosystem. This platform is targeted at media and entertainment companies and other businesses focused on delivering their digital products and services through the Internet. We also expect, through this platform, to further integrate our Fios and wireless offerings.
- During 2016, we established Verizon Hearst Media Partners, LLC, a content joint venture with Hearst Entertainment & Syndication (Hearst), to build new multiplatform digital video channels targeted to the mobile millennial audience. In partnership with Hearst, we have also invested in two media companies, AwesomenessTV Holdings, LLC and Complex Media, Inc. & CM Partners, LLC, which are leaders in producing content targeted at key demographics, in order to further diversify our content and distribution businesses within our digital media portfolio.

## **Internet of Things and Telematics**

The adoption of IoT technology continues to grow as companies across a wide range of industries are leveraging IoT technologies to increase efficiency, gain better customer insights, facilitate compliance with regulations and build new business models. Although IoT growth is expanding broadly, adoption is particularly strong in the telematics and transportation industries, as well as the fields of smart communities, healthcare, utilities and energy management. We are building our growth capabilities in the IoT market by developing business models that monetize usage on our network at the connectivity, platform and solution layers. For example, we have developed IoT solutions that address key market needs for electric and other utilities, farms and other purveyors of food and agriculture, drug companies and others with complex supply chains. In addition, our IoT customers can turn the data that our solutions provide into actionable opportunities to develop new services and create revenue growth.

Our strategy to simplify IoT technology and accelerate its adoption also includes ThingSpace, an IoT platform. ThingSpace is designed to help developers create, test, manage and market IoT-based solutions aimed at major vertical markets, such as energy, health care and connected cities. ThingSpace comes with a portal that includes immediate access to dedicated application programming interfaces and partner development kits. In October 2016, we acquired Sensity Systems, Inc., a leading provider of IoT solutions for smart communities, in order to add a leading comprehensive suite of smart city solutions.

Through Verizon Telematics, we provide connectivity and telematics services and applications to manufacturers such as Mercedes-Benz and help businesses manage large vehicle fleets more efficiently. Our suite of real-time vehicle communications services and applications connects automobiles with content services and call centers. Our platform enables factory and aftermarket-installed automotive safety and security features as well as location-based services and vehicle diagnostics. We provide usage-based data services to new vehicles in the United States, China and Europe. Our Verizon Telematics solution provides commercial fleet managers throughout North America with real-time access to data that yields operational efficiencies, increased vehicle reliability and improved driver safety. We also provide this service to over 23,000 vehicles operated by Verizon.

In 2015, we introduced hum, an aftermarket vehicle technology and subscription service. This subscription-based service provides consumers with diagnostic technology in their vehicles, access to live assistance and roadside assistance with GPS accuracy when needed. Our hum service also offers the ability to connect with a certified mechanic to diagnose potential problems and offer solutions.

In 2016, we acquired Fleetmatics Group PLC, a global provider of fleet and mobile workforce management solutions, and Telogis, Inc., a global, cloud-based mobile enterprise management software company. We expect these acquisitions to advance our fleet telematics solutions, expand our distribution relationships and position our telematics business as a leading provider of fleet and mobile workforce management solutions globally.

## **Table of Contents**

### **Patents, Trademarks and Licenses**

We own or have licenses to various patents, copyrights, trademarks, domain names and other intellectual property rights necessary to conduct our business. We actively pursue the filing and registration of patents, copyrights, domain names, trademarks and service marks to protect our intellectual property rights within the United States and abroad. We also actively grant licenses, in exchange for appropriate fees or other consideration and subject to appropriate safeguards and restrictions, to other companies that enable them to utilize certain of our intellectual property rights and proprietary technology as part of their products and services. Such licenses enable the licensees to take advantage of the results of Verizon's research and development efforts. While these licenses result in valuable consideration being paid to us, we do not believe that the loss of such consideration, or the expiration of any of our intellectual property rights, would have a material effect on our results of operations.

We periodically receive offers from third parties to purchase or obtain licenses for patents and other intellectual property rights in exchange for royalties or other payments. We also periodically receive notices alleging that our products or services infringe on third-party patents or other intellectual property rights. These claims, whether against us directly or against third-party suppliers of products or services that we, in turn, sell to our customers, if successful, could require us to pay damages or royalties, or cease offering the relevant products or services.

### **Acquisitions and Divestitures**

Information about our acquisitions and divestitures is included in the 2016 Verizon Annual Report to Shareowners under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations - Acquisitions and Divestitures", which is incorporated by reference into this report.

### **Regulatory and Competitive Trends**

#### **Regulatory and Competitive Landscape**

Verizon operates in a regulated and highly competitive market. Current and potential competitors include other voice and data service providers such as other wireless companies, traditional telephone companies, cable companies, Internet service providers, software and application providers, and other non-traditional companies. Many of these companies have strong market presence, brand recognition and existing customer relationships, all of which contribute to intensifying competition that may affect our future revenue growth. Some of our competitors also are subject to fewer regulatory constraints than Verizon. For many services offered by Verizon, the FCC is our primary regulator. The FCC has jurisdiction over interstate telecommunications services and other matters under the Communications Act of 1934, as amended (Communications Act or Act). Other Verizon services are subject to state and local regulation.

#### **Federal Regulation**

##### *Wireless Services*

The FCC regulates several aspects of our wireless operations. Generally, the FCC has jurisdiction over the construction, operation, acquisition and transfer of wireless communications systems. All wireless services require use of radio frequency spectrum, the assignment and distribution of which is subject to FCC oversight. Verizon anticipates that it will need additional spectrum to meet future demand. We can meet our needs for licensed spectrum by purchasing licenses or leasing spectrum from others, or by participating in a competitive bidding process to acquire new spectrum from the FCC. Those processes are subject to certain reviews, approvals and potential conditions.

Today, Verizon holds FCC spectrum licenses that allow it to provide a wide range of mobile and fixed communications services, including both voice and data services. FCC spectrum licenses typically have a term of 10 years, at which time they are subject to renewal. While the FCC has routinely renewed all of Verizon's wireless licenses, challenges could be raised in the future. If a wireless license was revoked or not renewed, Verizon would not be permitted to provide services on the spectrum covered by that license. Some of our licenses require us to comply with so-called "open access" FCC regulations, which generally require licensees of particular spectrum to allow customers to use devices and applications of their choice, subject to certain technical limitations. The FCC has also imposed certain specific mandates on wireless carriers, including construction and geographic coverage requirements, technical operating standards, provision of enhanced 911 services, roaming obligations and requirements for wireless tower and antenna facilities.

##### *Broadband*

Verizon offers many different broadband services. Traditionally, the FCC recognized that broadband Internet access services as "information services" subject to a "light touch" regulatory approach rather than to the traditional, utilities-style regulations. In 2015, the FCC reversed course and declared that broadband Internet access services are "telecommunications services" subject to common carriage regulation under Title II of the Communications Act. This decision created uncertainty concerning the level of regulation that will apply to

broadband services. It created a risk that such regulation would limit the ways that broadband Internet access service providers structure their business arrangements and manage their networks and could spur additional restrictions, including rate regulation, that could adversely affect broadband investment and innovation. The FCC's decision was affirmed by the United States Court of Appeals, but may be subject to further challenge in the courts. In addition, Congress and the FCC are likely to continue to debate the proper scope of such regulations. Regardless of regulation, Verizon remains committed to the open Internet which provides consumers with competitive choices and unblocked access to lawful websites and content when, where, and how they want, and our commitment to our customers can be found on our website at <http://responsibility.verizon.com/broadband-commitment>.

## **Table of Contents**

### *Wireline Voice*

Verizon offers many different wireline voice services, including traditional telephone service and other services that rely on technologies such as VoIP. For regulatory purposes, legacy telephone services are generally considered to be “common carrier” services. Common carrier services are subject to heightened regulatory oversight with respect to rates, terms and conditions and other aspects of the services. The FCC has not decided the regulatory classification of VoIP but has said VoIP service providers must comply with certain rules, such as 911 capabilities and law enforcement assistance requirements.

### *Video*

Verizon offers a multichannel video service that is regulated like traditional cable service. The FCC has a body of rules that apply to cable operators, and these rules also generally apply to Verizon. In areas where Verizon offers its facilities-based multichannel video services, Verizon has typically been required to obtain a franchise from local authorities.

### *Privacy and Data Security*

We are subject to federal, state and international laws and regulations relating to privacy and data security that impact all parts of our business, including voice, wireless, broadband and the development and roll out of new products, such as those in the IoT space. At the federal level, much of our business is subject to the FCC’s privacy and data security requirements. In November 2016, the FCC released new privacy and data security rules that will apply to all telecommunications services, including our fixed and mobile voice and broadband services. Other parts of our business are subject to the privacy and data security oversight of other federal regulators, including the Federal Trade Commission. Generally, attention to privacy and data security requirements is increasing at both the state and federal level. In addition, a new data protection regulation will go into effect in Europe in May 2018 that includes significant penalties for non-compliance.

### *Public Safety and Cybersecurity*

The FCC has played a role in addressing public safety concerns by regulating emergency communications services and mandating widespread availability of both media (broadcast/cable) and wireless emergency alerting services. In response to recent cyber attacks, however, the FCC or other regulators may attempt to increase regulation of the cybersecurity practices of providers.

### *Inter-carrier Compensation and Network Access*

The FCC regulates some of the rates that carriers pay each other for the exchange of voice traffic (particularly traditional wireline traffic) over different networks and other aspects of interconnection for some voice services. The FCC also regulates some of the rates and terms and conditions for certain wireline “business data services” and other services and network facilities. Verizon is both a seller and a buyer of these services, and both makes and receives interconnection payments. The FCC has focused in recent years on whether changes in the rates, terms and conditions for both the exchange of traffic and for business data services may be appropriate.

## **State Regulation and Local Regulation**

### *Wireless Services*

The Act generally preempts regulation by state and local governments of the entry of, or the rates charged by, wireless carriers. The Act does not prohibit states from regulating the other “terms and conditions” of wireless service. For example, some states attempt to regulate wireless customer billing matters and impose reporting requirements. Several states also have laws or regulations that address safety issues (e.g., use of wireless handsets while driving) and taxation matters. In addition, wireless tower and antenna facilities are often subject to state and local zoning and land use regulation, and securing approvals for new or modified facilities is often a lengthy and expensive process.

### *Wireline Services*

State public utility commissions regulate Verizon’s telephone operations with respect to certain telecommunications intrastate matters. Verizon operates as an “incumbent local exchange carrier” in nine states and the District of Columbia. These incumbent operations are subject to various levels of pricing flexibility and other state oversight and requirements. Verizon also has other wireline operations that are more lightly regulated. In addition, as a video services operator in many states, Verizon has been required to obtain a cable franchise from local government entities, or in some cases a state-wide franchise, and comply with certain one-time and ongoing obligations, as a result.

**Table of Contents****Environmental Matters**

Reserves have been established to cover environmental matters relating to discontinued businesses and past telecommunications activities. These reserves include funds to address contamination at the site of a former Sylvania facility in Hicksville, NY, which had processed nuclear fuel rods in the 1950s and 1960s. In September 2005, the Army Corps of Engineers (ACE) accepted the site into its Formerly Utilized Sites Remedial Action Program. As a result, the ACE has taken primary responsibility for addressing the contamination at the site. An adjustment to the reserves may be made after a cost allocation is conducted with respect to the past and future expenses of all of the parties. Adjustments to the environmental reserve may also be made based upon the actual conditions found at other sites requiring remediation.

**Executive Officers**

See Part III, Item 10. "Directors, Executive Officers and Corporate Governance" of this Annual Report on Form 10-K for information about our executive officers.

**Employees**

As of December 31, 2016, Verizon and its subsidiaries had approximately 160,900 employees. Unions represent approximately 23% of our employees.

**Information on Our Internet Website**

We make available, free of charge on our website, our annual reports on Form 10-K and Form SD, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports at <http://www.verizon.com/about/investors>.

## Table of Contents

### **Cautionary Statement Concerning Forward-Looking Statements**

In this report we have made forward-looking statements. These statements are based on our estimates and assumptions and are subject to risks and uncertainties. Forward-looking statements include the information concerning our possible or assumed future results of operations. Forward-looking statements also include those preceded or followed by the words "anticipates," "believes," "estimates," "hopes" or similar expressions. For those statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

The following important factors, along with those discussed elsewhere in this report and in other filings with the Securities and Exchange Commission (SEC), could affect future results and could cause those results to differ materially from those expressed in the forward-looking statements:

- adverse conditions in the U.S. and international economies;
- the effects of competition in the markets in which we operate;
- material changes in technology or technology substitution;
- disruption of our key suppliers' provisioning of products or services;
- changes in the regulatory environment in which we operate, including any increase in restrictions on our ability to operate our networks;
- breaches of network or information technology security, natural disasters, terrorist attacks or acts of war or significant litigation and any resulting financial impact not covered by insurance;
- our high level of indebtedness;
- an adverse change in the ratings afforded our debt securities by nationally accredited ratings organizations or adverse conditions in the credit markets affecting the cost, including interest rates, and/or availability of further financing;
- material adverse changes in labor matters, including labor negotiations, and any resulting financial and/or operational impact;
- significant increases in benefit plan costs or lower investment returns on plan assets;
- changes in tax laws or treaties, or in their interpretation;
- changes in accounting assumptions that regulatory agencies, including the SEC, may require or that result from changes in the accounting rules or their application, which could result in an impact on earnings;
- the inability to implement our business strategies; and
- the inability to realize the expected benefits of strategic transactions.

## **Table of Contents**

### *Item 1A. Risk Factors*

*The following discussion of "Risk Factors" identifies the most significant factors that may adversely affect our business, operations, financial condition or future performance. This information should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Result of Operations" and the consolidated financial statements and related notes. The following discussion of risks is not all-inclusive but is designed to highlight what we believe are important factors to consider when evaluating our business and expectations. These factors could cause our future results to differ materially from our historical results and from expectations reflected in forward-looking statements.*

#### ***Adverse conditions in the U.S. and international economies could impact our results of operations.***

Unfavorable economic conditions, such as a recession or economic slowdown in the United States or elsewhere, could negatively affect the affordability of and demand for some of our products and services. In difficult economic conditions, consumers may seek to reduce discretionary spending by forgoing purchases of our products, electing to use fewer higher margin services or obtaining lower-cost products and services offered by other companies. Similarly, under these conditions, the business customers that we serve may delay purchasing decisions, delay full implementation of service offerings or reduce their use of services. In addition, adverse economic conditions may lead to an increased number of our consumer and business customers that are unable to pay for services. If these events were to occur, it could have a material adverse effect on our results of operations.

#### ***We face significant competition that may reduce our profits.***

We face significant competition in our industry. The rapid development of new technologies, services and products has eliminated many of the traditional distinctions among wireless, cable, Internet, local and long distance communication services and brought new competitors to our markets, including other telephone companies, cable companies, wireless service providers, satellite providers, application and device providers and providers of VoIP services. While these changes have enabled us to offer new types of products and services, they have also allowed other providers to broaden the scope of their own competitive offerings. In addition, wireless service providers are significantly altering the financial relationships with their customers through commercial offers that vary service and device pricing, promotions, incentives and levels of service provided – in some cases specifically targeting Verizon Wireless customers. Our ability to compete effectively will depend on, among other things, our network quality, capacity and coverage, the pricing of our products and services, the quality of our customer service, our development of new and enhanced products and services, the reach and quality of our sales and distribution channels and our capital resources. It will also depend on how successfully we anticipate and respond to various factors affecting our industry, including new technologies and business models, changes in consumer preferences and demand for existing services, demographic trends and economic conditions. If we are not able to respond successfully to these competitive challenges, we could experience reduced profits.

#### ***If we are not able to adapt to changes and disruptions in technology and address changing consumer demand on a timely basis, we may experience a decline in the demand for our services, be unable to implement our business strategy and experience reduced profits.***

Our industry is rapidly changing as new technologies are developed that offer consumers an array of choices for their communications needs and allow new entrants into the markets we serve. In order to grow and remain competitive, we will need to adapt to future changes in technology, enhance our existing offerings and introduce new offerings to address our customers' changing demands. If we are unable to meet future challenges from competing technologies on a timely basis or at an acceptable cost, we could lose customers to our competitors. We may not be able to accurately predict technological trends or the success of new services in the market. In addition, there could be legal or regulatory restraints on our introduction of new services. If our services fail to gain acceptance in the marketplace, or if costs associated with the implementation and introduction of these services materially increase, our ability to retain and attract customers could be adversely affected.

In addition to introducing new technologies and offerings, we must phase out outdated and unprofitable technologies and services. If we are unable to do so on a cost-effective basis, we could experience reduced profits. In addition, there could be legal or regulatory restraints on our ability to phase out current services.

#### ***We depend on key suppliers and vendors to provide equipment that we need to operate our business.***

We depend on various key suppliers and vendors to provide us, directly or through other suppliers, with equipment and services, such as switch and network equipment, smartphones and other wireless devices, that we need in order to operate our business and provide products to our customers. For example, our smartphone and other device suppliers often rely on one vendor for the manufacture and supply of critical components, such as chipsets, used in their devices. If these suppliers or vendors fail to provide equipment or service on a timely basis or fail to meet our performance expectations, we may be unable to provide products and services as and when requested by our customers. We also may be unable to continue to maintain or upgrade our networks. Because of the cost and time lag that can be associated with transitioning from one supplier to another, our business could be substantially disrupted if we were required to, or chose

to, replace the products or services of one or more major suppliers with products or services from another source, especially if the replacement became necessary on short notice. Any such disruption could increase our costs, decrease our operating efficiencies and have a material adverse effect on our business, results of operations and financial condition.

The suppliers and vendors on which we rely may also be subject to litigation with respect to technology on which we depend, including litigation involving claims of patent infringement. Such claims are frequently made in the communications industry. We are unable to predict whether our business will be affected by any such litigation. We expect our dependence on key suppliers to continue as we develop and introduce more advanced generations of technology.

## Table of Contents

### ***Changes in the regulatory framework under which we operate could adversely affect our business prospects or results of operations.***

Our domestic operations are subject to regulation by the FCC and other federal, state and local agencies, and our international operations are regulated by various foreign governments and international bodies. These regulatory regimes frequently restrict or impose conditions on our ability to operate in designated areas and provide specified products or services. We are frequently required to maintain licenses for our operations and conduct our operations in accordance with prescribed standards. We are often involved in regulatory and other governmental proceedings or inquiries related to the application of these requirements. It is impossible to predict with any certainty the outcome of pending federal and state regulatory proceedings relating to our operations, or the reviews by federal or state courts of regulatory rulings. Without relief, existing laws and regulations may inhibit our ability to expand our business and introduce new products and services. Similarly, we cannot guarantee that we will be successful in obtaining the licenses needed to carry out our business plan or in maintaining our existing licenses. For example, the FCC grants wireless licenses for terms generally lasting 10 years, subject to renewal. The loss of, or a material limitation on, certain of our licenses could have a material adverse effect on our business, results of operations and financial condition.

New laws or regulations or changes to the existing regulatory framework at the federal, state and local, or international level could restrict the ways in which we manage our wireline and wireless networks, impose additional costs, impair revenue opportunities and potentially impede our ability to provide services in a manner that would be attractive to us and our customers. For example, we are subject to federal, state and international laws related to privacy and data protection. A new data protection regulation will go into effect in Europe in May 2018 that includes significant penalties for non-compliance. In addition, in its order imposing so-called "network neutrality" regulations, the FCC reversed course in 2015 on the longstanding "light touch" approach and "reclassified" broadband Internet access services as telecommunications services subject to utilities-style common carriage regulation. While the full scope and effect of this new regulatory approach is uncertain, these rules limit the ways that a broadband Internet access service provider can structure business arrangements, manage its network and open the door to additional restrictions, including rate regulation that could adversely affect broadband investment and innovation. These rules may be subject to further challenge in the courts and the proper scope of such regulations is being debated in Congress and the FCC, but the outcome and timing of those challenges and debates remain uncertain. As another example, we hold certain wireless licenses that require us to comply with so-called "open access" FCC regulations, which generally require licensees of particular spectrum to allow customers to use devices and applications of their choice. Moreover, certain services could be subject to conflicting regulation by the FCC and/or various state and local authorities, which could significantly increase the cost of implementing and introducing new services. The further regulation of broadband, wireless and our other activities and any related court decisions could restrict our ability to compete in the marketplace and limit the return we can expect to achieve on past and future investments in our networks.

### ***Cyber attacks impacting our networks or systems could have an adverse effect on our business.***

Cyber attacks, including through the use of malware, computer viruses, dedicated denial of services attacks, credential harvesting and other means for obtaining unauthorized access to or disrupting the operation of our networks and systems and those of our suppliers, vendors and other service providers, could have an adverse effect on our business. Cyber attacks may cause equipment failures, loss of information, including sensitive personal information of customers or employees or valuable technical and marketing information, as well as disruptions to our or our customers' operations. Cyber attacks against companies, including Verizon, have increased in frequency, scope and potential harm in recent years. Further, the perpetrators of cyber attacks are not restricted to particular groups or persons. These attacks may be committed by company employees or external actors operating in any geography, including jurisdictions where law enforcement measures to address such attacks are unavailable or ineffective, and may even be launched by or at the behest of nation states. While, to date, we have not been subject to cyber attacks which, individually or in the aggregate, have been material to our operations or financial condition, the preventive actions we take to reduce the risks associated with cyber attacks, including protection of our systems and networks, may be insufficient to repel or mitigate the effects of a major cyber attack in the future.

The inability to operate our networks and systems or those of our suppliers, vendors and other service providers as a result of cyber attacks, even for a limited period of time, may result in significant expenses to Verizon and/or a loss of market share to other communications providers. The costs associated with a major cyber attack on Verizon could include expensive incentives offered to existing customers and business partners to retain their business, increased expenditures on cybersecurity measures and the use of alternate resources, lost revenues from business interruption and litigation. The potential costs associated with these attacks could exceed the insurance coverage we maintain. Further, certain of Verizon's businesses, such as those offering security solutions and infrastructure and cloud services to business customers, could be negatively affected if our ability to protect our own networks and systems is called into question as a result of a cyber attack. Moreover, our increasing presence in the IoT industry with offerings of telematics products and services, including vehicle telematics, could also increase our exposure to potential costs and expenses and reputational harm in the event of cyber attacks impacting these products or services. In addition, a compromise of security or a theft or other compromise of valuable information, such as financial data and sensitive or private personal information, could result in lawsuits and government claims,

investigations or proceedings. Any of these occurrences could damage our reputation, adversely impact customer and investor confidence, and could further result in a material adverse effect on Verizon's results of operation or financial condition.

*Natural disasters, terrorist acts or acts of war could cause damage to our infrastructure and result in significant disruptions to our operations.*

Our business operations are subject to interruption by natural disasters, power outages, terrorist attacks, other hostile acts and events beyond our control. Such events could cause significant damage to our infrastructure upon which our business operations rely, resulting in degradation or disruption of service to our customers. While we maintain insurance coverage for some of these events, the potential liabilities associated with these events could exceed the insurance coverage we maintain. Our system redundancy may be ineffective or inadequate, and our disaster recovery

## **Table of Contents**

planning may not be sufficient for all eventualities. These events could also damage the infrastructure of the suppliers that provide us with the equipment and services that we need to operate our business and provide products to our customers. A natural disaster or other event causing significant physical damage could cause us to experience substantial losses resulting in significant recovery time and expenditures to resume operations. In addition, these occurrences could result in lost revenues from business interruption as well as damage to our reputation.

### ***Verizon has significant debt, which could increase further if Verizon incurs additional debt in the future and does not retire existing debt.***

As of December 31, 2016, Verizon had approximately \$108.1 billion of outstanding indebtedness, as well as approximately \$8.9 billion of unused borrowing capacity under its existing credit facility. Verizon's debt level and related debt service obligations could have negative consequences, including:

- requiring Verizon to dedicate significant cash flow from operations to the payment of principal, interest and other amounts payable on its debt and the preferred stock issued by an entity acquired in a transaction with Vodafone, which would reduce the funds Verizon has available for other purposes, such as working capital, capital expenditures and acquisitions;
- making it more difficult or expensive for Verizon to obtain any necessary future financing for working capital, capital expenditures, debt service requirements, debt refinancing, acquisitions or other purposes;
- reducing Verizon's flexibility in planning for or reacting to changes in its industry and market conditions;
- making Verizon more vulnerable in the event of a downturn in its business; and
- exposing Verizon to increased interest rate risk to the extent that its debt obligations are at variable interest rates.

In addition, our term loan agreements require Verizon to maintain a certain leverage ratio unless Verizon's credit ratings are at or above a certain level, which could limit Verizon's ability to obtain additional financing in the future.

### ***Adverse changes in the credit markets could increase our borrowing costs and the availability of financing.***

We require a significant amount of capital to operate and grow our business. We fund our capital needs in part through borrowings in the public and private credit markets. Adverse changes in the credit markets, including increases in interest rates, could increase our cost of borrowing and/or make it more difficult for us to obtain financing for our operations or refinance existing indebtedness. In addition, our borrowing costs can be affected by short- and long-term debt ratings assigned by independent rating agencies, which are based, in significant part, on our performance as measured by customary credit metrics. A decrease in these ratings would likely increase our cost of borrowing and/or make it more difficult for us to obtain financing. A severe disruption in the global financial markets could impact some of the financial institutions with which we do business, and such instability could also affect our access to financing.

### ***Increases in costs for pension benefits and active and retiree healthcare benefits may reduce our profitability and increase our funding commitments.***

With approximately 160,900 employees and approximately 201,000 retirees as of December 31, 2016 eligible to participate in Verizon's benefit plans, the costs of pension benefits and active and retiree healthcare benefits have a significant impact on our profitability. Our costs of maintaining these plans, and the future funding requirements for these plans, are affected by several factors, including the legislative and regulatory uncertainty regarding the potential repeal and replacement or modification of the Patient Protection and Affordable Care Act, increases in healthcare costs, decreases in investment returns on funds held by our pension and other benefit plan trusts and changes in the discount rate and mortality assumptions used to calculate pension and other postretirement expenses. If we are unable to limit future increases in the costs of our benefit plans, those costs could reduce our profitability and increase our funding commitments.

### ***A significant portion of our workforce is represented by labor unions, and we could incur additional costs or experience work stoppages as a result of the renegotiation of our labor contracts.***

As of December 31, 2016, approximately 23% of our workforce was represented by labor unions. While less than 1% of the workforce of our wireless and other businesses outside of wireline are represented by unions, we cannot predict what level of success unions may have in organizing these workforces or the potentially negative impact it would have on our costs.

### ***We are subject to a significant amount of litigation, which could require us to pay significant damages or settlements.***

We are subject to a substantial amount of litigation, including, from time to time, shareholder derivative suits, patent infringement lawsuits, antitrust class actions, wage and hour class actions, personal injury claims and lawsuits relating to our advertising, sales, billing and collection practices. In addition, our wireless business also faces personal injury and consumer class action lawsuits relating to alleged

health effects of wireless phones or radio frequency transmitters, and class action lawsuits that challenge marketing practices and disclosures relating to alleged adverse health effects of handheld wireless phones. We may incur significant expenses in defending these lawsuits. In addition, we may be required to pay significant awards or settlements.

**Table of Contents***Item 1B. Unresolved Staff Comments*

None.

*Item 2. Properties*

Our principal properties do not lend themselves to simple description by character and location. Our total investment in plant, property and equipment was approximately \$232 billion at December 31, 2016 and \$220 billion at December 31, 2015, including the effect of retirements, but before deducting accumulated depreciation. Our gross investment in plant, property and equipment consisted of the following:

At December 31,	2016	2015
Network equipment	78.5%	78.8%
Land, buildings and building equipment	12.0%	11.9%
Furniture and other	9.5%	9.3%
	100.0%	100.0%

Our properties as a percentage of total properties are as follows:

At December 31,	2016	2015
Wireline	51.7%	53.2%
Wireless	46.8%	45.4%
Other	1.5%	1.4%
	100.0%	100.0%

Network equipment consists primarily of cable (aerial, buried, underground or undersea) and the related support structures of poles and conduit, wireless plant, switching equipment, network software, transmission equipment and related facilities. Land, buildings and building equipment consists of land and land improvements, central office buildings or any other buildings that house network equipment, and buildings that are used for administrative and other purposes. Substantially all the switching centers are located on land and in buildings we own due to their critical role in the network and high set-up relocation costs. We also maintain facilities throughout the United States comprised of administrative and sales offices, customer care centers, retail sales locations, garage work centers, switching centers, cell sites and data centers. Furniture and other consists of telephone equipment, furniture, data processing equipment, office equipment, motor vehicles, plant under construction and leasehold improvements.

*Item 3. Legal Proceedings*

In October 2013, the California Attorney General's Office notified Verizon California Inc. and other Verizon companies of potential violations of California state hazardous waste statutes primarily arising from the disposal of electronic components, batteries and aerosol cans at certain California facilities. We are cooperating with this investigation and continue to review our operations relating to the management of hazardous waste. While penalties relating to the alleged violations could exceed \$100,000, we do not expect that any penalties ultimately incurred will be material. On April 1, 2016, we completed the sale to Frontier of our landline business operated by Verizon California Inc. and certain other Verizon landline companies. As a result of this transaction, Frontier now owns and operates Verizon California Inc. and has assumed the liabilities of Verizon California Inc. that may arise as a result of these alleged violations.

*Item 4. Mine Safety Disclosures*

None.

## Table of Contents

### PART II

#### *Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities*

The principal market for trading in the common stock of Verizon is the New York Stock Exchange. As of December 31, 2016, there were 690,741 shareowners of record.

High and low stock prices, as reported on the New York Stock Exchange composite tape of transactions, and dividend data are as follows:

	Market Price		Cash Dividend Declared
	High	Low	
2016 Fourth Quarter	\$ 53.90	\$ 46.01	\$ .5775
Third Quarter	56.95	51.02	.5775
Second Quarter	55.92	49.05	.5650
First Quarter	54.37	43.79	.5650
2015 Fourth Quarter	\$ 47.23	\$ 42.20	\$ .5650
Third Quarter	48.26	38.06	.5650
Second Quarter	50.86	46.60	.5500
First Quarter	49.99	45.37	.5500

#### **Stock Repurchases**

In March 2014, the Verizon Board of Directors authorized a three-year share buyback program to repurchase up to 100 million shares of the Company's common stock. Under the program, shares may be repurchased in privately negotiated transactions and on the open market, including through plans complying with Rule 10b5-1(c) under the Exchange Act. The timing and number of shares purchased under the program, if any, will depend on market conditions and the Company's capital allocation priorities.

During the fourth quarter of 2016, Verizon did not repurchase any shares of Verizon common stock. At December 31, 2016, the maximum number of shares that could be purchased by or on behalf of Verizon under our share buyback program was 97.2 million.

For other information required by this item, see the section entitled "Stock Performance Graph" in the 2016 Verizon Annual Report to Shareowners, which is incorporated herein by reference.

#### *Item 6. Selected Financial Data*

Information required by this item is included in the 2016 Verizon Annual Report to Shareowners under the heading "Selected Financial Data", which is incorporated herein by reference.

#### *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations*

Information required by this item is included in the 2016 Verizon Annual Report to Shareowners under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations", which is incorporated herein by reference.

#### *Item 7.A. Quantitative and Qualitative Disclosures About Market Risk*

Information required by this item is included in the 2016 Verizon Annual Report to Shareowners under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations - Market Risk", which is incorporated herein by reference.

#### *Item 8. Financial Statements and Supplementary Data*

Information required by this item is included in the consolidated financial statements and related notes of Verizon Communications Inc. and Subsidiaries in the 2016 Verizon Annual Report to Shareowners, which is incorporated herein by reference.

#### *Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure*

None.

## Table of Contents

### *Item 9A. Controls and Procedures*

Our chief executive officer and chief financial officer have evaluated the effectiveness of the registrant's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934), as of the end of the period covered by this Annual Report, that ensure that information relating to the registrant which is required to be disclosed in this report is recorded, processed, summarized and reported within required time periods using the criteria for effective internal control established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013. Based on this evaluation, our chief executive officer and chief financial officer have concluded that the registrant's disclosure controls and procedures were effective as of December 31, 2016.

In the ordinary course of business, we routinely review our system of internal control over financial reporting and make changes to our systems and processes that are intended to ensure an effective internal control environment. There were no changes in the Company's internal control over financial reporting during the fourth quarter of 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Management's report on internal control over financial reporting and the attestation report of Verizon's independent registered public accounting firm are included in the 2016 Verizon Annual Report to Shareowners and are incorporated herein by reference.

### *Item 9B. Other Information*

None.

## PART III

### *Item 10. Directors, Executive Officers and Corporate Governance*

Set forth below is information with respect to our executive officers.

Name	Age	Office	Held Since
Lowell C. McAdam	62	Chairman and Chief Executive Officer	2011
Matthew D. Ellis	45	Executive Vice President and Chief Financial Officer	2016
Roger Gurmani	56	Executive Vice President and Chief Information and Technology Architect	2015
Marc C. Reed	58	Executive Vice President and Chief Administrative Officer	2012
Diego Scotti	44	Executive Vice President and Chief Marketing Officer	2014
Craig L. Silliman	49	Executive Vice President of Public Policy and General Counsel	2015
Anthony T. Skiadas	48	Senior Vice President and Controller	2013
John G. Stratton	55	Executive Vice President and President of Operations	2015
Marni M. Walden	49	Executive Vice President and President of Product Innovation and New Businesses	2015

Prior to serving as an executive officer, each of the above officers has held high-level managerial positions with the Company or one of its subsidiaries for at least five years, with the exception of Mr. Ellis, who has been with the Company since 2013 and Mr. Scotti, who has been with the Company since 2014. Officers are not elected for a fixed term of office and may be removed from office at any time at the discretion of the Board of Directors.

Matthew D. Ellis is the Executive Vice President and Chief Financial Officer for Verizon. Mr. Ellis served as Senior Vice President and CFO of Operations - Finance of the Company from February 2015 until the appointment to his current role in November 2016 and as Senior Vice President and Treasurer of the Company from the time he joined the Company in 2013 until February 2015. Prior to joining Verizon, Mr. Ellis served in leadership positions at Tyson Foods, Inc. for 15 years, most recently as Vice President and Treasurer responsible for financing, cash management, insurance and credit.

Diego Scotti is Executive Vice President and Chief Marketing Officer for Verizon. Mr. Scotti joined the company in October 2014. Prior to joining Verizon, Mr. Scotti served as Chief Marketing Officer of J. Crew from 2011 to 2014 and as Executive Director of Marketing at Conde Nast Publications, where he oversaw 20 print and digital media brands, from 2008 to 2011. Mr. Scotti also previously served as the head of global advertising and brand management at American Express.

## Table of Contents

For other information required by this item, see the sections entitled “Governance — Where to find more information on governance at Verizon and — Business conduct and ethics,” “Item 1: Election of Directors — Director nominations,” “Board and Committees — Board committees” and “Stock Ownership — Section 16(a) Beneficial Ownership Reporting Compliance” in our definitive Proxy Statement to be filed with the Securities and Exchange Commission and delivered to shareholders in connection with our 2017 Annual Meeting of Shareholders, which are incorporated herein by reference.

### *Item 11. Executive Compensation*

For information with respect to executive compensation, see the sections entitled “Executive Compensation — Compensation Discussion and Analysis, — Compensation Committee Report and — Compensation Tables” in our definitive Proxy Statement to be filed with the Securities and Exchange Commission and delivered to shareholders in connection with our 2017 Annual Meeting of Shareholders, which is incorporated by reference. There were no relationships to be disclosed under paragraph (e)(4) of Item 407 of Regulation S-K.

### *Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters*

For information with respect to the security ownership of the Directors and executive officers and for information with respect to securities authorized for issuance under Verizon’s equity compensation plan, see the sections entitled “Stock Ownership — Security Ownership of Certain Beneficial Owners and Management” and “Item 5: Approval of Verizon’s 2017 Long-Term Incentive Plan,” respectively, in our definitive Proxy Statement to be filed with the Securities and Exchange Commission and delivered to shareholders in connection with our 2017 Annual Meeting of Shareholders, which is incorporated herein by reference.

### *Item 13. Certain Relationships and Related Transactions, and Director Independence*

For information with respect to certain relationships and related transactions and Director independence, see the sections entitled “Governance — Related person transactions” and “Item 1: Election of Directors — Independence” in our definitive Proxy Statement to be filed with the Securities and Exchange Commission and delivered to shareholders in connection with our 2017 Annual Meeting of Shareholders, which are incorporated by reference.

### *Item 14. Principal Accounting Fees and Services*

For information with respect to principal accounting fees and services, see the section entitled “Audit Matters — Item 2: Ratification of Appointment of Independent Registered Public Accounting Firm” in our definitive Proxy Statement to be filed with the Securities and Exchange Commission and delivered to shareholders in connection with our 2017 Annual Meeting of Shareholders, which are incorporated by reference.

**Table of Contents**

## PART IV

*Item 15. Exhibits, Financial Statement Schedules*

## (a) Documents filed as part of this report:

	Page
(1) Report of Management on Internal Control Over Financial Reporting	*
(2) Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting	*
(3) Report of Independent Registered Public Accounting Firm on Financial Statements	*
Financial Statements covered by Report of Independent Registered Public Accounting Firm:	
Consolidated Statements of Income	*
Consolidated Statements of Comprehensive Income	*
Consolidated Balance Sheets	*
Consolidated Statements of Cash Flows	*
Consolidated Statements of Changes in Equity	*
Notes to Consolidated Financial Statements	*
* Incorporated herein by reference to the appropriate portions of the registrant's Annual Report to Shareowners for the fiscal year ended December 31, 2016. (See Part II.)	
(4) Financial Statement Schedule	
<u>II – Valuation and Qualifying Accounts</u>	29
(5) Exhibits	

Exhibits identified in parentheses below, on file with the SEC, are incorporated herein by reference as exhibits hereto. Unless otherwise indicated, all exhibits so incorporated are from File No. 1-8606.

**Table of Contents****Exhibit****Number Description**

- 
- 3a Restated Certificate of Incorporation of Verizon Communications Inc. (Verizon) (filed as Exhibit 3a to Form 10-Q for the period ended June 30, 2014 and incorporated herein by reference).
- 3b Bylaws of Verizon, as amended and restated, effective as of November 3, 2016 (filed as Exhibit 3b to Form 8-K filed on November 4, 2016 and incorporated herein by reference).
- 4a Indenture between Verizon, both individually and as successor in interest to Verizon Global Funding Corp., and U.S. Bank National Association, as successor trustee to Wachovia Bank, National Association, formerly known as First Union National Bank, as Trustee, dated as of December 1, 2000 (incorporated by reference to Verizon Global Funding Corp.'s Registration Statement on Form S-4, Registration No. 333-64792, Exhibit 4.1).
- 4b First Supplemental Indenture between Verizon, both individually and as successor in interest to Verizon Global Funding Corp., and U.S. Bank National Association, as successor trustee to Wachovia Bank, National Association, formerly known as First Union National Bank, as Trustee, dated as of May 15, 2001 (incorporated by reference to Verizon Global Funding Corp.'s Registration Statement on Form S-3, Registration No. 333-67412, Exhibit 4.2).
- 4c Second Supplemental Indenture between Verizon, both individually and as successor in interest to Verizon Global Funding Corp., and U.S. Bank National Association, as successor trustee to Wachovia Bank, National Association, formerly known as First Union National Bank, as Trustee, dated as of September 29, 2004 (incorporated by reference to Form 8-K filed on February 9, 2006, Exhibit 4.1).
- 4d Third Supplemental Indenture between Verizon, both individually and as successor in interest to Verizon Global Funding Corp., and U.S. Bank National Association, as successor trustee to Wachovia Bank, National Association, formerly known as First Union National Bank, as Trustee, dated as of February 1, 2006 (incorporated by reference to Form 8-K filed on February 9, 2006, Exhibit 4.2).
- 4e Fourth Supplemental Indenture between Verizon, both individually and as successor in interest to Verizon Global Funding Corp., and U.S. Bank National Association, as successor trustee to Wachovia Bank, National Association, formerly known as First Union National Bank, as Trustee, dated as of April 4, 2016 (incorporated by reference to Verizon Communications Inc.'s Registration Statement on Form S-4, Registration No. 333-212307, Exhibit 4.5).

Except for Exhibits 4a – 4e above, no other instrument which defines the rights of holders of long-term debt of Verizon and its consolidated subsidiaries is filed herewith pursuant to Regulation S-K, Item 601(b)(4)(iii)(A). Pursuant to this regulation, Verizon hereby agrees to furnish a copy of any such instrument to the SEC upon request.

- 10a NYNEX Directors' Charitable Award Program (filed as Exhibit 10i to Form 10-K for the year ended December 31, 2000 and incorporated herein by reference).\*\*
- 10b 2009 Verizon Long-Term Incentive Plan, As Amended and Restated (incorporated by reference to Appendix D of the Registrant's Proxy Statement included in Schedule 14A filed on March 18, 2013).\*\*
- 10b(i) Form of 2011 Special Performance Stock Unit Agreement (filed as Exhibit 10 to Form 10-Q for the period ended September 30, 2011 and incorporated by reference).\*\*
- 10b(ii) Performance Stock Unit Agreement 2014-2016 Award Cycle (filed as Exhibit 10a to Form 10-Q for the period ended March 31, 2014 and incorporated herein by reference).\*\*
- 10b(iii) Restricted Stock Unit Agreement 2014-2016 Award Cycle (filed as Exhibit 10b to Form 10-Q for the period ended March 31, 2014 and incorporated herein by reference).\*\*

## Table of Contents

- 10b(iv) Performance Stock Unit Agreement 2015-2017 Award Cycle (filed as Exhibit 10a to Form 10-Q for the period ended March 31, 2015 and incorporated herein by reference).\*\*
- 10b(v) Restricted Stock Unit Agreement 2015-2017 Award Cycle (filed as Exhibit 10b to Form 10-Q for the period ended March 31, 2015 and incorporated herein by reference).\*\*
- 10b(vi) Performance Stock Unit Agreement 2016-2018 Award Cycle (filed as Exhibit 10a to Form 10-Q for the period ended March 31, 2016 and incorporated herein by reference).\*\*
- 10b(vii) Restricted Stock Unit Agreement 2016-2018 Award Cycle (filed as Exhibit 10b to Form 10-Q for the period ended March 31, 2016 and incorporated herein by reference).\*\*
- 10c Verizon Short-Term Incentive Plan, As Amended and Restated (incorporated by reference to Appendix C of the Registrant's Proxy Statement included in Schedule 14A filed on March 23, 2009).\*\*
- 10d Verizon Income Deferral Plan (filed as Exhibit 10f to Form 10-Q for the period ended June 30, 2002 and incorporated herein by reference).\*\*
  - 10d(i) Description of Amendment to Plan (filed as Exhibit 10o(i) to Form 10-K for the year ended December 31, 2004 and incorporated herein by reference).\*\*
- 10e Verizon Excess Pension Plan (filed as Exhibit 10p to Form 10-K for the year ended December 31, 2004 and incorporated herein by reference).\*\*
  - 10e(i) Description of Amendment to Plan (filed as Exhibit 10p(i) to Form 10-K for the year ended December 31, 2004 and incorporated herein by reference).\*\*
- 10f GTE's Executive Salary Deferral Plan, as amended (filed as Exhibit 10.10 to GTE's Form 10-K for the year ended December 31, 1998, File No. 1-2755 and incorporated herein by reference).\*\*
- 10g Bell Atlantic Senior Management Long-Term Disability and Survivor Protection Plan, as amended (filed as Exhibit 10h to Form SE filed on March 27, 1986 and Exhibit 10b(ii) to Form 10-K for the year ended December 31, 1997 and incorporated herein by reference).\*\*
- 10h IGTE Executive Retiree Life Insurance Plan (filed as Exhibit 10q to Form 10-K for the year ended December 31, 2010 and incorporated herein by reference).\*\*
- 10i Verizon Executive Life Insurance Plan, As Amended and Restated September 2009 (filed as Exhibit 10s to Form 10-K for the year ended December 31, 2010 and incorporated herein by reference).\*\*
- 10j Verizon Executive Deferral Plan (filed as Exhibit 10e to Form 10-Q for the period ended June 30, 2009 and incorporated herein by reference).\*\*
- 10k Form of Aircraft Time Sharing Agreement (filed as Exhibit 10v to Form 10-K for the year ended December 31, 2010 and incorporated herein by reference).\*\*
- 10l NYNEX Deferred Compensation Plan for Non-Employee Directors (filed as Exhibit 10gg to NYNEX's Registration Statement No. 2-87850, File No. 1-8608 and incorporated herein by reference).\*\*
- 10m Amendment to NYNEX Deferred Compensation Plan for Non-Employee Directors (filed as Exhibit 10iii 5a to NYNEX's Quarterly Report on Form 10-Q for the period ended June 30, 1996, File No. 1-8608 and incorporated herein by reference).\*\*
- 10n Verizon Senior Manager Severance Plan (filed as Exhibit 10d to Form 10-Q for the period ended March 31, 2010 and incorporated herein by reference).\*\*

Table of Contents

- 10o Securities Purchase Agreement, dated as of February 5, 2015, by and between Frontier Communications Corporation and Verizon Communications Inc. (filed as Exhibit 10q to Form 10-K for the year ended December 31, 2014 and incorporated herein by reference).
- 12 Computation of Ratio of Earnings to Fixed Charges filed herewith.
- 13 Portions of Verizon's Annual Report to Shareowners for the fiscal year ended December 31, 2016 filed herewith. Only the information incorporated by reference into this Form 10-K is included in the exhibit.
- 21 List of principal subsidiaries of Verizon filed herewith.
- 23 Consent of Ernst & Young LLP filed herewith.
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 filed herewith.
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 filed herewith.
- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 filed herewith.
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 filed herewith.
- 101.INS XBRL Instance Document.
- 101.SCH XBRL Taxonomy Extension Schema Document.
- 101.PRE XBRL Taxonomy Presentation Linkbase Document.
- 101.CAL XBRL Taxonomy Calculation Linkbase Document.
- 101.LAB XBRL Taxonomy Label Linkbase Document.
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document.
- \*\* Indicates management contract or compensatory plan or arrangement.

Table of Contents**Schedule II - Valuation and Qualifying Accounts****Verizon Communications Inc. and Subsidiaries**

For the Years Ended December 31, 2016, 2015 and 2014

(dollars in millions)

Description	Balance at Beginning of Period	Additions		Deductions Note (c)(d)	Balance at End of Period
		Charged to Expenses	Charged to Other Accounts Note (a)(b)		
Allowance for Uncollectible Accounts Receivable:					
Year 2016 (e)	\$ 1,037	\$ 1,420	\$ 204	\$ 1,515	\$ 1,146
Year 2015 (e)	739	1,610	200	1,512	1,037
Year 2014	645	1,095	141	1,142	739
Valuation Allowance for Deferred Tax Assets:					
Year 2016	\$ 3,414	\$ 146	\$ 47	\$ 1,134	\$ 2,473
Year 2015	1,841	237	1,701	365	3,414
Year 2014	1,685	505	5	354	1,841

- (a) Allowance for Uncollectible Accounts Receivable primarily includes amounts previously written off which were credited directly to this account when recovered.
- (b) Valuation Allowance for Deferred Tax Assets includes an increase to the valuation allowance as a result of the acquisition of AOL in 2015 and amounts charged to equity and reclassifications from other balance sheet accounts.
- (c) Amounts written off as uncollectible or transferred to other accounts or utilized.
- (d) Reductions to valuation allowances related to deferred tax assets.
- (e) Allowance for Uncollectible Accounts Receivable includes approximately \$301 million and \$155 million at December 31, 2016 and 2015, respectively, related to long-term device payment plan receivables.

**Table of Contents****Signatures**

Pursuant to the requirements of Section 13 or 15(d) 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.

VERIZON COMMUNICATIONS INC.

By: /s/ Anthony T. Skiadas  
 Anthony T. Skiadas  
 Senior Vice President and Controller

Date: February 21, 2017

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Principal Executive Officer:

<u>/s/ Lowell C. McAdam</u>	Chairman and Chief	February 21, 2017
Lowell C. McAdam	Executive Officer	

Principal Financial Officer:

<u>/s/ Matthew D. Ellis</u>	Executive Vice President and Chief	February 21, 2017
Matthew D. Ellis	Financial Officer	

Principal Accounting Officer:

<u>/s/ Anthony T. Skiadas</u>	Senior Vice President and	February 21, 2017
Anthony T. Skiadas	Controller	

Table of Contents

<u>/s/ Lowell C. McAdam</u> Lowell C. McAdam	Director	February 21, 2017
<u>/s/ Shellye L. Archambeau</u> Shellye L. Archambeau	Director	February 21, 2017
<u>/s/ Mark T. Bertolini</u> Mark T. Bertolini	Director	February 21, 2017
<u>/s/ Richard L. Carrión</u> Richard L. Carrión	Director	February 21, 2017
<u>/s/ Melanie L. Healey</u> Melanie L. Healey	Director	February 21, 2017
<u>/s/ M. Frances Keeth</u> M. Frances Keeth	Director	February 21, 2017
<u>/s/ Karl-Ludwig Kley</u> Karl-Ludwig Kley	Director	February 21, 2017
<u>/s/ Clarence Otis, Jr.</u> Clarence Otis, Jr.	Director	February 21, 2017
<u>/s/ Rodney E. Slater</u> Rodney E. Slater	Director	February 21, 2017
<u>/s/ Kathryn A. Tesija</u> Kathryn A. Tesija	Director	February 21, 2017
<u>/s/ Gregory D. Wasson</u> Gregory D. Wasson	Director	February 21, 2017
<u>/s/ Gregory G. Weaver</u> Gregory G. Weaver	Director	February 21, 2017

10-K 1 ye16\_10k.htm AT&T INC. 2016 FORM 10-K

**FORM 10-K**

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

(Mark One)

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

**For the fiscal year ended December 31, 2016**

**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 1-8610

**AT&T INC.**

Incorporated under the laws of the State of Delaware  
I.R.S. Employer Identification Number 43-1301883

208 S. Akard St., Dallas, Texas, 75202  
Telephone Number 210-821-4105

Securities registered pursuant to Section 12(b) of the Act: (See attached Schedule A)

Securities registered pursuant to Section 12(g) of the Act: None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

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

No

Yes

Based on the closing price of \$43.21 per share on June 30, 2016, the aggregate market value of our voting and non-voting common stock held by non-affiliates was \$266 billion.

At February 10, 2017, common shares outstanding were 6,141,570,142.

**DOCUMENTS INCORPORATED BY REFERENCE**

- (1) Portions of AT&T Inc.'s Annual Report to Stockholders for the fiscal year ended December 31, 2016 (Parts I and II).
- (2) Portions of AT&T Inc.'s Notice of 2017 Annual Meeting and Proxy Statement dated on or about March 10, 2017 to be filed within the period permitted under General Instruction G(3) (Parts III and IV).

**SCHEDULE A**

Securities Registered Pursuant To Section 12(b) Of The Act:

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Shares (Par Value \$1.00 Per Share)	New York Stock Exchange
5.875% AT&T Inc. Global Notes due April 28, 2017	New York Stock Exchange
Floating Rate AT&T Inc. Global Notes due June 4, 2019	New York Stock Exchange
1.875% AT&T Inc. Global Notes due December 4, 2020	New York Stock Exchange
2.65% AT&T Inc. Global Notes due December 17, 2021	New York Stock Exchange
1.45% AT&T Inc. Global Notes due June 1, 2022	New York Stock Exchange
2.50% AT&T Inc. Global Notes due March 15, 2023	New York Stock Exchange
1.30% AT&T Inc. Global Notes due September 5, 2023	New York Stock Exchange
2.75% AT&T Inc. Global Notes due May 19, 2023	New York Stock Exchange
2.40% AT&T Inc. Global Notes due March 15, 2024	New York Stock Exchange
3.50% AT&T Inc. Global Notes due December 17, 2025	New York Stock Exchange
4.375% AT&T Inc. Global Notes due September 14, 2029	New York Stock Exchange
2.60% AT&T Inc. Global Notes due December 17, 2029	New York Stock Exchange
3.55% AT&T Inc. Global Notes due December 17, 2032	New York Stock Exchange
5.20% AT&T Inc. Global Notes due November 18, 2033	New York Stock Exchange
3.375% AT&T Inc. Global Notes due March 15, 2034	New York Stock Exchange



**SCHEDULE A - Continued**

2.45% AT&T Inc. Global Notes due March 15, 2035	New York Stock Exchange
7.00% AT&T Inc. Global Notes due April 30, 2040	New York Stock Exchange
4.25% AT&T Inc. Global Notes due June 1, 2043	New York Stock Exchange
4.875% AT&T Inc. Global Notes due June 1, 2044	New York Stock Exchange

**TABLE OF CONTENTS**

<b>Item</b>		<b>Page</b>
<b>PART I</b>		
1.	Business	1
1A.	Risk Factors	11
2.	Properties	12
3.	Legal Proceedings	12
4.	Mine Safety Disclosures	12
	Executive Officers of the Registrant	13
<b>PART II</b>		
5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	14
6.	Selected Financial Data	15
7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	15
7A.	Quantitative and Qualitative Disclosures about Market Risk	15
8.	Financial Statements and Supplementary Data	15
9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	15
9A.	Controls and Procedures	15
9B.	Other Information	16
<b>PART III</b>		
10.	Directors, Executive Officers and Corporate Governance	16
11.	Executive Compensation	16
12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	16
13.	Certain Relationships and Related Transactions, and Director Independence	17
14.	Principal Accountant Fees and Services	18
<b>PART IV</b>		
15.	Exhibits and Financial Statement Schedules	18

**AT&T Inc.**

---

**PART I****ITEM 1. BUSINESS****GENERAL**

AT&T Inc. ("AT&T," "we" or the "Company") is a holding company incorporated under the laws of the State of Delaware in 1983 and has its principal executive offices at 208 S. Akard St., Dallas, Texas, 75202 (telephone number 210-821-4105). We maintain an internet website at [www.att.com](http://www.att.com). (This website address is for information only and is not intended to be an active link or to incorporate any website information into this document.) We make available, free of charge, on our website our annual report on Form 10-K, our quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). We also make available on that website, and in print, if any stockholder or other person so requests, our "Code of Ethics" applicable to all employees and Directors, our "Corporate Governance Guidelines," and the charters for all committees of our Board of Directors, including Audit, Human Resources and Corporate Governance and Nominating. Any changes to our Code of Ethics or waiver of our Code of Ethics for senior financial officers, executive officers or Directors will be posted on that website.

**History**

AT&T, formerly known as SBC Communications Inc. (SBC), was formed as one of several regional holding companies created to hold AT&T Corp.'s (ATTC) local telephone companies. On January 1, 1984, we were spun-off from ATTC pursuant to an anti-trust consent decree, becoming an independent publicly-traded telecommunications services provider. At formation, we primarily operated in five southwestern states. Our subsidiaries merged with Pacific Telesis Group in 1997, Southern New England Telecommunications Corporation in 1998 and Ameritech Corporation in 1999, thereby expanding our wireline operations as the incumbent local exchange carrier (ILEC) into a total of 13 states. In November 2005, one of our subsidiaries merged with ATTC, creating one of the world's leading telecommunications providers. In connection with the merger, we changed the name of our company from "SBC Communications Inc." to "AT&T Inc." In December 2006, one of our subsidiaries merged with BellSouth Corporation (BellSouth) making us the ILEC in an additional nine states. With the BellSouth acquisition, we also acquired BellSouth's 40 percent economic interest in AT&T Mobility LLC (AT&T Mobility), formerly Cingular Wireless LLC, resulting in 100 percent ownership of AT&T Mobility. In 2014, we completed the acquisition of wireless provider Leap Wireless International, Inc. (Leap) and sold our ILEC operations in Connecticut, which we had previously acquired in 1998. In 2015, we completed acquisitions of wireless properties in Mexico and DIRECTV, a leading provider of digital television entertainment services in both the United States and Latin America. Our services and products are marketed under the AT&T, Cricket, DIRECTV, SKY, and Unefon brand names.

**Scope**

We are a leading provider of communications and digital entertainment services in the United States and the world. We offer our services and products to consumers in the U.S., Mexico and Latin America and to businesses and other providers of telecommunications services worldwide. We also own and operate three regional TV sports networks, and retain non-controlling interests in another regional sports network and a network dedicated to game-related programming as well as internet interactive game playing.

The services and products that we offer vary by market, and include: wireless communications, data/broadband and internet services, digital video services, local and long-distance telephone services, telecommunications equipment, managed networking, and wholesale services. Our operating subsidiaries are organized as follows, corresponding to our operating segments for financial reporting purposes:

- Business Solutions business units provide services to business customers, including multinational companies; governmental and wholesale customers; and individual subscribers who purchase wireless services through employer-sponsored plans. We provide advanced IP-based services including Virtual Private Networks (VPN); Ethernet-related products and broadband, collectively referred to as fixed strategic services; as well as traditional data and voice products. We utilize our wireless and wired networks (referred to as "wired" or "wireline") to provide a complete integrated communications solution to our business customers.
- Entertainment Group business units provide video, internet, voice communication, and interactive and targeted advertising services to customers located in the United States or in U.S. territories. We utilize our copper and IP-based network and/or our satellite technology.
- Consumer Mobility business units provide nationwide wireless service to consumers, and wholesale and resale subscribers located in the United States or in U.S. territories. We utilize our network to provide voice and data services, including high-speed internet, video and home-monitoring services over wireless devices.

**AT&T Inc.**

---

- International business units provide entertainment services in Latin America and wireless services in Mexico. Video entertainment services are provided to primarily residential customers using satellite technology. We utilize our regional and national wireless networks in Mexico to provide consumer and business customers with wireless data and voice communication services.

Our Corporate and Other unit includes (1) operations that are not considered reportable segments and that are no longer integral to our operations or which we no longer actively market, and (2) impacts of corporate-wide decisions for which the individual operating segments are not being evaluated, including interest costs and expected return on plan assets for our pension and postretirement benefit plans.

With continuing advances in technology and in response to changing demands from our customers, in recent years we have focused on providing enhanced broadband, video and voice services. In 2015, we purchased DIRECTV to expand our involvement in the digital entertainment space. The nationwide reach of DIRECTV and superior content-owner relationships significantly improve the economics and expanded the geographic reach of our pre-existing AT&T U-verse® video service. We also purchased wireless operations in Mexico, moving quickly to build a world-class mobile business in a country with a strong economic outlook, a growing middle class, and cultural and geographic ties to the United States. These acquisitions and our continued investment in a premier network experience make our customers' lives more convenient and productive and foster competition and further innovation in the communications and entertainment industry. In late 2016, we took another step in our strategy of providing an unmatched communication and entertainment experience for our customers when we agreed to purchase Time Warner Inc., a global leader in creating premium media and entertainment content. In 2017, we plan to focus on the areas discussed below.

**Wireless**

AT&T Mobility began operations in October 2000 as a joint venture between us and BellSouth and, in 2004, acquired AT&T Wireless Services, Inc. Upon our acquisition of BellSouth in 2006, AT&T Mobility became a wholly-owned subsidiary. We provide wireless video, data and voice services. We are experiencing rapid growth in video and data usage as consumers are demanding seamless access across their wired and wireless devices, and as more and more machines are being connected to the internet.

As of December 31, 2016, we served 146.8 million wireless subscribers in North America, with nearly 135 million in the United States. Our LTE technology covers almost 400 million people in North America, and, in the United States, we cover all major metropolitan areas and almost 320 million people with our LTE technology. We also provide 4G coverage using another technology (HSPA+), and, when combined with our upgraded backhaul network, we are able to enhance our network capabilities and provide superior mobile broadband speeds for data and video services. Our wireless network also relies on other GSM digital transmission technologies for 3G data communications.

We have also started planning for deployment of the latest wireless technology (5G) and are currently testing in our labs and in the field various ways to deploy that technology. We expect global 5G technology standards to be set over the next two years or so, enabling companies to begin commercial deployment thereafter. The increased speeds and network operating efficiency expected with 5G technology should enable massive deployment of devices connected to the internet as well as faster delivery of video and data services.

As the wireless industry continues to mature, future wireless growth will become increasingly dependent on our ability to offer innovative video and data services and a wireless network that has sufficient spectrum and capacity to support these innovations. We continue to invest significant capital in expanding our network capacity, as well as to secure and utilize spectrum that meets our long-term needs. To that end, we submitted winning bids for 251 AWS spectrum licenses for a near-nationwide contiguous block of high-quality AWS spectrum in the AWS-3 Auction (FCC Auction 97). Our strategy also includes redeploying spectrum previously used for basic 2G services to support more advanced mobile internet services on our 3G and 4G networks. We have bid on FirstNet, the First Responder Network Authority, which if awarded will provide access to a nationwide low band 20 MHz of spectrum, assuming all states "opt in," and are participating in the FCC 600 MHz Auction (Auction 1000). We will continue to invest in our wireless network as we look to provide future service offerings and participate in technologies such as 5G and millimeter-wave bands.

**Business Solutions**

We expect to continue to strengthen the reach and sophistication of our network facilities and our ability to offer a variety of communications services, both fixed and mobile, to businesses customers, including multinational companies; governmental and wholesale customers; and individual subscribers who purchase wireless services through employer-sponsored plans.

**AT&T Inc.**

---

**Internet Protocol (IP) Technology**

IP is generally used to describe the transmission of data, which can include voice (called voice over IP or VoIP), using a software-based technology rather than a traditional wire and physical switch-based telephone network. A company using this technology can provide voice and data services at a lower cost because this technology uses bandwidth more efficiently than a traditional network. Using this technology also presents growth opportunities, especially in providing data and video services to both fixed locations and mobile devices. To take advantage of both these growth and cost-savings opportunities, we have encouraged the migration of wireline customers in our current 21-state ILEC service area to services using IP, and expect to continue this transition through at least 2020.

**Integration of Data/Broadband and Entertainment Services**

As the communications industry continues to move toward internet-based technologies that are capable of blending traditional wireline and wireless services, we plan to offer services that take advantage of these new and more sophisticated technologies. In particular, we intend to continue to focus on expanding our high-speed internet and video offerings and on developing IP-based services that allow customers to unite their home or business fixed services with their mobile service. During 2017, we will continue to develop and provide unique integrated video, mobile and broadband solutions, including our recently introduced over-the-top video service, DIRECTV NOW.

**International**

We believe that the wireless model in the U.S., with exploding demand for mobile internet service and the associated economic benefits, will be repeated around the world as companies invest in high-speed mobile networks. Due in part to changes in the legal and regulatory framework in Mexico in 2015, we acquired Mexican wireless operations to establish a unique, seamless, cross-border North American wireless network covering nearly 400 million people and businesses in the United States and Mexico. During 2017, we will continue to build a world-class mobile business and network in Mexico.

**BUSINESS OPERATIONS****OPERATING SEGMENTS**

Our segments are strategic business units that offer different products and services over various technology platforms and/or in different geographies that are managed accordingly. We analyze our operating segments based on Segment Contribution, which consists of operating income, excluding acquisition-related costs and other significant items, and equity in net income (loss) of affiliates for investments managed within each operating segment. We have four reportable segments: (1) Business Solutions, (2) Entertainment Group, (3) Consumer Mobility and (4) International.

Additional information about our segments, including financial information, is included under the heading "Segment Results" on pages 13 through 21 and in Note 4 of the Annual Report and is incorporated herein by reference pursuant to General Instruction G(2).

**BUSINESS SOLUTIONS**

Our Business Solutions segment provides services to business customers, including multinational companies; governmental and wholesale customers; and individual subscribers who purchase wireless services through employer-sponsored plans. We provide advanced IP-based services including Virtual Private Networks (VPN); Ethernet-related products and broadband, collectively referred to as fixed strategic services; as well as traditional data and voice products. We utilize our wireless and wired networks (referred to as "wired" or "wireline") to provide a complete integrated communications solution to our business customers. The Business Solutions segment provided approximately 44% of 2016 segment operating revenues and 52% of our 2016 total Segment Contribution. We divide Business Solutions revenue into the following categories: wireless service, fixed strategic services, legacy voice and data services, other services and wireless equipment.

**Wireless Service** – We offer a comprehensive range of high-quality nationwide wireless voice and data communications services in a variety of pricing plans to approximately 81.4 million Business Solutions wireless subscribers. Our offerings are tailored to meet the communications needs of targeted customer categories. We classify our subscribers as either postpaid, connected device or reseller.

Wireless data services continue to be a growing area for this segment, representing an increasing share of overall subscriber revenue. We are experiencing solid growth in this area as an increasing number of our subscribers have upgraded their handsets to more advanced integrated devices, are using data-centric devices such as tablets and connected cars and are utilizing the network to connect and control physical devices using embedded computing systems and/or software, commonly called the Internet of Things (IoT). We offer both Mobile Share plans and an integrated offer combining unlimited wireless data with our video services. These plans allow sharing of voice, text and data across multiple devices. We also offer equipment installment programs, such as AT&T Next<sup>SM</sup> (AT&T Next), a program allowing subscribers to more frequently upgrade handsets using an installment payment plan; and Rollover Data on Mobile Share plans, which allows unused shareable plan data to be rolled over and used within the next month. Such offerings are intended to encourage existing subscribers to upgrade their current services and/or add connected devices, attract subscribers from other providers and minimize subscriber churn. Participation in these plans continues to increase. Customers in our "connected device" category (e.g., users of session-based tablets, monitoring devices and automobile systems) purchase those devices from third-party suppliers that buy data access supported by our network. We continue to upgrade our network and coordinate with equipment manufacturers and applications developers to further capitalize on the continued growing demand for wireless data services.

**AT&T Inc.**

---

During the first quarter of 2016, we discontinued offering subsidized smartphones to most of our customers. Under our no-subsidy model, subscribers must purchase a device under an equipment installment program or choose to bring their own device, with no annual service contract. Our wireless services include data and voice services, including long-distance service and roaming services. Roaming services enable our subscribers to utilize other carriers' networks when they are "roaming" outside our network footprint.

**Fixed Strategic Services** – Fixed strategic services (previously known as strategic business services) are our most advanced business solutions. Our offerings use high-capacity digital circuits, and allow customers to create internal data networks and access external data networks. Switched Transport services transmit data using switching equipment to transfer the data between multiple lines before reaching its destination. Dedicated transport services use a single direct line to transmit data between destinations. Due to advances in technology, our most advanced business solutions are subject to change periodically. We review and evaluate our fixed strategic service offerings annually, which may result in an updated definition and the recast of our historical financial information to conform to the current period presentation. Any modifications will be reflected in the first quarter.

We provide businesses voice applications over IP-based networks (i.e., Enhanced Virtual Private Networks or "EVPN"). Over the past several years, we have built out our new IP/MPLS (Internet Protocol/MultiProtocol Label Switching) network, to supplement our IP-based product set, and eventually replace our older circuit-based networks and services. These products allow us to provide highly complex global data networks. Additional IP-based services include internet access and network integration, network security, dedicated internet and enterprise networking services. These advanced IP-based services continued to grow during 2016 as customers shift from our older circuit-based services. We expect this trend to continue in 2017 as customers continue to use more services based on internet access and demand ever-increasing transmission speeds, especially for video. To align with these trends, we continue to reconfigure our wireline network to take advantage of the latest technologies and services.

Packet services consist of data networks using packet switching and transmission technologies, including traditional circuit-based and IP connectivity services. Packet services enable customers to transmit large volumes of data economically and securely and are used for local area network (LAN) interconnection and inter-office communications. High-speed packet services are used extensively by enterprise (large business) customers.

Enterprise networking services provide comprehensive support from network design, implementation and installation to ongoing network operations and management for networks of varying scales, including LANs and virtual private networks. These services include applications such as e-mail, order entry systems, employee directories, human resource transactions and other database applications. We also offer Wi-Fi service.

**Legacy Voice and Data Services** – Voice services include traditional local and long-distance service provided directly to business and governmental customers, or through wholesale arrangements with other service providers. Our circuit-based, traditional data products include switched and dedicated transport services that allow customers to transmit data at high speeds, as well as access the internet using a DSL connection.

Revenues from our traditional voice services continue to decline as customers switch to wireless or VoIP services provided by either us, cable companies or other internet-based providers. In addition, the continuing slow economic growth and business starts have led some wireline customers to terminate their business phone service. We have responded by offering packages of combined voice and data services, including broadband and video, and intend to continue this strategy during 2017.

**AT&T Inc.**

---

**Other Services** – Other service revenues include project-based revenue, which is nonrecurring in nature, as well as revenues from other managed services, outsourcing, government professional service and equipment.

We provide intrastate, interstate and international wholesale networking capacity to other service providers. We offer a combination of high-volume transmission capacity and conventional dedicated line services on a regional, national and international basis to our wholesale customers, which are primarily wireless carriers, interexchange carriers, Internet Service Providers (ISPs), and facility-based and switchless resellers.

**Wireless Equipment** – We sell a wide variety of handsets, wirelessly enabled computers (e.g., tablets and notebooks) and personal computer wireless data cards manufactured by various suppliers for use with our voice and data services. We sell through our own company-owned stores, agents and third-party retail stores. Like other wireless service providers, we have historically provided postpaid contract subscribers substantial equipment subsidies to initiate, renew or upgrade service. We have now largely eliminated these subsidies and provide our customers with more service options, the ability to purchase handsets on an installment basis and the opportunity to bring their own device. With the elimination of handset subsidies, our subscribers have been retaining their handsets for longer periods; accordingly, we expect equipment revenues to be pressured in 2017. We also sell accessories, such as carrying cases, hands-free devices and other items.

Additional information on our Business Solutions segment is contained in the Annual Report in the “Operating Environment Overview” section beginning on page 14 and is incorporated herein by reference pursuant to General Instruction G(2).

**ENTERTAINMENT GROUP**

Our Entertainment Group segment provides video, internet, voice communication, and interactive and targeted advertising services to customers in the United States and U.S. territories by utilizing our copper and IP-based wired network and/or our satellite technology. In July 2015, we acquired DIRECTV, a leading provider of digital television entertainment engaged in acquiring, promoting, selling and distributing digital entertainment programming primarily via satellite to subscribers. The Entertainment Group segment provided approximately 32% of 2016 segment operating revenues and 19% of our 2016 total Segment Contribution. We divide this segment’s revenue into the following categories: video entertainment, high-speed internet, legacy voice and data services, and equipment and other.

**Video Entertainment** – We offer video entertainment services using satellite and IP-based technologies (referred to as “linear”) as well as a streaming option that does not require either satellite or wired IP services (referred to as “over-the-top”). Our offerings are structured to provide customers with the best video experience both inside and outside of the home by offering subscribers attractive programming, technology and customer service. Due to the rising cost of programming as well as higher costs to acquire new subscribers in an increasingly competitive industry, it is even more important to distinguish and elevate our video entertainment experience for our new and existing customers.

We provide approximately 25.3 million subscribers with access to hundreds of channels of digital-quality video entertainment and audio programming. For our satellite subscribers, we provide video-on-demand (VOD) by “pushing” top-rated movies onto customers’ digital video recorders (DVRs) for instant viewing, as well as via broadband to our subscribers who have connected their set-top receiver to their broadband service. In addition, our video entertainment subscribers have the ability to use the internet and/or our mobile applications for smartphones and tablets to view authorized content, search program listings and schedule DVR recordings.

We believe it is critical that we continue to extend our brand leadership as the premium pay-TV provider in the marketplace by providing the best video experience both at home and on mobile devices. We believe that our flexible platform that uses a combination of satellite, IP-based and cloud infrastructure with a broadband and wireless connection is the most efficient way to transport content to subscribers when and where they want it. Through this integrated approach, we’re able to optimize the use of storage in the home as well as in the cloud, while also providing a seamless service for consumers across screens and locations.

**High-Speed Internet** – We offer broadband and internet services to 12.9 million residential subscribers. Our IP-based technology provides more advanced high-speed internet services.

**Legacy Voice and Data Services** – Voice services include traditional local and long-distance service provided to residential customers. Our circuit-based, traditional data products include DSL internet access.

**AT&T Inc.**

---

Revenues from our traditional voice services continue to decline as customers switch to wireless or VoIP services provided by either us, cable or other internet-based providers. We have responded by offering packages of combined voice and data services, including broadband, video and wireless, and intend to continue this strategy during 2017.

**Equipment and Other** – Other service revenues include revenue from voice services provided over IP-based technology (VoIP) as well as revenues associated with technical support and other customer service functions and equipment.

Additional information on our Entertainment Group segment is contained in the Annual Report in the “Operating Environment Overview” section beginning on page 16 and is incorporated herein by reference pursuant to General Instruction G(2).

**CONSUMER MOBILITY**

Our Consumer Mobility segment consists of AT&T Mobility operations that provide nationwide wireless services to consumers and wholesale and resale wireless subscribers located in the United States or U.S. territories by utilizing our network to provide voice and data services, including high-speed internet, video and home-monitoring services over wireless devices. Wireless services include data and voice, including long-distance and roaming services. Roaming services enable our subscribers to utilize other carriers’ networks when they are “roaming” outside our network footprint. The Consumer Mobility segment provided approximately 20% of 2016 total segment operating revenues and 31% of our 2016 total Segment Contribution. We classify our subscribers as either postpaid, prepaid, connected device or reseller. At December 31, 2016, we served 53.5 million Consumer Mobility subscribers, including 27.1 million postpaid, 13.5 million prepaid, 11.9 million reseller and 942,000 connected devices. We divide our revenue into the following categories: services and equipment.

**Wireless Services** – We offer a comprehensive range of high-quality nationwide wireless voice and data communications services in a variety of postpaid and prepaid pricing plans. Wireless data services continue to be a growing area of Consumer Mobility’s business, representing an increasing share of overall subscriber revenue. Subscribers continue to upgrade their handsets to more advanced integrated devices, contributing to growth from wireless data services. We offer Mobile Share plans and an integrated offer combining our unlimited wireless data with our video services. These plans allow sharing of voice, text and data across multiple devices. We also offer equipment installment programs, such as AT&T Next, a program allowing subscribers to more frequently upgrade handsets using an installment payment plan; and Rollover Data on Mobile Share plans, which allows unused shareable plan data to be rolled over and used within the next month. We also launched in 2016 a program for wireless subscribers that also purchase our video service to view such programming without it counting against their wireless data allowances. Such offerings are intended to encourage existing subscribers to upgrade their current services and/or add connected devices, attract subscribers from other providers, and minimize subscriber churn. Participation in these plans continues to increase. Customers in our “connected device” category (e.g., users of session-based tablets) purchase those devices from third-party suppliers that buy data access supported by our network. We continue to upgrade our network and coordinate with equipment manufacturers and applications developers in order to further capitalize on the continued growth in the demand for wireless data services.

During the first quarter of 2016, we discontinued offering subsidized smartphones to most of our customers. Under our no-subsidy model, subscribers must purchase a device under an equipment installment program or choose to bring their own device, with no annual service contract. Market maturity, competition and the migration of subscribers to employer plans offered by our Business Solutions segment have slowed the growth in subscribers.

We also offer nationwide wireless voice and data communications to certain customers who prefer to pay in advance. These services are offered under the Cricket and Go Phone brands and are typically monthly prepaid services.

**Other Service** – Other services includes consulting, advertising, application and co-location, as well as fees we charge to other carriers for providing roaming services to their customers utilizing our network.

**Equipment** – We sell a wide variety of handsets, wirelessly enabled computers (e.g., tablets and notebooks) and personal computer wireless data cards manufactured by various suppliers for use with our voice and data services. We sell through our own company-owned stores, agents and third-party retail stores. Like other wireless service providers, we have historically provided postpaid contract subscribers substantial equipment subsidies to initiate, renew or upgrade service. We have now largely eliminated these subsidies and provide our customers with more service options, the ability to purchase handsets on an installment basis and the opportunity to bring their own device. We also sell accessories, such as carrying cases, hands-free devices, and other items, to consumers, as well as to agents and third-party distributors for resale.

Additional information on our Consumer Mobility segment is contained in the Annual Report in the “Operating Environment Overview” section beginning on page 18 and is incorporated herein by reference pursuant to General Instruction G(2).

**AT&T Inc.**

---

**INTERNATIONAL**

Our International segment provides entertainment services in Latin America and wireless services in Mexico. Video entertainment services are provided to primarily residential customers using satellite technology. We utilize our regional and national wireless networks in Mexico to provide consumer and business customers with wireless data and voice communication services. The International segment provided approximately 4% of 2016 segment operating revenues. We divide our revenue into the following categories: video entertainment, wireless service and wireless equipment.

**Video Entertainment** – We are a leading provider of digital television services throughout Latin America, providing a wide selection of local and international digital-quality video entertainment and audio programming under the DIRECTV and SKY brands. We believe we provide one of the most extensive collections of programming available in the Latin America pay-TV market, including HD sports video content and the most innovative interactive technology across the region. In addition, we have the unique ability to sell superior offerings of our differentiated products and services on a continent-wide basis with an operational cost structure that we believe to be lower than that of our competition.

We have approximately 12.5 million video subscribers in Latin America. Our operations are comprised of: PanAmericana, which provides services in Argentina, Chile, Colombia, Ecuador, Peru, Venezuela and certain other countries in the region; and SKY Brasil Servicos Ltda., or SKY Brasil, which is a 93% owned subsidiary. Our Latin American operations also include our 41% equity method investment in Innova. S. de R.L. de C.V., or SKY Mexico, which we include in our International segment. As of December 31, 2016, PanAmericana had approximately 7.2 million subscribers and SKY Brasil had approximately 5.3 million subscribers.

**Wireless** – We offer postpaid and prepaid wireless services in Mexico to approximately 12.0 million subscribers under the AT&T and Unefon brands. Postpaid services allow for (1) no annual service contract for subscribers who bring their own device or purchase a device on installment (the device must be paid in full if the customer chooses to drop their service from AT&T); and (2) service contracts for periods up to 24 months for subscribers who purchase their equipment under the traditional device subsidy model. All plans offer no roaming charges in the United States or Canada, unlimited minutes and messages to the extended AT&T community and unlimited social networking. We also offer prepaid services to certain customers who prefer to pay in advance.

**Equipment** – We sell a wide variety of handsets, including smartphones manufactured by various suppliers for use with our voice and data services. We sell through our own company-owned stores, agents and third-party retail stores.

Additional information on our International segment is contained in the Annual Report in the “Operating Environment Overview” section beginning on page 20 and is incorporated herein by reference pursuant to General Instruction G(2).

AT&amp;T Inc.

**MAJOR CLASSES OF SERVICE**

The following table sets forth the percentage of total consolidated reported operating revenues by any class of service that accounted for 10% or more of our consolidated total operating revenues in any of the last three fiscal years:

	Percentage of Total Consolidated Operating Revenues		
	2016	2015	2014
<b>Business Solutions Segment</b>			
Wireless service	19 %	21 %	23 %
Legacy voice and data services	10	12	15
Equipment <sup>1</sup>	5	6	6
<b>Entertainment Group Segment</b>			
Video entertainment	22	14	5
Legacy voice and data services	3	4	6
<b>Consumer Mobility Segment</b>			
Wireless service	17	20	23
Equipment	3	4	4
<b>International Segment</b>			
Video entertainment	3	1	-

<sup>1</sup> Includes customer premises equipment of \$982 million in 2016, \$929 million in 2015 and \$979 million in 2014 that is reported as other service and equipment revenues in our Business Solutions segment.

Additional information on our geographical distribution of revenues is contained in the Annual Report in the "Segment Information" section beginning on page 54 and is incorporated herein by reference pursuant to General Instruction G(2).

**GOVERNMENT REGULATION**

Wireless communications providers must be licensed by the U.S. Federal Communications Commission (FCC) to provide communications services at specified spectrum frequencies within defined geographic areas and must comply with the rules and policies governing the use of the spectrum as adopted by the FCC. The FCC's rules have a direct impact on whether the wireless industry has sufficient spectrum available to support the high-quality, innovative services our customers demand. Wireless licenses are issued for a fixed time period, typically 10 years, and we must seek renewal of these licenses. While the FCC has generally renewed licenses given to operating companies such as us, the FCC has authority to both revoke a license for cause and to deny a license renewal if a renewal is not in the public interest. Additionally, while wireless communications providers' prices and service offerings are generally not subject to regulation, the federal government and various states are considering new regulations and legislation relating to various aspects of wireless services.

The Communications Act of 1934 and other related acts give the FCC broad authority to regulate the U.S. operations of our satellite services, which are licensed by the FCC. In addition, states representing a majority of our local service access lines have adopted legislation that enables us to provide IP-based video service through a single statewide or state-approved franchise (as opposed to the need to acquire hundreds or even thousands of municipal-approved franchises) to offer a competitive video product. We also are supporting efforts to update and improve regulatory treatment for retail services. Regulatory reform and passage of legislation is uncertain and depends on many factors.

In February 2015, the FCC released an order in response to the D.C. Circuit's January 2014 decision adopting new rules, and classifying both fixed and mobile consumer broadband internet access as telecommunications services, subject to comprehensive regulation under the Telecommunications Act of 1996. The FCC's decision significantly expands its existing authority to regulate the provision of fixed and mobile broadband internet access services. The FCC also asserted jurisdiction over internet interconnection arrangements, which until now have been unregulated. These actions could have an adverse impact on our fixed and mobile broadband services and operating results. AT&T and several other parties, including US Telecom and CTIA trade groups, have challenged the FCC's order.

**AT&T Inc.**

---

Our ILEC subsidiaries are subject to regulation by state governments, which have the power to regulate intrastate rates and services, including local, long-distance and network access services, provided such state regulation is consistent with federal law. Some states have eliminated or reduced regulations on our retail offerings. These subsidiaries are also subject to the jurisdiction of the FCC with respect to intercarrier compensation, interconnection, and interstate and international rates and services, including interstate access charges. Access charges are a form of intercarrier compensation designed to reimburse our wireline subsidiaries for the use of their networks by other carriers.

Our subsidiaries operating outside the United States are subject to the jurisdiction of national and supranational regulatory authorities in the market where service is provided.

Additional information relating to regulation of our subsidiaries is contained in the Annual Report under the headings "Operating Environment Overview" beginning on page 24 and "Regulatory Developments" beginning on page 27 and is incorporated herein by reference pursuant to General Instruction G(2).

**IMPORTANCE, DURATION AND EFFECT OF LICENSES**

Certain of our subsidiaries own or have licenses to various patents, copyrights, trademarks and other intellectual property necessary to conduct business. Many of our subsidiaries also hold government-issued licenses or franchises to provide wireline, satellite or wireless services and additional information relating to regulation affecting those rights is contained in the Annual Report under the heading "Operating Environment Overview" beginning on page 24 and is incorporated herein by reference pursuant to General Instruction G(2). We actively pursue patents, trademarks and service marks to protect our intellectual property within the United States and abroad. We maintain a significant global portfolio of patents, trademarks and service mark registrations. We have also entered into agreements that permit other companies, in exchange for fees and subject to appropriate safeguards and restrictions, to utilize certain of our trademarks and service marks. We periodically receive offers from third parties to obtain licenses for patents and other intellectual rights in exchange for royalties or other payments. We also receive notices asserting that our products or services infringe on their patents and other intellectual property rights. These claims, whether against us directly or against third-party suppliers of products or services that we, in turn, sell to our customers, such as wireless handsets, could require us to pay damages, royalties, stop offering the relevant products or services and/or cease other activities. While the outcome of any litigation is uncertain, we do not believe that the resolution of any of these infringement claims or the expiration or non-renewal of any of our intellectual property rights would have a material adverse effect on our results of operations.

**MAJOR CUSTOMER**

No customer accounted for 10% or more of our consolidated revenues in 2016, 2015 or 2014.

**COMPETITION**

Information relating to competition in each of our operating segments is contained in the Annual Report under the heading "Competition" beginning on page 27, and is incorporated herein by reference pursuant to General Instruction G(2).

**AT&T Inc.**

---

**RESEARCH AND DEVELOPMENT**

AT&T scientists and engineers conduct research in a variety of areas, including IP networking, advanced network design and architecture, network and cyber security, network operations support systems, satellite technology and data analytics. The majority of the development activities are performed to create new services and to invent tools and systems to manage secure and reliable networks for us and our customers. In recent years, we initiated a technology outreach effort aimed at venture capital funded startups with the objective of rapidly introducing new solutions, products and applications developed by third parties. Research and development expenses were \$1.649 million in 2016, \$1.693 million in 2015, and \$1.730 million in 2014.

**EMPLOYEES**

As of January 31, 2017, we employed approximately 268,000 persons. Approximately 48% of our employees are represented by the Communications Workers of America, the International Brotherhood of Electrical Workers or other unions. Contracts covering approximately 20,000 mobility employees across the country and approximately 25,000 traditional wireline employees in our Southwest and Midwest regions will expire in 2017. Additionally, negotiations continue with approximately 15,000 traditional wireline employees in our West region where the contract expired in April 2016. Approximately 11,000 former DIRECTV employees were eligible for and chose union representation. Bargaining has resulted in approximately 70% of these employees now being covered under ratified contracts that expire between 2017 and 2020. After expiration of the current agreements, work stoppages or labor disruptions may occur in the absence of new contracts or other agreements being reached.

At December 31, 2016, we had approximately 533,000 retirees and dependents that were eligible to receive retiree benefits.

AT&amp;T Inc.

**ITEM IA. RISK FACTORS**

Information required by this Item is included in the Annual Report under the heading "Risk Factors" on pages 39 through 43 which is incorporated herein by reference pursuant to General Instruction G(2).

**CAUTIONARY LANGUAGE CONCERNING FORWARD-LOOKING STATEMENTS**

Information set forth in this report contains forward-looking statements that are subject to risks and uncertainties, and actual results could differ materially. Many of these factors are discussed in more detail in the "Risk Factors" section. We claim the protection of the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995.

The following factors could cause our future results to differ materially from those expressed in the forward-looking statements:

- Adverse economic and/or capital access changes in the markets served by us or in countries in which we have significant investments, including the impact on customer demand and our ability and our suppliers' ability to access financial markets at favorable rates and terms.
- Changes in available technology and the effects of such changes, including product substitutions and deployment costs.
- Increases in our benefit plans' costs, including increases due to adverse changes in the United States and foreign securities markets, resulting in worse-than-assumed investment returns and discount rates; adverse changes in mortality assumptions; adverse medical cost trends; and unfavorable or delayed implementation or repeal of healthcare legislation, regulations or related court decisions.
- The final outcome of FCC and other federal, state or foreign government agency proceedings (including judicial review, if any, of such proceedings) involving issues that are important to our business, including, without limitation, special access and business data services; intercarrier compensation; interconnection obligations; pending Notices of Apparent Liability; the transition from legacy technologies to IP-based infrastructure, including the withdrawal of legacy TDM-based services; universal service; broadband deployment; E911 services; competition policy; privacy net neutrality, including the FCC's order classifying broadband as Title II services subject to much more comprehensive regulation; unbundled network elements and other wholesale obligations; multi-channel video programming distributor services and equipment; availability of new spectrum, on fair and balanced terms; and wireless and satellite license awards and renewals.
- The final outcome of state and federal legislative efforts involving issues that are important to our business, including deregulation of IP-based services, relief from Carrier of Last Resort obligations and elimination of state commission review of the withdrawal of services.
- Enactment of additional state, local, federal and/or foreign regulatory and tax laws and regulations, or changes to existing standards and actions by tax agencies and judicial authorities including the resolution of disputes with any taxing jurisdictions, pertaining to our subsidiaries and foreign investments, including laws and regulations that reduce our incentive to invest in our networks, resulting in lower revenue growth and/or higher operating costs.
- Our ability to absorb revenue losses caused by increasing competition, including offerings that use alternative technologies or delivery methods (e.g., cable, wireless, VoIP and over-the-top video service) and our ability to maintain capital expenditures.
- The extent of competition including from governmental networks and other providers and the resulting pressure on customer and access line totals and segment operating margins.
- Our ability to develop attractive and profitable product/service offerings to offset increasing competition.
- The ability of our competitors to offer product/service offerings at lower prices due to lower cost structures and regulatory and legislative actions adverse to us, including state regulatory proceedings relating to unbundled network elements and non-regulation of comparable alternative technologies (e.g., VoIP).
- The continued development and delivery of attractive and profitable video offerings through satellite and IP-based networks; the extent to which regulatory and build-out requirements apply to our offerings; and the availability, cost and/or reliability of the various technologies and/or content required to provide such offerings.
- Our continued ability to maintain margins, attract and offer a diverse portfolio of wireless service and devices and device financing plans.
- The availability and cost of additional wireless spectrum and regulations and conditions relating to spectrum use, licensing, obtaining additional spectrum, technical standards and deployment and usage, including network management rules.
- Our ability to manage growth in wireless video and data services, including network quality and acquisition of adequate spectrum at reasonable costs and terms.
- The outcome of pending, threatened or potential litigation (which includes arbitrations), including, without limitation, patent and product safety claims by or against third parties.
- The impact from major equipment failures on our networks, including satellites operated by DIRECTV; the effect of security breaches related to the network or customer information; our inability to obtain handsets, equipment/software or have handsets, equipment/software serviced in a timely and cost-effective manner from suppliers; and in the case of satellites launched, timely provisioning of services from vendors; or severe weather conditions, natural disasters, pandemics, energy shortages, wars or terrorist attacks.
- The issuance by the Financial Accounting Standards Board or other accounting oversight bodies of new accounting standards or changes to existing standards.
- Our ability to integrate our acquisition of DIRECTV.
- Our ability to close our pending acquisition of Time Warner Inc. and successfully integrate its operations.
- Our ability to adequately fund our wireless operations, including payment for additional spectrum, network upgrades and technological advancements.
- Our increased exposure to video competition and foreign economics due to our recent acquisitions of DIRECTV and Mexican wireless properties, including foreign exchange fluctuations as well as regulatory and political uncertainty.
- Changes in our corporate strategies, such as changing network-related requirements or acquisitions and dispositions, which may require significant amounts of cash or stock, to respond to competition and regulatory, legislative and technological developments.
- The uncertainty surrounding further congressional action to address spending reductions, which may result in a significant decrease in government spending and reluctance of businesses and consumers to spend in general.

- The uncertainty and impact of anticipated regulatory and corporate tax reform, which may impact the overall economy and incentives for business investments.

Readers are cautioned that other factors discussed in this report, although not enumerated here, also could materially affect our future earnings.

**AT&T Inc.****ITEM 2. PROPERTIES**

Our properties do not lend themselves to description by character and location of principal units. At December 31, 2016, central office equipment represented 29%; outside plant (including cable, wiring and other non-central office network equipment) represented approximately 25%; satellites represented 1%; other equipment, comprised principally of wireless network equipment attached to towers, furniture and office equipment and vehicles and other work equipment, represented 27%; land, building and wireless communications towers represented 12%; and other miscellaneous property represented 6%.

Substantially all of the installations of central office equipment are located in buildings and on land we own. Many garages, administrative and business offices, wireless towers, telephone centers and retail stores are leased. Property on which communication towers are located may be either owned or leased.

**ITEM 3. LEGAL PROCEEDINGS**

We are a party to numerous lawsuits, regulatory proceedings and other matters arising in the ordinary course of business. As of the date of this report, we do not believe any pending legal proceedings to which we or our subsidiaries are subject are required to be disclosed as material legal proceedings pursuant to this item.

We are subject from time to time to judicial and administrative proceedings brought by various governmental authorities under federal, state or local environmental laws. We are required to discuss three of these proceedings in our Forms 10-Q and 10-K, because each could result in monetary sanctions (exclusive of interest and costs) of \$100,000 or more. However, we do not believe that any of them currently pending will have a material adverse effect on our results of operations.

- (a) **Waste Disposal Inquiry Involving DIRECTV** In August 2012, a unit organized by the California Attorney General and the District Attorney for Alameda County, California notified DIRECTV that the unit was examining allegations that DIRECTV had failed to properly manage, store, transport and dispose of Hazardous and Universal Waste in accordance with the California Health & Safety Code. No litigation has been filed. DIRECTV is cooperating with the unit and is seeking to resolve all claims. A monetary settlement has been proposed and agreed to in principle by DIRECTV in an amount that is not material. Negotiation of final terms is proceeding.
- (b) **San Diego County Inquiry Involving Cricket Communications, Inc.** In February 2014, the San Diego County Air Pollution Control District began inquiring into alleged violations of California regulations governing removal, handling and disposal of asbestos containing materials arising from an independent dealer's demolition and construction activity in preparation to install upgraded point of purchase and fixtures in accordance with Cricket Dealer Guidelines. While the independent dealer was in sole control of contractors performing the work at issue, the County has focused on Cricket Communications dealer agreement terms and interactions with the independent dealer as a basis for asserting direct liability against Cricket Communications, Inc. After discussions, in November 2015, the County issued a penalty demand in excess of \$100,000. In October 2016, we reached a monetary settlement with the County of this matter for an immaterial amount.
- (c) **South Coast Air Quality** In January 2016, AT&T Mobility received an offer to enter into an administrative settlement with California's South Coast Air Quality Management District associated with a Notice of Violation (NOV) received in 2015. The 2015 NOV alleged violations of local environmental air permitting and emissions rules issued by the District in connection with operation of a back-up power generator system at one AT&T Mobility facility. After discussions, the parties resolved the alleged violations without admission of fault by AT&T Mobility for a payment of civil penalties in an amount of less than \$100,000.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

**AT&T Inc.**

---

**EXECUTIVE OFFICERS OF THE REGISTRANT  
(As of February 1, 2017)**

<u>Name</u>	<u>Age</u>	<u>Position</u>	<u>Held Since</u>
Randall L. Stephenson	56	Chairman of the Board, Chief Executive Officer and President	6/2007
F. Thaddeus Arroyo	53	Chief Executive Officer – Business Solutions and International	1/2017
William A. Blase Jr.	61	Senior Executive Vice President – Human Resources	6/2007
John M. Donovan	56	Chief Strategy Officer and Group President – AT&T Technology and Operations	2/2016
David S. Huntley	58	Senior Executive Vice President and Chief Compliance Officer	12/2014
Lori M. Lee	51	Senior Executive Vice President and Global Marketing Officer	4/2015
David R. McAtee II	48	Senior Executive Vice President and General Counsel	10/2015
Robert W. Quinn Jr.	56	Senior Executive Vice President – External and Legislative Affairs. AT&T Services, Inc.	10/2016
John T. Stankey	54	Chief Executive Officer-AT&T Entertainment Group, AT&T Services, Inc.	7/2015
John J. Stephens	57	Senior Executive Vice President and Chief Financial Officer	6/2011

All of the above executive officers have held high-level managerial positions with AT&T or its subsidiaries for more than the past five years. Executive officers are not appointed to a fixed term of office.

AT&amp;T Inc.

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

(a) Our common stock is listed on the New York Stock Exchange. The number of stockholders of record as of December 31, 2016 and 2015 was 1,020,203 and 1,074,894. The number of stockholders of record as of February 10, 2017, was 1,015,975. We declared dividends, on a quarterly basis, totaling \$1.93 per share in 2016 and \$1.89 per share in 2015.

Other information required by this Item is included in the Annual Report under the headings "Quarterly Financial Information" on page 83, "Selected Financial and Operating Data" on page 10, and "Stock Trading Information" on the back cover, which are incorporated herein by reference pursuant to General Instruction G(2).

(c) In July 2012, the Board of Directors approved an authorization to repurchase 300 million shares, which we completed in May 2013. In March 2013, our Board of Directors approved an authorization to repurchase up to an additional 300 million shares of our common stock. In March 2014, our Board of Directors approved another authorization to repurchase up to an additional 300 million shares of our common stock. For the year ended December 31, 2016, we repurchased 11 million shares for distribution through our employee benefit plans, totaling \$444 million under the March 2013 authorization. For the year ended December 31, 2015, we repurchased 8 million shares totaling \$269 million under the March 2013 authorization. The emphasis of our 2017 financing activities will be the issuance of debt and the payment of dividends, subject to approval by our Board of Directors, and the repayment of debt.

To implement these authorizations, we used open market repurchase programs, relying on Rule 10b5-1 of the Securities Exchange Act of 1934 where feasible.

We will continue to fund any share repurchases through a combination of cash from operations, borrowings dependent on market conditions, or cash from the disposition of certain non-strategic investments.

A summary of our repurchases of common stock during the fourth quarter of 2016 is as follows:

## ISSUER PURCHASES OF EQUITY SECURITIES

Period	(a) Total Number of Shares (or Units) Purchased <sup>1,2,3</sup>	(b) Average Price Paid Per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs <sup>1</sup>	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) That May Yet Be Purchased Under The Plans or Programs
October 1, 2016 - October 31, 2016	45,330	\$ -	-	395,550,000
November 1, 2016 - November 30, 2016	1,841,719	-	-	395,550,000
December 1, 2016 - December 31, 2016	528,674	-	-	395,550,000
<b>Total</b>	<b>2,415,723</b>	<b>\$ -</b>	<b>-</b>	

<sup>1</sup> In March 2014, our Board of Directors approved an authorization to repurchase up to 300 million shares of our common stock. In March 2013, our Board of Directors approved an authorization to repurchase up to 300 million shares of our common stock. The authorizations have no expiration date.

<sup>2</sup> Of the shares purchased, 73,743 shares were acquired through the withholding of taxes on the vesting of restricted stock or through the payment in stock of taxes on the exercise price of options.

<sup>3</sup> Of the shares repurchased, 2,341,980 were acquired through reimbursements from the AT&T maintained Voluntary Employee Benefit Association (VEBA) trusts or through litigation settlement.

**AT&T Inc.**

---

**ITEM 6. SELECTED FINANCIAL DATA**

Information required by this Item is included in the Annual Report under the heading "Selected Financial and Operating Data" on page 10, which is incorporated herein by reference pursuant to General Instruction G(2).

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Information required by this Item is included in the Annual Report on pages 11 through 44, which is incorporated herein by reference pursuant to General Instruction G(2).

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Information required by this Item is included in the Annual Report under the heading "Market Risk" on page 38, which is incorporated herein by reference pursuant to General Instruction G(2).

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

Information required by this Item is included in the Annual Report on pages 45 through 83, which is incorporated herein by reference pursuant to General Instruction G(2).

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

During our two most recent fiscal years, there has been no change in the independent accountant engaged as the principal accountant to audit our financial statements, and the independent accountant has not expressed reliance on other independent accountants in its reports during such time period.

**ITEM 9A. CONTROLS AND PROCEDURES****Disclosure Controls and Procedures**

The registrant maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed by the registrant is recorded, processed, summarized, accumulated and communicated to its management, including its principal executive and principal financial officers, to allow timely decisions regarding required disclosure, and reported within the time periods specified in the SEC's rules and forms. The Chief Executive Officer and Chief Financial Officer have performed an evaluation of the effectiveness of the design and operation of the registrant's disclosure controls and procedures as of December 31, 2016. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the registrant's disclosure controls and procedures were effective as of December 31, 2016.

**Internal Control Over Financial Reporting****(a) Management's Annual Report on Internal Control over Financial Reporting**

The management of AT&T is responsible for establishing and maintaining adequate internal control over financial reporting. AT&T's internal control system was designed to provide reasonable assurance as to the integrity and reliability of the published financial statements. AT&T management assessed the effectiveness of the company's internal control over financial reporting as of December 31, 2016. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control – Integrated Framework* (2013 framework). Based on its assessment, AT&T management believes that, as of December 31, 2016, the Company's internal control over financial reporting is effective based on those criteria.

**(b) Attestation Report of the Independent Registered Public Accounting Firm**

The independent registered public accounting firm that audited the financial statements included in the Annual Report containing the disclosure required by this Item, Ernst & Young LLP, has issued an attestation report on the Company's internal control over financial reporting. The attestation report issued by Ernst & Young LLP is included in the Annual Report on page 85, which is incorporated herein by reference pursuant to General Instruction G(2).

**AT&T Inc.**

---

**ITEM 9B. OTHER INFORMATION**

There is no information that was required to be disclosed in a report on Form 8-K during the fourth quarter of 2016 but was not reported.

**PART III****ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Information regarding executive officers required by Item 401 of Regulation S-K is furnished in a separate disclosure at the end of Part I of this report since the registrant did not furnish such information in its definitive proxy statement prepared in accordance with Schedule 14A. Information regarding directors required by Item 401 of Regulation S-K is incorporated herein by reference pursuant to General Instruction G(3) from the registrant's definitive proxy statement, dated on or about March 10, 2017 (Proxy Statement) under the heading "Management Proposal Item 1. Election of Directors."

Information required by Item 405 of Regulation S-K is incorporated herein by reference pursuant to General Instruction G(3) from the registrant's Proxy Statement under the heading "Section 16(a) Beneficial Ownership Reporting Compliance."

The registrant has a separately-designated standing audit committee established in accordance with Section 3(a)(58)(A) of the Securities Exchange Act of 1934. The members of the committee are Messrs. Di Piazza, Jr. and McCallister, and Mses. Taylor and Tyson. The additional information required by Item 407(d)(5) of Regulation S-K is incorporated herein by reference pursuant to General Instruction G(3) from the registrant's Proxy Statement under the heading "Audit Committee."

The registrant has adopted a code of ethics entitled "Code of Ethics" that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer, or controller or persons performing similar functions. The additional information required by Item 406 of Regulation S-K is provided in this report under the heading "General" under Part I, Item 1. Business.

**ITEM 11. EXECUTIVE COMPENSATION**

Information required by Item 402(k) of Regulation S-K is incorporated herein by reference pursuant to General Instruction G(3) from the registrant's Proxy Statement under the heading "Director Compensation." Information regarding officers is included in the registrant's Proxy Statement on the pages beginning with the heading "Compensation Discussion and Analysis" and ending with, and including, the pages under the heading "Potential Payments upon Change in Control" which are incorporated herein by reference pursuant to General Instruction G(3). Information required by Item 407(e)(5) of Regulation S-K is included in the registrant's Proxy Statement under the heading "Compensation Committee Report" and is incorporated herein by reference pursuant to General Instruction G(3) and shall be deemed furnished in this Annual Report on Form 10-K and will not be deemed incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934.

Information required by this Item is included in the registrant's Proxy Statement, under the heading "Director Compensation," and the pages beginning with the heading "Summary Compensation Table," and ending with, and including, the page immediately before the heading "Cost of Proxy Solicitation" which are incorporated herein by reference pursuant to General Instruction G(3).

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Information required by Item 403 of Regulation S-K is included in the registrant's Proxy Statement under the heading "Common Stock Ownership," which is incorporated herein by reference pursuant to General Instruction G(3).

**AT&T Inc.****Equity Compensation Plan Information**

The following table provides information as of December 31, 2016, concerning shares of AT&T common stock authorized for issuance under AT&T's existing equity compensation plans.

<b>Equity Compensation Plan Information</b>			
<b>Plan Category</b>	<b>Number of securities to be issued upon exercise of outstanding options, warrants and rights</b>	<b>Weighted-average exercise price of outstanding options, warrants and rights</b>	<b>Number of securities remaining available for future issuance under equity compensation Plans (excluding securities reflected in column (a))</b>
	(a)	(b)	(c)
Equity compensation plans approved by security holders	38,989,880 (1)	29.46	129,216,883(2)
Equity compensation plans not approved by security holders	-	-	-
<b>Total</b>	<b>38,989,880 (3)</b>	<b>\$29.46</b>	<b>129,216,883 (2)</b>

(1) Includes stock to be issued in connection with the following stockholder approved plans: (a) 5,684,800 stock options under the Stock Purchase and Deferral Plan (SPDP), (b) 2,086,954 phantom stock units under the Stock Savings Plan (SSP), 10,124,461 phantom stock units under the SPDP, 13,515 restricted stock units under the 2016 Incentive Plan, and 6,094,321 restricted stock units under the 2011 Incentive Plan, and (c) 6,022 target number of stock-settled performance shares under the 2016 Incentive Plan, and 12,690,355 target number of stock-settled performance shares under the 2011 Incentive Plan. At payout, the target number of performance shares may be reduced to zero or increased by up to 150%. Each phantom stock unit and performance share is settleable in stock on a 1-to-1 basis. The weighted-average exercise price in the table does not include outstanding performance shares or phantom stock units.

The SSP was approved by stockholders in 1994 and then was amended by the Board of Directors in 2000 to increase the number of shares available for purchase under the plan (including shares from the Company match and reinvested dividend equivalents). Stockholder approval was not required for the amendment. To the extent applicable, the amount shown for approved plans in column (a), in addition to the above amounts, includes 2,289,453 phantom stock units (computed on a first-in-first-out basis) that were approved by the Board in 2000. Under the SSP, shares could be purchased with payroll deductions and reinvested dividend equivalents by mid-level and above managers and limited Company partial matching contributions. No new contributions may be made to the plan.

(2) Includes 20,429,062 shares that remain available for future issuance under the SPDP, 88,541,244 shares remaining under the 2011 Incentive Plan, and up to 2,943,330 shares that may be purchased through reinvestment of dividends on phantom shares held in the SSP.

(3) Does not include certain stock options issued by companies acquired by AT&T that were converted into options to acquire AT&T stock. As of December 31, 2016, there were 640,749 shares of AT&T common stock subject to the converted options, having a weighted-average exercise price of \$19.34. Also, does not include 3,570,683 outstanding phantom stock units that were issued by companies acquired by AT&T that are convertible into stock on a 1-to-1 basis, along with up to 120,227 shares that may be purchased with reinvested dividend equivalents paid on the outstanding phantom stock units. No further phantom stock units, other than reinvested dividends, may be issued under the assumed plans. The weighted-average exercise price in the table does not include outstanding performance shares or phantom stock units.

**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

Information required by Item 404 of Regulation S-K is included in the registrant's Proxy Statement under the heading "Related Person Transactions Disclosure," which is incorporated herein by reference pursuant to General Instruction G(3). Information required by Item 407(a) of Regulation S-K is included in the registrant's Proxy Statement under the heading "Director Independence," which is incorporated herein by reference pursuant to General Instruction G(3).

**AT&T Inc.****ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

Information required by this Item is included in the registrant's Proxy Statement under the heading "Principal Accountant Fees and Services," which is incorporated herein by reference pursuant to General Instruction G(3).

**Part IV****ITEM 15. EXHIBITS and FINANCIAL STATEMENT SCHEDULES**

(a) Documents filed as a part of the report:

	Page
(1) Report of Independent Registered Public Accounting Firm	*
Financial Statements covered by Report of Independent Registered Public Accounting Firm:	*
Consolidated Statements of Income	*
Consolidated Statements of Comprehensive Income	*
Consolidated Balance Sheets	*
Consolidated Statements of Cash Flows	*
Consolidated Statements of Changes in Stockholders' Equity	*
Notes to Consolidated Financial Statements	

\* Incorporated herein by reference to the appropriate portions of the registrant's Annual Report to Stockholders for the fiscal year ended December 31, 2016. (See Part II.)

	Page
(2) Financial Statement Schedules:	23
II - Valuation and Qualifying Accounts	

Financial statement schedules other than those listed above have been omitted because the required information is contained in the financial statements and notes thereto, or because such schedules are not required or applicable.

**(3) Exhibits:**

Exhibits identified in parentheses below, on file with the SEC, are incorporated herein by reference as exhibits hereto. Unless otherwise indicated, all exhibits so incorporated are from File No. 1-8610.

Exhibit Number	
2	Agreement and Plan of Merger, dated as of October 22, 2016, among AT&T Inc., Time Warner Inc. and West Merger Sub, Inc. (Exhibit 10.1 to Form 8-K dated October 24, 2016.)
3-a	Restated Certificate of Incorporation, filed with the Secretary of State of Delaware on December 13, 2013. (Exhibit 3.1 to Form 8-K dated December 13, 2013.)
3-b	Bylaws amended December 18, 2015. (Exhibit 3 to Form 8-K dated December 18, 2015.)
4-a	No instrument which defines the rights of holders of long-term debt of the registrant and all of its consolidated subsidiaries is filed herewith pursuant to Regulation S-K, Item 601(b)(4)(iii)(A), except for the instruments referred to in 4-b, 4-c, 4-d, 4-e, 4-f, 4-g, 4-h, 4-i, and 4-j below. Pursuant to this regulation, the registrant hereby agrees to furnish a copy of any such instrument not filed herewith to the SEC upon request.
4-b	Guaranty of certain obligations of Pacific Bell Telephone Co. and Southwestern Bell Telephone Co. (Exhibit 4-c to Form 10-K for 2011.)

**AT&T Inc.**

---

- 4-c Guaranty of certain obligations of Ameritech Capital Funding Corp., Indiana Bell Telephone Co. Inc., Michigan Bell Telephone Co., Pacific Bell Telephone Co., Southwestern Bell Telephone Company, Illinois Bell Telephone Company, The Ohio Bell Telephone Company, The Southern New England Telephone Company, Southern New England Telecommunications Corporation, and Wisconsin Bell, Inc. (Exhibit 4-d to Form 10-K for 2011.)
- 4-d Guarantee of certain obligations of AT&T Corp. (Exhibit 4-e to Form 10-K for 2011.)
- 4-e Indenture, dated as of May 15, 2013, between AT&T Inc. and The Bank of New York Mellon Trust Company, N.A. as Trustee. (Exhibit 4.1 to Form 8-K dated May 15, 2013.)
- 4-f Indenture dated as of November 1, 1994 between SBC Communications Inc. and The Bank of New York, as Trustee. (Exhibit 4-h to Form 10-K for 2013.)
- 10-a 2016 Incentive Plan (Exhibit 10-a to Form 10-Q filed for March 31, 2016.)
- 10-b 2011 Incentive Plan, amended September 24, 2015. (Exhibit 10-a to Form 10-Q filed for September 30, 2015.)
- 10-c Supplemental Life Insurance Plan, amended September 24, 2015. (Exhibit 10-c to Form 10-Q filed for September 30, 2015.)
- 10-d Supplemental Retirement Income Plan, amended December 31, 2008. (Exhibit 10-e to Form 10-K for 2013.)
- 10-e 2005 Supplemental Employee Retirement Plan, amended December 18, 2014. (Exhibit 10.1 to Form 8-K dated December 18, 2014.)
- 10-f Senior Management Deferred Compensation Program of 1988 (effective for Units of Participation Having a Unit Start Date of January 1, 1988 or later) as amended through April 1, 2002. (Exhibit 10-g to Form 10-K for 2013.)
- 10-g Salary and Incentive Award Deferral Plan, amended December 31, 2004. (Exhibit 10-k to Form 10-K for 2011.)
- 10-h Stock Savings Plan, amended December 31, 2004. (Exhibit 10-l to Form 10-K for 2011.)
- 10-i Stock Purchase and Deferral Plan, amended September 24, 2015. (Exhibit 10-d to Form 10-Q filed for September 30, 2015.)
- 10-j Cash Deferral Plan, amended September 24, 2015. (Exhibit 10-c to Form 10-Q filed for September 30, 2015.)
- 10-k Master Trust Agreement for AT&T Inc. Deferred Compensation Plans and Other Executive Benefit Plans and subsequent amendments dated August 1, 1995 and November 1, 1999. (Exhibit 10-dd to Form 10-K for 2009.)
- 10-l Officer Disability Plan, amended January 1, 2010. (Exhibit 10-i to Form 10-Q filed for June 30, 2009.)
- 10-m AT&T Inc. Health Plan, amended January 1, 2017. (Exhibit 10-a to Form 10-Q filed for September 30, 2016.)
- 10-n Pension Benefit Makeup Plan No.1, amended December 31, 2016.

**AT&T Inc.**

- 10-o AT&T Inc. Equity Retention and Hedging Policy. (Exhibit 10.2 to Form 8-K dated December 15, 2011.)
- 10-p Administrative Plan, amended September 24, 2015.
- 10-q AT&T Inc. Non-Employee Director Stock and Deferral Plan, amended September 25, 2015. (Exhibit 99.1 to Form 8-K dated September 25, 2015.)
- 10-r AT&T Inc. Non-Employee Director Stock Purchase Plan, dated June 27, 2008. (Exhibit 10-t to Form 10-K for 2013.)
- 10-s Communications Concession Program for Directors, amended and restated February 1, 2013. (Exhibit 10-aa to Form 10-K for 2012.)
- 10-t Form of Indemnity Agreement, effective July 1, 1986, between SBC (now AT&T Inc.) and its directors and officers. (Exhibit 10-bb to Form 10-K for 2011.)
- 10-u Transition Agreement by and between BellSouth Corporation and Rafael de la Vega, dated December 29, 2003. (Exhibit 10-cc to Form 10-K for 2011.)
- 10-v AT&T Corp. Executive Deferred Compensation Plan (formerly known as AT&T Corp. Senior Management Incentive Award Deferral Plan), amended and restated January 1, 2008. (Exhibit 10-aa to Form 10-K for 2013.)
- 10-w Master Trust Agreement for AT&T Corp. Deferred Compensation Plans and Other Executive Benefit Plans, effective January 13, 1994. (Exhibit 10-nn to Form 10-K for 2011.)
- 10-w(i) First Amendment to Master Trust Agreement, effective December 23, 1997. (Exhibit 10-nn(i) to Form 10-K for 2011.)
- 10-x AT&T Corp. Non-Qualified Pension Plan, amended December 31, 2008. (Exhibit 10-cc to Form 10-K for 2013.)
- 10-y AT&T Corp. Excess Benefit and Compensation Plan, amended December 31, 2008. (Exhibit 10-dd to Form 10-K for 2013.)
- 10-z BellSouth Corporation Nonqualified Deferred Compensation Plan, dated January 1, 2005. (Exhibit 10-ss to Form 10-K for 2011.)
- 10-aa BellSouth Corporation Stock and Incentive Compensation Plan, amended June 28, 2004. (Exhibit 10-qq for Form 10-K for 2009.)
- 10-aa(i) First Amendment to the BellSouth Corporation Stock and Incentive Compensation Plan, dated September 26, 2005. (Exhibit 10-xx(i) to Form 10-K for 2011.)
- 10-aa(ii) Second Amendment to BellSouth Corporation Stock and Incentive Compensation Plan, effective June 26, 2008. (Exhibit 10-hh(ii) to Form 10-K for 2013.)
- 10-bb BellSouth Corporation Supplemental Executive Retirement Plan, amended December 18, 2014. (Exhibit 10.2 to Form 8-K dated December 18, 2014.)
- 10-cc BellSouth Nonqualified Deferred Income Plan, amended May 1, 2012. (Exhibit 10-fff to Form 10-K for 2012.)
- 10-dd Cingular Wireless Cash Deferral Plan, dated November 1, 2001. (Exhibit 10-hhh to Form 10-K for 2011.)

**AT&T Inc.**

---

10-ee	AT&T Mobility 2005 Cash Deferral Plan, dated January 1, 2005. (Exhibit 10-III to Form 10-K for 2011.)
10-ff	AT&T Executive Physical Program, dated January 1, 2011.
10-gg	Equalization Agreement for John Stankcy (Exhibit 10.1 to Form 8-K dated August 20, 2015.)
10-hh	Agreement between D. Wayne Watts and AT&T Inc. (Exhibit 10.2 to Form 8-K dated August 20, 2015.)
10-ii	Agreement between James Cicconi and AT&T Inc. (Exhibit 10-b to Form 10-Q filed for September 30, 2016.)
10-jj	Agreement between Ralph de la Vega and AT&T Inc. (Exhibit 10.1 to Form 8-K dated December 16, 2016.)
10-kk	\$9,155,000,000 Term Loan Credit Agreement, dated January 21, 2015, among AT&T, certain lenders named therein and Mizuho Bank, Ltd., as administrative agent. (Exhibit 10.1 to Form 8-K dated January 21, 2015.)
10-ll	\$12,000,000,000 Amended and Restated Credit Agreement, dated December 11, 2015, among AT&T, certain lenders named therein and Citibank, N.A., as administrative agent. (Exhibit 10 to Form 8-K dated December 15, 2015.)
10-mm	\$40,000,000,000 Term Loan Credit Agreement, dated October 22, 2016, among AT&T Inc., certain lenders named therein, and JPMorgan Chase Bank, N.A., as agent. (Exhibit 10.2 to Form 8-K dated October 24, 2016.)
	10-mm (i) \$30,000,000,000 Term Loan Credit Agreement, dated October 22, 2016, amended November 15, 2016, among AT&T Inc., the initial lenders named therein, and JPMorgan Chase Bank, N.A., as agent.
	10-mm (ii) \$30,000,000,000 Term Loan Credit Agreement, dated October 22, 2016, amended February 10, 2017, among AT&T Inc., the initial lenders named therein, and JPMorgan Chase Bank, N.A., as agent.
10-nn	\$10,000,000,000 Term Loan Credit Agreement, dated as of November 15, 2016, among AT&T Inc., the lenders named therein and JPMorgan Chase Bank, N.A., as Agent (Exhibit 10.1 to Form 8-K dated November 15, 2016.)
12	Computation of Ratios of Earnings to Fixed Charges
13	Portions of AT&T's Annual Report to Stockholders for the fiscal year ended December 31, 2016. Only the information incorporated by reference into this Form 10-K is included in the exhibit.
21	Subsidiaries of AT&T Inc.
23	Consent of Ernst & Young LLP
24	Powers of Attorney

**AT&T Inc.**

---

31	Rule 13a-14(a)/15d-14(a) Certifications
31.1	Certification of Principal Executive Officer
31.2	Certification of Principal Financial Officer
32	Section 1350 Certification
99	Supplemental Interim Financial Information
101	XBRL Instance Document

We will furnish to stockholders upon request, and without charge, a copy of the Annual Report to Stockholders and the Proxy Statement, portions of which are incorporated by reference in the Form 10-K. We will furnish any other exhibit at cost.

**AT&T INC.**  
**SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS**  
**Allowance for Doubtful Accounts**  
Dollars in Millions

COL. A	COL. B	COL. C			COL. D	COL. E
		Additions				
	Balance at Beginning of Period	(1) Charged to Costs and Expenses (a)	(2) Charged to Other Accounts (b)	(3) Acquisitions (c)	Deductions (d)	Balance at End of Period
<b>Year 2016</b>	<b>\$ 704</b>	<b>1,474</b>	-	-	<b>1,517</b>	<b>\$ 661</b>
Year 2015	\$ 454	1,416	-	214	1,380	\$ 704
Year 2014	\$ 483	1,032	(32)	-	1,029	\$ 454

- (a) Includes amounts previously written off which were credited directly to this account when recovered. Excludes direct charges and credits to expense for nontrade receivables in the consolidated statements of income.
- (b) Includes amounts related to long-distance carrier receivables which were billed by AT&T.
- (c) Acquisitions of DIRECTV and wireless properties in Mexico in 2015.
- (d) Amounts written off as uncollectible, or related to divested entities.

**AT&T INC.**  
**SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS**  
**Allowance for Deferred Tax Assets**  
Dollars in Millions

COL. A	COL. B	COL. C			COL. D	COL. E
		Additions				
	Balance at Beginning of Period	(1) Charged to Costs and Expenses	(2) Charged to Other Accounts (a)	(3) Acquisitions (b)	Deductions (c)	Balance at End of Period
<b>Year 2016</b>	<b>\$ 2,141</b>	<b>81</b>	<b>61</b>	-	-	<b>\$ 2,283</b>
Year 2015	\$ 1,182	283	373	420	117	\$ 2,141
Year 2014	\$ 927	-	445	-	190	\$ 1,182

- (a) Includes current year reclassifications from other balance sheet accounts.  
(b) Acquisitions of DIRECTV and wireless properties in Mexico in 2015.  
(c) Reductions to valuation allowances related to deferred tax assets.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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, on the 17<sup>th</sup> day of February, 2017.

AT&T INC.

/s/ John J. Stephens  
John J. Stephens  
Senior Executive Vice President  
and Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated.

Principal Executive Officer:  
Randall Stephenson\*  
Chairman of the Board, Chief Executive Officer  
and President

Principal Financial and Accounting Officer:  
John J. Stephens  
Senior Executive Vice President  
and Chief Financial Officer

/s/ John J. Stephens  
John J. Stephens, as attorney-in-fact  
and on his own behalf as Principal  
Financial Officer and Principal  
Accounting Officer

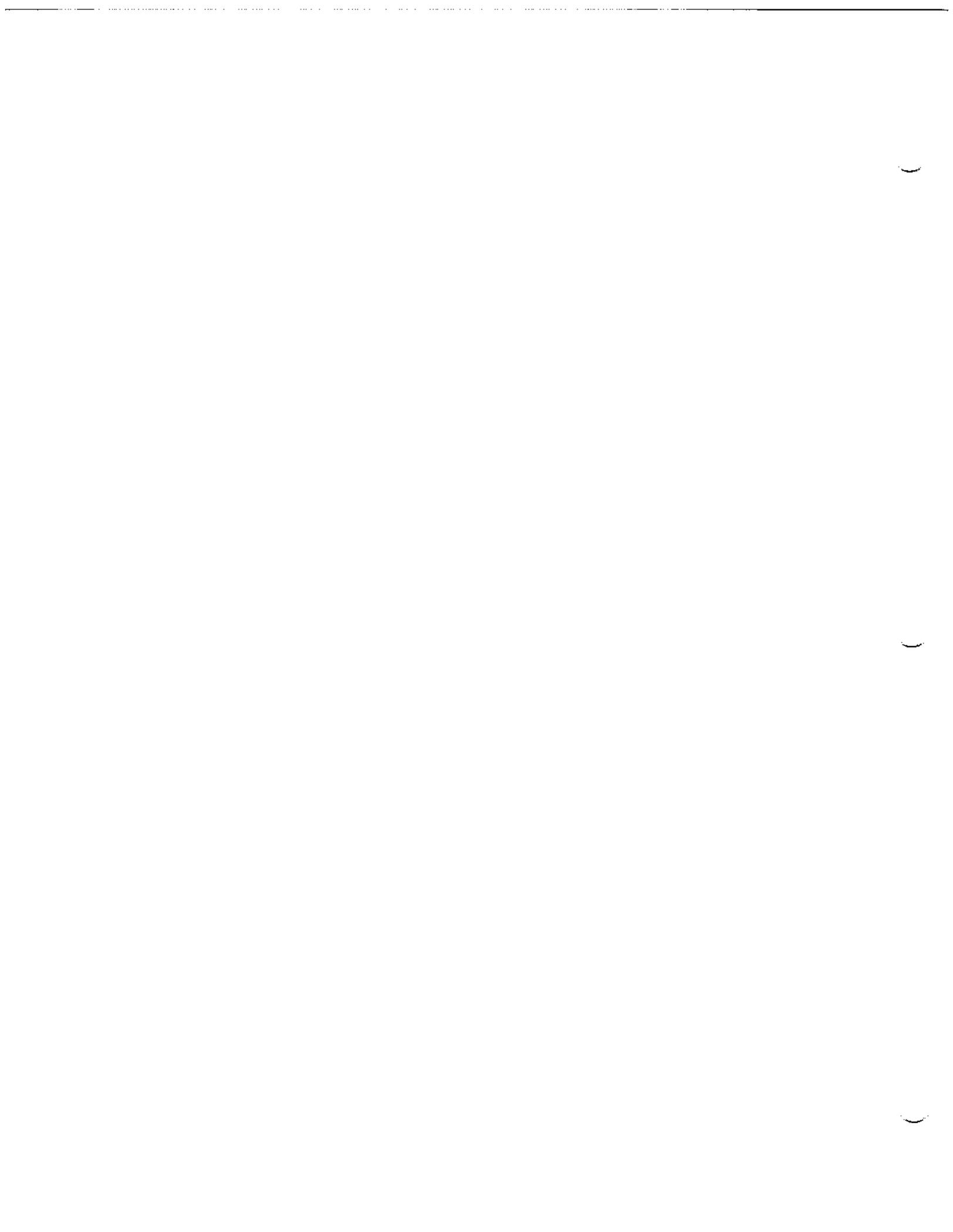
February 17, 2017

Directors:

Randall L. Stephenson\*  
Samuel A. Di Piazza, Jr.\*  
Richard W. Fisher\*  
Scott T. Ford\*  
Glenn H. Hutchins\*  
William E. Kennard\*

Michael B. McCallister\*  
Beth E. Mooney\*  
Joyce M. Roché\*  
Matthew K. Rose\*  
Cynthia B. Taylor\*  
Laura D'Andrea Tyson\*  
Geoffrey Y. Yang\*

\* by power of attorney



10-K 1 cabo20161231\_10k.htm FORM 10-K [Table of Contents](#)

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 10-K**

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

For the fiscal year ended December 31, 2016

Commission File Number: 001-36863

**Cable One, Inc.**

*(Exact name of registrant as specified in its charter)*

**Delaware**  
*(State or Other Jurisdiction of  
Incorporation)*

**13-3060083**  
*(I.R.S. Employer  
Identification No.)*

**210 E. Earll Drive, Phoenix, Arizona**  
*(Address of Principal Executive Offices)*

**85012**  
*(Zip Code)*

**(602) 364-6000**

*(Registrant's Telephone Number, Including Area Code)*

Securities registered pursuant to Section 12(b) of the Act:

<u>Title Of Each Class</u>	<u>Name Of Each Exchange On Which Registered</u>
Common Stock, par value \$0.01	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act:

**None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes   
No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes   
No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment of this Form 10-K.

\*\*\*\*\*

Table of Contents

Indicate by check mark 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. (Check one):

Large accelerated filer       Accelerated filer       Non-accelerated filer       Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

The aggregate market value of the registrant's common stock held by non-affiliates as of June 30, 2016 was approximately \$2.4 billion, based on the closing price for the registrant's common stock on such date. For purposes of this computation only, all executive officers, directors, and 10% beneficial owners of the registrant as of June 30, 2016 are deemed to be affiliates of the registrant. Such determination should not be deemed to be an admission that such executive officers, directors, or 10% beneficial owners are, in fact, affiliates of the registrant.

There were 5,719,502 shares of the registrant's common stock issued and outstanding as of February 21, 2017.

**Documents Incorporated by Reference**

Portions of the registrant's Definitive Proxy Statement relating to its 2017 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the registrant's fiscal year ended December 31, 2016, are incorporated by reference in Part III of this Form 10-K.

Table of Contents**TABLE OF CONTENTS**

	<u>Page</u>
<b>PART I</b>	
Item 1. Business	<u>3</u>
Item 1A. Risk Factors	<u>19</u>
Item 1B. Unresolved Staff Comments	<u>30</u>
Item 2. Properties	<u>30</u>
Item 3. Legal Proceedings	<u>30</u>
Item 4. Mine Safety Disclosures	<u>30</u>
<b>PART II</b>	
Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	<u>31</u>
Item 6. Selected Financial Data	<u>33</u>
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations	<u>34</u>
Item 7A. Quantitative and Qualitative Disclosures About Market Risk	<u>49</u>
Item 8. Financial Statements and Supplementary Data	<u>49</u>
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	<u>50</u>
Item 9A. Controls and Procedures	<u>50</u>
Item 9B. Other Information	<u>51</u>
<b>PART III</b>	
Item 10. Directors, Executive Officers and Corporate Governance	<u>51</u>
Item 11. Executive Compensation	<u>51</u>
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	<u>51</u>
Item 13. Certain Relationships and Related Transactions, and Director Independence	<u>51</u>
Item 14. Principal Accounting Fees and Services	<u>51</u>
<b>PART IV</b>	
Item 15. Exhibits, Financial Statement Schedules	<u>52</u>
Item 16. Form 10-K Summary	<u>54</u>
SIGNATURES	<u>S-1</u>
INDEX TO CONSOLIDATED FINANCIAL STATEMENTS	<u>F-1</u>

Table of Contents**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

This document contains “forward-looking statements” that involve risks and uncertainties. These statements can be identified by the fact that they do not relate strictly to historical or current facts, but rather are based on current expectations, estimates, assumptions and projections about the cable industry and our business and financial results. Forward-looking statements often include words such as “anticipates,” “estimates,” “expects,” “projects,” “intends,” “plans,” “believes” and words and terms of similar substance in connection with discussions of future operating or financial performance. As with any projection or forecast, forward-looking statements are inherently susceptible to uncertainty and changes in circumstances. Our actual results may vary materially from those expressed or implied in our forward-looking statements. Accordingly, undue reliance should not be placed on any forward-looking statement made by us or on our behalf. Important factors that could cause our actual results to differ materially from those in our forward-looking statements include government regulation, economic, strategic, political and social conditions and the following factors:

- uncertainties as to the timing of the acquisition of RBI Holding LLC (“NewWave”) and the risk that the transaction may not be completed in a timely manner or at all;
- the possibility that any or all of the various conditions to the consummation of the acquisition of NewWave may not be satisfied or waived, including failure to receive any required regulatory approvals (or any conditions, limitations or restrictions placed in connection with such approvals);
- risks regarding the failure to obtain the necessary financing to complete the NewWave transaction;
- the effect of the announcement or pendency of the transaction on our and NewWave’s ability to retain and hire key personnel and their ability to maintain relationships with customers, suppliers and other business partners;
- the potential diversion of senior management’s attention from our ongoing operations;
- uncertainties as to our ability and the amount of time necessary to realize the expected synergies and other benefits of the NewWave transaction;
- our ability to integrate NewWave’s operations into our own in an efficient and effective manner;
- rising levels of competition from historical and new entrants in our markets;
- recent and future changes in technology;
- our ability to continue to grow our business services product;
- increases in programming costs and retransmission fees;
- our ability to obtain support from vendors;
- the effects of any significant acquisitions by us;
- adverse economic conditions;
- the integrity and security of our network and information systems;
- legislative and regulatory efforts to impose new legal requirements on our data services;
- changing and additional regulation of our data, video and voice services;
- our ability to renew cable system franchises;
- increases in pole attachment costs;
- the failure to meet earnings expectations;
- the adequacy of our risk management framework;
- changes in tax and other laws and regulations;
- changes in accounting principles generally accepted in the United States (“GAAP”) or other applicable accounting policies; and
- the other risks and uncertainties detailed in the section titled “Risk Factors” in this Annual Report on Form 10-K.

Any forward-looking statements made by us in this document speak only as of the date on which they are made. We are under no obligation to, and expressly disclaim any obligation to, update or alter our forward-looking statements, whether as a result of new information, subsequent events or otherwise.

[Table of Contents](#)**PART I****ITEM 1. BUSINESS****Overview**

On July 1, 2015, Cable One, Inc. (“Cable One,” “us,” “our,” “we” or the “Company”) became an independent company traded under the ticker symbol “CABO” on the New York Stock Exchange after completion of its spin-off from Graham Holdings Company (“GHC”). The spin-off was effected through the distribution by GHC of 100% of the outstanding shares of common stock of Cable One to GHC stockholders as of the record date for the distribution (the “spin-off”) in a pro rata dividend (the “Distribution”). In connection with the spin-off, approximately 5.84 million shares of Cable One’s common stock were issued and outstanding on July 1, 2015, based on approximately 0.96 million shares of GHC Class A Common Stock and 4.88 million shares of GHC Class B Common Stock outstanding as of June 30, 2015. No preferred stock was issued or outstanding.

We are a fully integrated provider of data, video and voice services in 19 Western, Midwestern and Southern states. We provide these broadband services to residential and business customers in more than 35 cable systems covering over 400 cities and towns. The markets we serve are primarily non-metropolitan, secondary markets, with 76% of our customers located in five states: Arizona, Idaho, Mississippi, Oklahoma and Texas. Our biggest customer concentrations are in the Mississippi Gulf Coast region and in the greater Boise, Idaho region. We are the seventh-largest cable system operator in the United States based on customers and revenues in 2016, making services available to approximately 1.7 million homes in the United States as of December 31, 2016.

As of December 31, 2016, we provided service to 657,222 residential and business customers out of approximately 1.7 million homes passed. Of these customers, 513,908 subscribed to data services, 320,246 to video services and 115,811 to voice services.

We generate revenues through five primary products. Ranked by share of our total revenues in 2016, they are residential data (42.0%), residential video (36.0%), business services (data, voice and video – 12.2%), residential voice (5.2%) and advertising sales (3.4%). The profit margins, growth rates and capital intensity of our five primary products vary significantly due to competition, product maturity and relative costs. In 2016, our Adjusted EBITDA margins for residential data and business services were approximately four and five times greater, respectively, than for residential video. We define Adjusted EBITDA margin for a product line as Adjusted EBITDA attributable to that product line divided by revenue attributable to that product line (see the section entitled “*Management’s Discussion and Analysis of Financial Condition and Results of Operations—Use of Adjusted EBITDA*” for the definition of Adjusted EBITDA and a reconciliation of Adjusted EBITDA to net income, which is the most directly comparable GAAP measure). This margin disparity is largely the result of significant programming costs and retransmission fees incurred to deliver residential video services, which in each of the last three years represented between 50% and 60% of total residential video revenues (in addition to the other material direct and indirect costs associated with residential video). None of our other product lines has direct costs representing as substantial a portion of revenues as programming costs and retransmission fees represent for residential video, and indirect costs are allocated equally on a per primary service unit (“PSU”) basis. Programming costs and retransmission fees have a meaningfully lower impact on business services margins than residential video because business services include data, voice and video, diminishing the relative impact of programming costs and retransmission fees on that product line as a whole.

Prior to 2012, we were focused on growing revenues through subscriber retention and growth in overall PSUs. To that end, our strategies consisted of, among others, offering promotional discounts to new and existing subscribers adding new services and to subscribers purchasing more than one service offering.

Since 2012, we have adapted our strategy to face the trend, which has affected the entire cable industry, of declining profitability of residential video and declining revenues from residential voice services. We believe the declining profitability of residential video services is primarily due to competition from other content providers and increasing programming costs and retransmission fees and the declining revenues from residential voice services is primarily due to the increasing use of wireless voice services in addition to, or instead of, landline voice service. Beginning in 2013, we shifted our focus away from maximizing customer PSUs and towards growing and maintaining our higher margin businesses, namely residential data and business services. Separately, we have also focused on retaining customers with a high expected life-time value (“LTV”), who are less attracted by discounting, require less support and churn less. This strategy focuses on increasing Adjusted EBITDA, Adjusted EBITDA less capital expenditures and margins.

Table of Contents

The trends described above have impacted our four largest product lines in the following ways:

- *Residential data.* We experienced growth in the number of and revenues from our residential data customers every year since 2013. We expect this growth to continue due to projected increases in the number of potential customers for us to serve, as there are still a number of households in our markets that do not subscribe to data services from any provider. We expect to capture a portion of these customers and anticipate capturing additional market share from existing data subscribers due to our recent upgrades in broadband capacity and our ability to offer higher access speeds than many of our competitors.
- *Residential video.* Residential video service is a competitive and highly-penetrated business. As we focus on the higher-margin businesses of residential data and business services, we are de-emphasizing our residential video business and, as a result, expect residential video revenues to continue to decline in the future.
- *Residential voice.* We have experienced declines in residential voice customers as a result of homes in the United States deciding to terminate their landline voice service and exclusively use wireless voice service. We believe this trend will continue because of competition from wireless voice service. Revenues from residential voice customers have declined over recent years, and we expect this decline will continue.
- *Business services.* We have experienced significant growth in business data and voice customers and revenues and expect this to continue. We attribute this growth to our strategic focus shift on increasing sales to business customers. More recently, we have expanded our efforts to attract enterprise business customers. Margins in products sold to business customers have remained attractive, and we expect this trend to continue.

We continue to experience increased competition, particularly from telephone companies, cable overbuilders, over-the-top (“OTT”) video providers and direct broadcast satellite (“DBS”) television providers. Because of the levels of competition we face, we believe it is important to make investments in our infrastructure. We made elevated levels of capital investments between 2012 and 2015 to increase our cable plant capacities and reliability, launch all-digital video services, which has freed up approximately three-fourths of average plant bandwidth for data services, and increase data capacity by moving from four-channel bonding to 32-channel bonding. We expect to continue devoting financial resources to infrastructure improvements because we believe these investments are necessary to remain competitive.

The spin-off provided us the opportunity to further tailor our strategies to achieve greater operational focus and drive our return on investment. Our goals are to continue to grow residential data and business services and to maintain profit margins to deliver strong Adjusted EBITDA. To achieve these goals, we intend to continue our industrial engineering-driven cost management, remain focused on customers with high LTV and follow through with further investments in broadband plant upgrades and new data services offerings for residential and business services customers.

Our business is subject to extensive governmental regulation. Such regulation has led to increases in our operational and administrative expenses. In addition, we could be significantly impacted by changes to the existing regulatory framework, whether triggered by legislative, administrative or judicial rulings. In 2015, the Federal Communications Commission (the “FCC”) used its Title II authority to regulate broadband Internet access services in its Open Internet Order (the “Order”). According to the Order, under this regime, the FCC will forbear from systematic rate regulation of Internet access service at the subscriber level, which we believe will permit us to continue to manage data usage efficiently by establishing appropriate rates. However, the Order also imposes on all providers of broadband Internet access service, including us, obligations that limit the ways we can manage certain types of traffic. In June 2016, the U.S. Court of Appeals for the D.C. Circuit upheld the Order in its entirety. A petition for an *en banc* rehearing of the June 2016 decision upholding the Order is currently pending in the U.S. Court of Appeals for the D.C. Circuit. In addition, the change in administration and the newly-constituted FCC may take steps to revise the Order and the resulting rules. We cannot predict whether or not future changes to the regulatory framework that are inconsistent with the Order will occur, whether the petition for an *en banc* rehearing will be granted, or whether the decision of the U.S. Court of Appeals for the D.C. Circuit will be appealed, and if any such rehearing or appeal would be successful.

We serve our customers through a plant and network with 100% two-way capacity currently measuring approximately 750 MHz on average and DOCSIS 3.0 capabilities in all of our systems. Our technically advanced infrastructure provides for delivery of a full suite of data, video and voice products. Our broadband plant offers fiber-to-the-node with ample unused capacity and standard download speeds of 100 Megabits per second (“Mbps”), which meaningfully distinguishes our offering from competitors in most of our markets. In 2016, we substantially completed a multi-year investment program in our plant, which resulted in increased broadband capacity and reliability and which has enabled and will continue to enable us to offer even higher download speeds to our customers (at both the standard and enhanced data service levels), which we believe will reinforce our competitive strength in this area.



Table of Contents**Corporate History**

In 1986, The Washington Post Company (the prior name of our prior corporate parent, GHC) acquired from Capital Cities Communications, Inc. a number of other companies owning, in total, 53 cable television systems. The Washington Post Company paid \$350 million for these systems. The cable systems acquired in that transaction had approximately 350,000 subscribers in 15 Western, Midwestern and Southern states. All other mid-sized cable operators that existed when we were established have since exited the cable business.

Subsequent to the Capital Cities transaction, we completed over 30 acquisitions and dispositions of cable systems, both through cash sales and trades of certain of our cable systems for cable systems of other cable operators, ultimately increasing our customer count to the current total of approximately 657,000. We have been disciplined about the price we pay in acquisitions, acquiring new customers opportunistically at what we considered favorable prices. In the process, we have substantially reshaped our original geographic footprint and resized our typical system, including exiting a number of metropolitan markets. For example, we traded to other cable operators our cable systems in the Chicago, San Francisco, Cleveland and Indianapolis markets (which we acquired as part of the Capital Cities transaction) for cable systems in non-metropolitan markets that fit our business model.

While we are smaller than the nation's biggest cable companies, we have a record of consistent, long-term financial and operational success driven by our differentiated operating philosophy. We emphasize focus as opposed to scale, which is a departure from more conventional strategies in the cable industry, but is well suited to the markets in which we operate and enables us to take advantage of our strengths as a cable operator.

**NewWave Acquisition**

On January 18, 2017, we announced that we and Frequency Merger Sub, LLC, our wholly owned subsidiary, entered into an Agreement and Plan of Merger, dated as of January 17, 2017 (the "Merger Agreement"), with NewWave, RBI Blocker Corp., RBI Blocker Holdings LLC and GTCR-RBI, LLC, as equityholder representative, pursuant to which we have agreed to acquire all of the outstanding equity interests in NewWave. NewWave is owned by funds affiliated with GTCR LLC, a leading private equity firm based in Chicago. Under the terms of the Merger Agreement, we will pay a purchase price of \$735 million in cash, subject to customary post-closing adjustments. The closing of the transaction is subject to the receipt of certain regulatory approvals and other customary closing conditions. We currently anticipate that the transaction will be completed in the second quarter of 2017.

We expect to finance the transaction with \$650 million of senior secured loans and cash on hand. In connection with the entry into the Merger Agreement, we entered into a commitment letter on January 17, 2017, as amended and restated on February 13, 2017, with JPMorgan Chase Bank, N.A. ("JPMorgan"), Wells Fargo Bank, National Association, Wells Fargo Securities, LLC, RBC Capital Markets, Royal Bank of Canada, Toronto Dominion Bank, New York Branch, TD Securities (USA) LLC, SunTrust Bank, SunTrust Robinson Humphrey, Inc. and U.S. Bank National Association (the "Lenders"). Pursuant to the amended and restated commitment letter, and subject to the terms and conditions set forth therein, the Lenders have committed to provide us with \$300 million of incremental five-year term "A" loans and \$350 million of incremental seven-year term "B" loans to finance the transaction.

On February 13, 2017, we entered into an amendment to our existing credit agreement to permit, among other things, the incurrence of the \$650 million of senior secured loans expected to be used to finance the acquisition of NewWave and the other transactions contemplated by the Merger Agreement.

**Industry Overview**

Cable companies in the United States are typically fully integrated providers of data, video and voice services to residential and business customers in various geographic regions. A headend typically serves each of a cable company's cable systems, receiving data, video and voice service signals by connecting directly to the network backbone, which aggregates signals delivered through over-the-air broadcasting, fiber optic networks and satellite transmissions. From the headend, cable companies modulate, amplify and distribute these signals over a proprietary network of coaxial and fiber optic cable to the homes and businesses of subscribers. In addition to building their own network backbone or leasing physical access to the network backbone from telecommunications companies, cable companies also purchase licenses to provide their subscribers with access to cable television channels owned by programmers and distributed over the network backbone. Cable companies also typically sell advertising on their video channels. The cable industry has benefited from a progression of profitable new product introductions over the past 15 years, including, but not limited to, high-speed data service, high-definition and digital video service and Voice over Internet Protocol ("VoIP") voice service.



Table of Contents

Cable companies generate revenue by charging subscription fees to their residential and business customers, typically billed in advance on a monthly basis, at rates that vary according to the data, video and/or voice services for which customers subscribe, and the type of video and Internet access equipment furnished to them, as well as through advertising sales. The margins that a cable company can earn on its PSU offerings vary from product to product. Because of rising programming costs and retransmission fees, the profit margin on video services is generally lower than it once was and significantly lower than the current margins on data services. Despite lower margins on video services, the strategy of many cable companies is to market and sell all three PSUs as a single "triple play" package in order to maximize the number of PSUs per household. Many in the industry believe it is desirable to sell all three products as a package because they consider video service a gateway offering to sell data service and because fixed costs per customer can be spread over multiple PSUs. However, recent industry trends have been towards increases in data subscribers even as video subscriptions have declined.

Cable companies generally operate by establishing cable systems in geographic markets under non-exclusive franchises granted by state or local authorities for specified periods of time. The most sought-after markets by major cable companies have generally been the largest metropolitan markets. These markets are thought to offer the advantages of population density (which may permit efficient construction and operation of a cable distribution system) and attractive demographics, including customers with higher income-per-household than their counterparts in non-metropolitan, secondary markets, leading to lower price sensitivity and a willingness to purchase a greater number of PSUs.

**Our Strengths**

We have a variety of strengths as a cable operator, stemming from, among other things, historical and ongoing capital investments in our plant and our focus on serving customers in non-metropolitan markets. These strengths include the following:

*Attractive markets.* Our customers are located primarily in non-metropolitan, secondary markets with favorable competitive dynamics in comparison to major urban centers. In particular:

- We tend to face less vigorous competition from telephone companies than cable operators in metropolitan markets.
- Advances in technology often come later to our markets—for example, very few of our competitors offer fiber-to-the-home.
- Our subscribers tend to be value-focused, enabling us to save video services costs by not carrying expensive programming options with low subscriber demand.
- We are regionally diversified, reducing the impact that an economic downturn in a specific geographic market would have on our overall business.

*Deep customer understanding.* We have operated as a non-metropolitan cable business for over 20 years. In order to understand our customers' demands and preferences, we have conducted daily customer research for nearly two decades and currently conduct thousands of customer satisfaction surveys per year. We believe we have gained valuable insight into how to serve customers in non-metropolitan markets, including with respect to providing an optimal mix of video channel options, price points and best-in-class customer service levels. In addition, the vast majority of our employees, or associates, reside and work in our markets, providing local service that enhances the communities we serve.

*Superior broadband technology with ample unused capacity.* We offer our residential and business data customers Internet products at faster speeds than those available from competitors in most of our markets. Our broadband plant consists of a hybrid fiber coax ("HFC") network offering fiber-to-the-node with ample unused capacity. Our standard broadband offering for our residential customers is a download speed of 100 Mbps, which is at the high end of the range of standard residential offerings in our markets. Our enhanced broadband offering for our residential customers is currently a download speed of up to 1 Gigabit per second ("Gpbs").

Table of Contents

In addition, we have made significant investments in our business consistent with our strategic focus to enhance sales of residential data services and business services. We substantially completed significant, multi-year plant and product enhancements in 2016, which increased our broadband capacity and reliability. These initiatives caused us to incur several years of higher than usual capital spending. However, we believe the competitive benefits will be significant, particularly for data services. Among the enhancements in 2016:

- We continued to decrease the average number of data customers per unique service by aggressively splitting service areas (fiber nodes), which substantially improves data throughput during periods of peak usage, minimizing disruptions in data access speeds to our customers.
- We substantially completed a multi-year plant reinforcement project, which enhanced reliability and expanded average plant bandwidth to an average of 750 MHz.
- We completed a 30-month replacement of nearly all headend cable modem termination systems, allowing us to move from four-channel bonding to 32-channel bonding.
- We rolled out our 1 Gbps data service (GigaONE™) to nearly 70% of our residential customers based on homes passed as of December 31, 2016. We expect that this level of service will be available to all of the residential customers in our current markets by the end of 2017.
- We substantially completed a multi-year video product conversion to all-digital distribution, which has freed up approximately three-fourths of average plant bandwidth for data services at speeds up to and exceeding 1 Gbps.

We anticipate the foregoing capital projects will facilitate sustained increases in residential data and business services and customer satisfaction.

**Low cost structure and competitive pricing.** We believe our operating and capital costs, taken as a whole, are as low as or lower than any major cable operator. We attribute our low cost structure to a commitment to focusing on retaining our highest value customers, rather than seeking to obtain as many customers as possible, and the lower costs of operations available in a non-metropolitan market compared to a metropolitan market. In addition, because we operate our residential and business data services with a competitive plant and cost structure, we are able to offer our customers both attractive pricing and compelling products.

**Customer satisfaction.** We have a customer-focused approach, influencing how we are organized, how we sell our services and how we service our customers. For example, we offer a same-day-service guarantee in almost every one of our markets, which we believe none of our major competitors in our markets currently offer. We believe that our dedication to providing a differentiated customer experience is an important driver of our overall value proposition and creates loyalty, improves customer retention and drives increased demand for our services. We have always focused on customer satisfaction, with an emphasis on consistently benchmarking our customer satisfaction over time and relative to our competitors based on internally and externally generated customer-satisfaction data.

**Associate satisfaction.** We have also focused on associate satisfaction, believing our customers' satisfaction is tightly linked to our associate satisfaction. Associate satisfaction has been routinely measured over time internally and has been consistently high throughout the past decade, based on internal measurements. We currently measure our associate satisfaction annually. None of our employees have been unionized for over two decades.

**Experienced management team.** Our senior management team is comprised of senior executives who have significant experience in the cable industry. Our executive management team has an average tenure at Cable One (or its predecessors) of approximately 20 years, and we believe this team is deeply knowledgeable about cost and competitive conditions in our markets. They also understand and are deeply committed to our strategy, which we developed on a collaborative basis over many years.

## Our Strategies

We have a multi-faceted strategy that builds upon our long track record of focusing on the right markets, the right products and the right customers, as well as controlling our operating and capital costs. More specifically, our strategy includes the following principal components:



Table of Contents

**Focus on larger non-metropolitan markets.** We believe our decision over 20 years ago to concentrate on non-metropolitan markets has served us well, and we intend to continue to focus on offering our products primarily in these markets. The cable economics of non-metropolitan markets, for which we have optimized our strategy and our operations, are different from cable operations in major cities, and have yielded positive operating results for our business. Because price points for services in non-metropolitan markets are generally lower, and customers in non-metropolitan markets tend to subscribe to fewer PSUs, our average revenue per customer and our PSUs per customer are lower than they might be in metropolitan markets. However, many of our costs are lower than they would be in metropolitan markets. The dynamics of larger, non-metropolitan markets enable us to operate at attractive margins and earn substantial returns, while remaining consistent with our focus on meeting customer demand for low prices while simultaneously keeping costs down. In addition, we tend to face less vigorous competition from telephone companies than cable operators in metropolitan markets.

**Maximize Adjusted EBITDA less capital expenditures and drive profitable growth.** We concentrate on the products and customers that maximize Adjusted EBITDA less capital expenditures and provide the best opportunity for profitable growth. We believe residential video and residential voice face inexorable long-term declines. With respect to the video product, programmers are charging higher rates for content to cable companies providing video services (often for content for which viewership is declining), and cable companies have had to choose between absorbing those increases to the detriment of their margins or passing on the full cost to customers, which adversely affects customer demand. At the same time, the rapid expansion of OTT offerings via the Internet has given customers new alternatives to cable companies' video offerings. In addition, demand for cellular and smartphone offerings have reduced residential voice starts for us and others in our industry. As a result, we have reduced our focus on these two products and prioritized higher growth opportunities such as residential data and business services.

We have declined to cross-subsidize our video business with cash flow from our higher growth, higher margin products, which has resulted in our residential video customers declining at a faster rate than the industry average. Our residential video customers decreased by 12.4% in 2016 versus 2015 and by 19.8% in 2015 versus 2014. Our residential video revenues declined by \$37.9 million, or 11.4%, for the year ended December 31, 2016 versus 2015 and by \$29.0 million, or 8.0%, for the year ended December 31, 2015 versus 2014. While this strategy runs contrary to conventional wisdom in the cable industry, which puts heavy emphasis on video customer counts and maximizing the number of PSUs per customer by bundling and discounting services, we believe it best positions us for long-term success. For us, success in growing and retaining residential data and business services customers is far more important than the number of triple-play customers we have.

**Target higher value residential customers.** Since 2013, we have introduced rigorous analytics to determine the LTV of current and potential residential customers. We target marketing and customer service at customers who we believe are likely to produce relatively higher value over the life of their service relationships with us, rather than seeking to maximize the number of new customers. We analyze the net present value of every residential start and seek to identify customers with high LTV, who are more likely to buy data service, less likely to churn and more likely to pay on time. Seeking to retain and sell more services to residential customers with a high LTV has enabled us to earn higher profits with fewer customers and PSU subscriptions. We believe that optimizing the LTV of data-only customers as video and voice cord-cutting accelerates is both a necessity and an opportunity for our business.

**Drive growth in residential data and business services.** We believe our residential data and business services products provide attractive current and future growth opportunities. Our disciplined prioritization of residential data and business services is reflected in everything we do, including pricing, the allocation of sales, marketing and customer service resources, capital spending and the way we conduct negotiations with suppliers, especially video suppliers. During 2016, we continued to further diversify our revenue streams away from video as residential data and business services represented 54.2% of our total revenues versus 47.5% for 2015 and 42.0% for 2014. Our residential data revenues grew to \$344.2 million in 2016, a 16.9% increase versus 2015. We believe we have demonstrated that it is possible to decouple unit growth in our residential data and residential video businesses, which historically have been marketed as a package. Our data-only connects are growing significantly faster than any other segment of our residential business as we have focused on selling data-only packages to new customers rather than on cross-selling video services to these customers.

Our business services revenues grew to \$100.3 million in 2016, a 13.0% increase versus 2015. We expect to generate continued growth in business services by leveraging our existing infrastructure capabilities and footprint to offer higher broadband speeds than other providers in our markets and to expand our business services to attract more small, medium- sized and enterprise business customers.

**Continue our culture of cost leadership.** We believe our total combined operating and capital costs per PSU over the past decade have been among the lowest of any cable company with publicly reported numbers and that our operating margins compare very favorably with those of significantly bigger companies in the cable industry. This is the antithesis of normal cable economies-of-

scale expectations, where higher volumes are expected to create lower costs per PSU and increase operating margins. Rather than increasing our size and seeking cost savings through economies-of-scale, we have achieved our lower cost structure over many years by focusing on:

## Table of Contents

- serving non-metropolitan, secondary markets and not expanding into metropolitan markets, which contain different customer dynamics and would require us to implement additional operational components;
- the adoption of new technologies only after they have been tested by other companies in other markets, rather than incurring the level of capital expenditures necessary to be an early adopter of most new technologies;
- implementing a virtually centralized call center to receive inbound customer service calls and dispatch technicians across all of our markets, while keeping the majority of our call center associates in our non-metropolitan markets;
- standardizing our cable programming offerings across our markets, which reduces our customer service costs, in contrast to other cable companies that offer different programming packages in different markets;
- focusing on retaining and seeking high-LTV customers rather than trying to maximize the number of customers or PSUs per customer; and
- aligning our resources to emphasize increased sales of residential data services and sales to business customers and continuing our industrial engineering-driven approach to cost management, rather than committing resources equally to sales of all of our products.

We believe our strategy of focus has produced positive results. From 2011 through December 31, 2016, we have experienced a 70% reduction in bad debt; a 34% reduction in the frequency of telephone customer service calls, resulting in a 32% headcount reduction in telephone customer service personnel; a decline of 33% in the frequency of technicians being dispatched to customer locations, resulting in a 17% headcount reduction in the staff devoted to that function; and an overall headcount reduction of 453, representing a reduction, primarily through attrition, of more than 19% of our total workforce (1,877 associates as of the end of 2016). During this same period, both our customer and associate satisfaction have remained high or improved based on internal measurements and, in the case of customer satisfaction, externally generated data.

**Balanced capital allocation.** We are committed to a disciplined approach to evaluating acquisitions and internal investments, capital structure optimization and return of capital.

## **Our Products**

### *Residential Data Services*

For 2016, residential data services represented approximately 42.0% of our total revenues. We offer multiple tiers of data services with download speeds up to 1 Gbps to nearly 70% of our residential customers as of December 31, 2016 and up to 200 Mbps to our remaining residential customers. We expect that our 1 Gbps level of service will be available to nearly all of the residential customers in our current markets by the end of 2017. Our data services also include our Internet portal, <http://home.cableone.net>, which provides multiple e-mail addresses. To meet the increasing bandwidth needs of our customers who use multiple Internet-connected devices in the home, our customers may lease wireless modems to maximize their wireless Internet speeds.

### *Residential Video Services*

For 2016, residential video services represented approximately 36.0% of our total revenues. We offer a broad variety of residential video services, generally ranging from a basic video service to a full digital service with access to hundreds of channels. Our basic video service generally consists of local networks, local community programming, such as governmental and public access, and certain other channels, such as weather, shopping and religious channels. Our digital video service includes national and regional cable networks, music channels and an interactive, electronic programming guide with parental controls. We also offer premium channels, which include networks such as HBO, Showtime, Starz and Cinemax that generally offer, without commercial interruption, movies, original programming, live sporting events and concerts and other features. Our digital video customers, which we expect will include all of the residential customers in our current markets by the end of 2017, may also subscribe to our advanced services. Our advanced video services include TiVo DVRs, which digitally record programming and pause and rewind live programming, and high-definition set-top boxes, which provide high-resolution picture quality, improved audio quality and a wide-screen format and allow our customers to access Internet content on their televisions.

Table of Contents

Our TV Everywhere product enables our video customers to stream many of their favorite channels and shows to mobile devices and computers, expanding the value of our video service. Our TV Everywhere product includes over 75 of the most popular networks across a wide range of genres, including HBO and Cinemax.

***Residential Voice Services***

For 2016, residential voice services represented approximately 5.2% of our total revenues. Our residential voice service transmits digital voice signals over our network and is an interconnected VoIP service. Our voice services include unlimited local and long-distance calling, voicemail, call waiting, three-way calling, caller ID, anonymous call rejection and other features. Our voice services also provide international calling by the minute.

***Business Services***

We consider the data, voice and video services products we sell to our business customers as a separate product from our residential versions of these services. For 2016, business services represented approximately 12.2% of our total revenues. We offer multiple tiers of data, voice and video services for a variety of small-sized to enterprise-level businesses. We offer our business customers data services over our coaxial network with download speeds ranging from 25 Mbps to 500 Mbps, with varying upload speed options. In 2016, we began delivering data services over an Ethernet Passive Optical Network ("EPON"). This shared fiber architecture offers a mixture of symmetrical and asymmetrical internet speeds ranging from 50 Mbps and 2 Gbps. We expect to offer EPON in several additional markets each year for the foreseeable future. Both our coaxial network and our EPON data services offer the ability to have a single Internet Protocol ("IP") address or multiple IP addresses. Business voice services packages range from one line to multi-line options, including availability of all the most popular calling features like caller ID, call waiting, call forwarding and much more. Business video packages range from a basic video service tier to a comprehensive video selection including variety, news and sports programming in high-definition. We also lease fiber optic cable capacity on a wholesale basis to our business customers.

We offer dedicated bandwidth via fiber optic technology to medium-sized and enterprise-level businesses, in addition to wholesale services to other carriers. Our fiber optic-based products include Dedicated Internet Access and Ethernet Private Line with speeds ranging from 10 Mbps to 10 Gbps in scalable increments. Each of these products requires the use of IP-compatible equipment to use the service. We also offer Network to Network Interface connections to other carriers at multiple Points of Presence across the United States.

***Advertising***

For 2016, advertising sales represented approximately 3.4% of our total revenues. Our agreements with each of our programmers provide that we may sell a specified amount of time on our programmers' channels, during both local and national programming spots, to our advertising customers. We also produce television commercials for these customers. We also sell advertising space on select cable network websites.

**Competition**

We operate in highly competitive, subscriber-driven and rapidly changing environments and compete with a growing number of companies that provide a broad range of communications products, services and content to subscribers. Our competitors have historically included, and we expect will continue to include, over-the-air reception providers; DBS providers; telephone companies that offer data and video services through digital subscriber line ("DSL") technology or fiber-to-the-node networks; and other cable companies that have been granted a franchise to operate in a geographic market in which we are already operating.

Substantially all of our cable systems are in markets in which CenturyLink or AT&T is the established local telephone company and our primary competitor. The remainder of our cable systems are in markets where we compete with various other companies. CenturyLink, AT&T (through its U-verse brand) and other companies have overbuilt approximately 28% of our homes passed with fiber-to-the-node or other high-speed networks, such that they are able to offer data, video and voice services, including data services with high access speeds (albeit generally lower when compared to those that we offer). However, less than 3% of the customers in our markets have access to fiber-to-the-home from our competitors, which offer a triple-play product offering comprised of high-speed data, video and voice. Fiber-to-the-home facilitates greater access speeds than we are able to offer through our fiber-to-the-node HFC infrastructure at this time, although in the next few years we expect our access speeds to be comparable to those provided by fiber-to-the-home. In addition, on their own or via strategic partnerships or other arrangements with DBS operators that permit telephone companies to package the video services of DBS operators with telephone companies' own DSL service, landline voice and wireless voice services, some telephone companies are competing with our video programming and data and voice services. An example of such an arrangement is the merger of AT&T and DirecTV. We also face increasing competition for residential voice services from

wireless telephone companies, as some of our customers are replacing our landline voice service completely with wireless voice service.

## Table of Contents

In addition, new entrants with significant financial resources may compete on a larger scale with our video and data services. For example, several years ago Alphabet launched Google Fiber, which offers data and video services in several areas of the country, although none of the existing or currently announced cities are in regions in which we compete. Google Fiber's infrastructure consists of fiber optic wirelines, which is technologically superior to the DSL technology of certain of our competitors. Although Alphabet announced in the fourth quarter of 2016 that it was pausing its Google Fiber expansion in most of its potential Google Fiber cities, if Alphabet expands its Google Fiber offerings into our markets, it may be able to offer our current customers attractive pricing and technology, increasing competition in our markets.

A number of municipalities have also announced plans to construct their own data networks with access speeds that match or exceed those of our own through the use of fiber optic technology. In some cases, local government entities and municipal utilities may legally compete with us without obtaining a franchise from a state or local governmental franchising authority ("LFA"), reducing their barriers to entry into our markets. The entrance of municipalities as competitors in our markets would add to the competition we face and could lead to additional customer attrition.

Our video business also faces substantial and increasing competition from other forms of in-home entertainment and recreational activities, including video games, mobile apps and the Internet, as well as from other media companies. Internet and other media companies, including Alphabet, Amazon, Apple, Sling TV, Hulu and Netflix, increasingly offer video programming via OTT streaming on the Internet. Because of the significant size and financial resources of such companies, we anticipate that they will continue to invest resources in increasing the availability of video content on the Internet.

### **Employees**

As of December 31, 2016, we had approximately 1,877 full-time employees, and none were represented by a union.

### **Available Information and Website**

Our Internet address is [www.cableone.net](http://www.cableone.net). We make available free of charge through our website, <http://ir.cableone.net>, copies of our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as soon as reasonably practicable after such documents are electronically filed with the Securities and Exchange Commission (the "SEC"). Printed copies of these documents will be furnished without charge (except exhibits) to any stockholder upon written request addressed to our Secretary at 210 E. Earl Drive, Phoenix, Arizona 85012. The SEC maintains a website, [www.sec.gov](http://www.sec.gov), that contains the reports, proxy and information statements and other information regarding issuers that file electronically with the SEC. Also, the public may read and copy any materials that we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The contents of these websites are not incorporated by reference into this Annual Report on Form 10-K and shall not be deemed "filed" under the Exchange Act. Further, our references to website URLs are intended to be inactive textual references only.

### **Executive Officers**

The following table presents certain information, as of March 1, 2017, concerning our executive officers.

<b>Name</b>	<b>Age</b>	<b>Position</b>
Mr. Thomas O. Might	65	Executive Chairman and Chairman of the Board
Ms. Julia M. Laulis	54	President and Chief Executive Officer and Director
Mr. Michael E. Bowker	48	Senior Vice President, Chief Sales and Marketing Officer
Mr. Kevin P. Coyle	65	Senior Vice President and Chief Financial Officer
Mr. Stephen A. Fox	51	Senior Vice President, Chief Network Officer
Mr. Eric M. Lardy	43	Senior Vice President
Mr. Charles B. McDonald	41	Senior Vice President, Operations
Mr. Alan H. Silverman	63	Senior Vice President, General Counsel, Director of Administration and Secretary

Table of Contents**Mr. Thomas O. Might**

Mr. Might has been Executive Chairman of Cable One since January 2017. He has served as Chairman of the board of directors (the "Board") of Cable One since 2015 and as a member of the Board of Cable One since 1995. Mr. Might served as Chief Executive Officer of Cable One from 1994 to 2016 and as President of Cable One from 1994 to 2014.

Mr. Might joined The Washington Post Company in 1978 as assistant to publisher Donald E. Graham after serving a summer internship at the newspaper in 1977. He was promoted to Vice President-Production in 1982 and served in that position until 1987, when he became Vice President-Production and Marketing. In 1991, Mr. Might was named Vice President-Advertising Sales.

In 1993, Mr. Might was promoted to President and Chief Operating Officer of Cable One (formerly named Post-Newsweek Cable). He became President and Chief Executive Officer of Cable One in 1994 and was elected to the Board in 1995.

Mr. Might serves on the boards of the American Cable Association, CableLabs, and C-SPAN. Mr. Might was a Combat Engineer Officer in the U.S. Army from 1972 to 1976.

**Ms. Julia M. Laulis**

Ms. Laulis has been Chief Executive Officer and a member of the Board since January 2017 and President of Cable One since January 2015.

Ms. Laulis joined Cable One in 1999 as Director of Marketing-NW Division. In 2001, she was named Vice President of Operations for the SW Division. In 2004, she accepted the additional responsibility for starting up Cable One's Phoenix Customer Care Center. In 2008, she was named Chief Operations Officer, and in 2012, she was named Chief Operating Officer of Cable One. In January 2015, she was promoted to President and Chief Operating Officer of Cable One.

Prior to joining Cable One, Ms. Laulis served in various senior marketing positions with Jones Communications. Ms. Laulis began her 30-plus-year career in the cable industry with Hauser Communications.

**Mr. Michael E. Bowker**

Mr. Bowker has been Senior Vice President, Chief Sales and Marketing Officer of Cable One since 2014.

Mr. Bowker joined Cable One in 1999 as Advertising Regional Sales Manager. Mr. Bowker was named Vice President of Sales in 2012, and was promoted to Senior Vice President, Chief Sales and Marketing Officer in 2014.

Prior to joining Cable One, Mr. Bowker was with AT&T Media Services and TCI Cable, where he served in various sales management positions.

**Mr. Kevin P. Coyle**

Mr. Coyle has been Senior Vice President and Chief Financial Officer of Cable One since March 2015.

Mr. Coyle has more than 30 years of financial and operations experience. Prior to joining Cable One, he served with Elauwit Networks, a private provider of telecom services to MDUs as Chief Financial Officer from September 2014 to March 2015 and as Senior Vice President – Business Development from May 2014 to September 2014. From 2012 to 2015, Mr. Coyle served as a director and as the chairman of the audit committee of WPCS International Incorporated, a publicly traded provider of fixed wireless technology services for corporations. Previously, Mr. Coyle performed strategic planning for Charter Communications and Comcast Communications in their MDU and business sales area as Senior Vice President – Business Development of Comcast from January 2011 to June 2011 and as a Principal with KPC Consulting, an independent, private consulting firm, from 2009 to January 2011 and from June 2011 to 2014. Before that, Mr. Coyle served as Treasurer and Chief Financial Officer at Jones Intercable, a publicly traded cable television company with 1.4 million subscribers that was acquired by Comcast in 1999. Mr. Coyle has been the Chief Executive Officer of two start-up companies and the Chief Financial Officer of two others in telecommunications and high-tech fields.

Table of Contents***Mr. Stephen A. Fox***

Mr. Fox has been Senior Vice President, Chief Network Officer of Cable One since July 2015.

Mr. Fox started his career in 1988 as a programmer/operator for Cable One (formerly named Post-Newsweek Cable). Mr. Fox's current areas of responsibility include long range planning and the strategic evolution of technology roadmaps related to products, internal and external networks and capital allocation. Prior to his current position, Mr. Fox was named Senior Vice President, Chief Technology Officer in 2008.

***Mr. Eric M. Lardy***

Mr. Lardy has been a Senior Vice President of Cable One since January 2017.

Mr. Lardy joined Cable One in 1997 as a manager in one of our systems and held a variety of positions of increasing responsibility in marketing, operations, and system general management. Mr. Lardy was named Vice President, Strategic Planning and Finance in 2014, and was promoted to Senior Vice President in January 2017.

***Mr. Charles B. McDonald***

Mr. McDonald has been Senior Vice President, Operations of Cable One since January 2016.

Mr. McDonald joined Cable One in 2008 as an Industrial Engineer. Mr. McDonald was named Vice President, Customer Service Operations in 2014, and was promoted to Senior Vice President, Operations in January 2016.

Prior to joining Cable One, Mr. McDonald worked as a Senior Process Engineer for Three-Five Systems and Brilliant Corp.

***Mr. Alan H. Silverman***

Mr. Silverman has been Senior Vice President, General Counsel, Director of Administration and Secretary of Cable One since January 2015.

From 1986 to December 2014, Mr. Silverman was Vice President, General Counsel, Director of Administration and Secretary of Cable One. Prior to joining Cable One, he was Assistant Counsel at Newsweek, Inc. (then a subsidiary of The Washington Post Company), and he also practiced law at Hughes Hubbard & Reed in New York.

**Regulation and Legislation*****General***

Our data, video and voice operations are subject to various requirements imposed by the U.S. local, state and Federal governmental authorities. The regulation of certain cable rates pursuant to procedures established by Congress has negatively affected our revenue. Certain other legislative and regulatory matters discussed in this section also have the potential to adversely affect our data, video and voice businesses. The following discussion does not purport to be a complete summary of all of the provisions of U.S. Federal and state law that may affect our operations. Proposals for additional or revised regulations and requirements are pending before Congress, state legislatures, and state and federal regulatory agencies. We generally cannot predict whether new legislation, court action, new regulations, or a change in the extent of application or enforcement of current laws and regulations would have an adverse impact on our operations.

***Cable***

Title VI of the U.S. Federal Communications Act of 1934, as amended (the "Communications Act"), establishes the principal federal regulatory framework for our operation of cable systems and for the provision of our video services. The Communications Act allocates primary responsibility for enforcing the federal policies among the FCC and state and local governmental authorities.

Table of Contents

*Franchising.* We are required to obtain franchises from state or local governmental authorities to operate our cable systems. Those franchises typically are non-exclusive and limited in time, contain various conditions and limitations and provide for the payment of fees to the local authority, determined generally as a percentage of revenues. Failure to comply with all of the terms and conditions of a franchise may give rise to rights of termination by the franchising authority. The FCC has adopted rules designed to expedite the process of awarding competitive franchises and relieving applicants for competing franchises of some locally-imposed franchise obligations. This development, which is especially beneficial to new entrants, is expected to continue to accelerate the competition we are experiencing in the video service marketplace.

*Rate Regulation.* FCC regulations prohibit LFAs or the FCC from regulating the rates that cable systems charge for certain levels of video cable service, equipment and service calls when those cable systems are subject to "effective competition." In 2015, the FCC revised its rate regulations to create a presumption that all cable systems are subject to the effective-competition exemption unless proven otherwise. That decision has been appealed to a U.S. Federal court, and we cannot predict the outcome.

*"Must-Carry" and Retransmission Consent and Content Rules.* U.S. Federal law provides that a television broadcast station may, subject to certain limitations, insist on carriage of its signal on cable systems located within the station's prescribed area. As a result, certain of our cable systems must carry broadcast stations that we might not otherwise have elected to carry.

In other cases, we have been required to provide consideration to broadcasters to obtain retransmission consent, such as commitments to carry other program services offered by a station or an affiliated company, to purchase advertising on a station or to provide advertising availabilities on cable to a station, or to provide cash compensation. This development results in increased operating costs for cable systems, which ultimately increases the rates cable systems charge subscribers. In March and November 2014, the FCC and Congress imposed new requirements in this area including restrictions on broadcasters' ability to jointly negotiate with cable providers for carriage of their stations, and the FCC is seeking comment on possible changes to regulations in this area, which could affect our business. In July 2016, the FCC announced that it would not adopt additional rules governing good faith negotiations for retransmission consent, but it would be prepared to assist in negotiations when necessary. In September 2014, the FCC repealed its sports blackout rules, which prohibited cable and satellite operators from retransmitting any sports event that was blacked out on a local broadcast station.

*Independent Programming.* On September 29, 2016, the FCC initiated a rulemaking proceeding to adopt rules prohibiting certain practices that may affect the relationship between multichannel video programming distributors ("MVPDs") such as cable companies and independent programmers. The proposal examines whether certain "most favored nation" and alternative distribution method provisions in program carriage agreements should be prohibited, and whether program bundling practices by large programmers affect the ability of MVPDs to carry independent programmers. We cannot predict whether the newly-constituted FCC will pursue this proceeding, and, if so, how it will proceed.

*Pole Attachments.* U.S. Federal law requires most telephone and power utilities to charge reasonable rates to cable operators for utilizing space on utility poles or in underground conduits. In May 2010 and again in April 2011, the FCC adopted new requirements relating to pole access and construction practices that were expected to improve the ability of cable operators to attach to utility poles on a timely basis and to lower the pole attachment rate for telecommunications services. In October 2013, the U.S. Supreme Court declined to review a lower court's decision to uphold the FCC's pole attachment regulations. The FCC further revised its pole attachment rules in November 2015 to adjust the formula for calculating pole rental rates, which resulted in similar rates for telecommunications attachments and cable attachments, and eliminated the ability of utility companies to justify higher rates for pole attachments used to provide broadband Internet access service. The FCC's revisions to the pole attachment rate formula have been challenged in a U.S. Federal court by the utility companies, where the matter is pending. In the meantime, the appropriate method for calculating pole attachment rates for cable operators that provide VoIP services remains unclear, although the FCC's recent rule revisions to equalize pole attachment rates make this issue less significant. We cannot predict the extent to which these and other rule changes will affect our ability over time to secure timely access to poles at reasonable rates for our data, voice and video services. As a general matter, changes to our pole attachment rate structure could significantly increase our annual pole attachment costs.

*U.S. Federal Copyright Issues.* The U.S. Federal Copyright Act of 1976, as amended (the "Copyright Act"), gives cable systems the ability, under certain terms and conditions and assuming that any applicable retransmission consents have been obtained, to retransmit the signals of television stations pursuant to a compulsory copyright license.

The U.S. Federal Copyright Office is considering requests for clarification and revisions of certain cable compulsory copyright license reporting requirements, and from time to time, other revisions to the cable compulsory copyright rules are considered. We cannot predict the outcome of any such inquiries. However, it is possible that changes in the rules or copyright compulsory license fee computations or compliance procedures could have an adverse effect on our business by, for example, increasing copyright

compulsory license fee costs or by causing us to reduce or discontinue carriage of certain broadcast signals that we currently carry on a discretionary basis.

Table of Contents

*Telephone Company Competition.* U.S. Federal law permits telephone companies to offer video programming services. Over the past decade, telephone companies have pursued multiple strategies to enter the market for the delivery of multichannel video programming services, such as merging with DBS operators, in the case of AT&T and DirecTV, or obtaining local franchise agreements. Increased competition from telephone companies that provide competing services could have a material effect on our business.

*Over-the-Top (OTT) Video Programming.* The continued proliferation of broadband services in the United States has enabled cable programmers and broadcast television stations and networks to “stream” their video content to consumers over the Internet. Although we have benefited generally from the growth in broadband due to our role as a provider of broadband services, the continued and growing availability of cable programming and broadcast television content on the Internet may result in less demand for our video cable service offering. Some providers of cable service are marketing their own version of OTT video programming, thus enabling their subscribers to access cable programming outside of their home or business. For example, Verizon Wireless offers the ability to stream NFL games on its smartphones over the Internet. Some fixed and wireless broadband providers are excluding certain streamed content from metered data charges or data limits in an effort to make their broadband service more attractive to consumers. In addition, online video distributors and other OTT video distributors have begun to stream broadcast programming over the Internet. In some cases, distributors streamed broadcast programming without the consent of broadcasters and copyright owners. Broadcasters challenged this practice, and in June 2014, the U.S. Supreme Court determined that such streaming requires the consent of the applicable copyright owner. However, there is a potential for other streaming services to attempt to enter the market, and in December 2014, the FCC opened a proceeding concerning how OTT providers should be classified for purposes of the FCC’s rules. We cannot predict the outcome of these proceedings, nor related litigation, nor how widespread these practices may become or the extent to which the integrated functionality and ease of use of the cable platform will continue to appeal to the majority of our subscribers.

*Wireless Services.* The FCC is in the process of preparing to auction additional spectrum, including spectrum currently in the television broadcast band, for use by wireless broadband providers. The FCC rules will provide for both the auction of spectrum and a “repacking,” whereby the FCC will require certain broadcast stations to move to new channel allotments so as to free up a nationwide block of spectrum for wireless broadband use. The availability of more spectrum to enable wireless video services over time will create additional competitive alternatives to cable services. The auction began in March 2016 and is scheduled to end in the first quarter of 2017, but we cannot predict when the auction will conclude or the effect it may have on us. After the auction concludes, the FCC is expected to allocate a portion of the \$1.75 billion reimbursement fund authorized by Congress to MVPDs that incur costs by continuing to carry stations that were reassigned to new channels. MVPDs, such as us, will be required to submit an estimate of their costs 90 days after the closing of the auction. We cannot predict the amount of funding, if any, that we might receive from the disbursement of these funds.

*Set-Top Boxes.* Congress, the FCC and other government agencies have for some time been developing and implementing regulations that affect the types of set-top boxes that cable operators can lease or deploy to their subscribers. Prior to 2015, FCC rules banned the integration of security and non-security function in set-top boxes and required MVPDs to allow third-party vendors to provide set-top boxes with basic converter functions. In 2015, Congress repealed the integration ban and mandated that the FCC establish a working group to a successor technology-and platform-neutral security solution. In February 2016, the FCC opened a rulemaking to consider proposals that would require any retail video device to work on any cable operator’s system, but the new administration has removed this item from active FCC review. We cannot predict if or when new changes may be proposed, what effect such changes may have on our operations, or if they will increase our costs and impair our ability to deliver programming to our customers.

*Disability Access.* In September 2010, Congress passed the Twenty-First Century Communications and Video Accessibility Act (the “CVAA”). The CVAA directs the FCC to impose additional accessibility requirements on cable operators. For example, cable operators that serve 50,000 or more subscribers must provide 50 hours of video description per calendar quarter, during prime time or on children’s programming, on each channel on which they carry one of the top five national non-broadcast networks. In addition, cable operators of all sizes must pass through video description that is provided for each broadcast station or non-broadcast network that they carry. Compliance imposes certain costs on us. The CVAA also directs the FCC to adopt rules to help ensure that persons with disabilities have access to video programming and related information. In October 2013, the FCC adopted a requirement that equipment used by consumers to access video programming and other services offered by cable operators make on-screen text menus and guides for the display or selection of video programming audibly accessible to individuals who are blind or visually impaired. The compliance deadline for these new rules was December 2016 (subject to certain exceptions). In October 2013, the FCC also initiated a proceeding to consider additional rules. In February 2014, the FCC issued an order adopting closed captioning quality standards for video programming distributors (“VPDs”) and, in February 2016, the FCC amended its rules to allocate responsibility for the quality of closed captioning between video programmers and VPDs. The FCC also revised its procedures for the handling of complaints

regarding closed captioning quality. We cannot predict any further actions the FCC will take in this proceeding or the extent to which any such requirements may impose new costs on us.

Table of Contents

In 2016, the FCC proposed to increase the number of video-described programming for covered broadcast and cable channels from 50 hours to 87.5 hours. The FCC also sought to increase the number of cable networks that are required to provide video-described programming. While a draft order implementing these increased requirements was expected to be voted on in September 2016, the FCC delayed its decision. We cannot predict if or how the new administration or newly-constituted FCC will proceed with these increased requirements or the extent that these obligations, if adopted, could impose costs on our business.

*Other Requirements.* The FCC regulates various other aspects of cable operations, including certain terms for commercial leased access, signal leakage, distant broadcast station signals and technical standards. We cannot predict whether, when or to what extent changes to these and other regulations may affect our operations or costs.

***Broadband Internet Access Service***

Broadband Internet access service, which we currently offer on virtually all of our cable systems, is subject to some regulation at the Federal level, and is not subject to state or local government regulation at this time.

*Regulatory Reclassification and Network Neutrality Regulation.* In 2015, the FCC elected, by a 3-2 vote, to reclassify broadband Internet access service as a “telecommunications service” and to subject the service to network neutrality and certain common carrier regulations under Title II of the Communications Act. The new regulations: (1) prohibit broadband Internet access service providers from blocking access to lawful content, applications, services or non-harmful devices; (2) prohibit broadband Internet access service providers from impairing or degrading lawful Internet traffic on the basis of content, applications or services; (3) prohibit broadband Internet access service providers from favoring lawful traffic from one provider of Internet content over lawful traffic of another content provider in exchange for consideration; (4) establish a new “general conduct standard” that prohibits broadband Internet access service providers from unreasonably interfering with or unreasonably disadvantaging the ability of consumers to select, access and use the lawful Internet content, applications, services or devices of their choosing; and (5) require broadband Internet access service providers to disclose information regarding network management, performance and commercial terms of the service to their customers. These new net neutrality obligations could cause us to incur certain compliance costs, and the FCC’s enforcement or interpretation of these new obligations could adversely affect our business. The FCC’s regulations have been challenged in a U.S. Federal court, and we cannot predict the outcome of that review. We also cannot predict if or how the new administration and newly-constituted FCC will revise these rules. States also may attempt to use the FCC’s reclassification of broadband Internet access service in an attempt to justify imposing new regulations or taxes and/or fees on broadband Internet access service providers that could adversely affect our business.

*Privacy.* Broadband Internet access service is subject to many of the same U.S. Federal and state privacy laws that apply to other electronic communications. These include the U.S. Federal Electronic Communications Privacy Act, which addresses interceptions of electronic communications that are in transit; the Stored Communications Act, which addresses acquisitions of electronic data in storage; and other Federal and state privacy laws and regulations. As the collection and use of consumer data becomes more prevalent in the communications industry, our compliance obligations may grow. In November 2016, the FCC adopted new rules for broadband Internet access services to protect the privacy of certain information broadband Internet access service providers obtain about their customers. These rules are subject to reconsideration before the FCC, and may be subject to court appeals. The new rules take effect at various times in 2017, and could be subject to review and revision by the new administration and the newly-constituted FCC. We cannot predict whether, when or to what extent these obligations may impose costs on our business.

In addition to FCC privacy regulations governing broadband Internet access service, the Federal Trade Commission also may exercise authority over privacy by using its existing authority over unfair and deceptive acts or practices to apply greater restrictions on the collection and use of personally identifiable and other information relating to consumers. It also has undertaken numerous enforcement actions against parties that do not provide sufficient security protections against the loss or unauthorized disclosure of this type of information. We also are subject to stringent data security and data retention requirements that apply to website operators and online services directed to children under 13 years of age, or that knowingly collect or post personal information from children under 13 years of age. Other privacy-oriented laws have been extended by courts to online video providers and are increasingly being used in privacy lawsuits, including class actions, against providers of video materials online. We cannot predict whether, when, or to what extent these obligations may impose costs on our business.

Table of Contents

We are also subject to state and federal laws and regulations regarding data security that primarily apply to sensitive personal information that could be used to commit identity theft. Most states have security breach notification laws that generally require a business to give notice to consumers and government agencies when certain information has been disclosed due to a security breach, and the FCC has adopted security breach rules for voice services and broadband Internet access services. Several states have also enacted general data security requirements to safeguard consumer information, including the proper disposal of consumer information. We cannot predict whether, when or to what extent these obligations may impose costs on our business.

*Digital Millennium Copyright Act.* Owners of copyrights and trademarks actively seek to prevent use of the Internet to violate their rights. For example, copyright and trademark owners assert claims that a customer used an Internet service or resources accessed via the Internet to post, download or disseminate copyrighted music, movies, software or other content without the consent of the copyright owner or to seek to profit from the use of the goodwill associated with another person's trademark. In some cases, copyright and trademark owners have sought to recover damages from the broadband Internet access service provider, as well as or instead of the customer. The law relating to the potential liability of broadband Internet access service providers in these circumstances is unsettled. In 1998, Congress adopted the Digital Millennium Copyright Act, which grants broadband Internet access service providers protection against certain claims of copyright infringement resulting from the actions of customers if the Internet provider complies with certain requirements. So far, Congress has not adopted similar immunity for broadband Internet access service providers for trademark infringement claims.

*Business Data Services.* In April 2016, the FCC proposed new rules for "business data services" (formerly known as "special access" services). These services provide dedicated point-to-point transmission of data at certain guaranteed speeds and service levels using high-capacity connections. The FCC proposed new rate regulation and other regulatory mandates that could apply to business data services offered by cable companies. The proposed rules or any variation of the proposed rules, if implemented, could impose substantial costs on us and have other significant adverse effects on our business. It appears the newly-constituted FCC has removed this item from review by the FCC for the time being. It is uncertain whether the FCC will pursue other rules in this area.

#### *Voice*

*Voice Over Internet Protocol (VoIP).* Cable companies, including Cable One and others, offer VoIP service, which permits users to make voice calls over broadband communications networks, including the Internet, to recipients on the public switched telephone network and other broadband communications networks. U.S. Federal law preempts state and local regulatory barriers to the offering of voice service by cable companies and others, and the FCC and U.S. Federal courts generally have preempted state laws that seek to regulate or classify VoIP.

The FCC has held that VoIP services are IP-enabled services, which are interstate in nature and thus subject exclusively to the FCC's U.S. Federal jurisdiction and not to state regulation. This decision was upheld on appeal, although the FCC has an ongoing proceeding to consider whether VoIP services provided by cable companies and others are properly classified as an "information service," "telecommunications service" or some other new category of service. This determination, once made, could have numerous regulatory implications for cable companies that provide interconnected VoIP services, including us. Although the FCC has yet to ascribe a regulatory definition to VoIP services, the FCC nevertheless has imposed a number of obligations on interconnected VoIP service providers, some of which are discussed more fully below.

*Emergency 911 Services.* The FCC has ruled that an interconnected VoIP service provider that enables its customers to make calls to and receive calls from persons who use the public switched telephone network must provide its customers with the same enhanced 911 ("E911") features that traditional telephone and wireless companies are obligated to provide. This requirement was upheld on appeal. In January 2015, the FCC established indoor location requirements when E911 calls are made by interconnected VoIP subscribers. The FCC also requires certain providers of facilities-based fixed, residential voice services, which includes interconnected VoIP service providers, to offer backup power options to consumers, and to inform consumers of the availability of such options.

*CALEA.* FCC regulations require providers of interconnected VoIP service to comply with the requirements of the Communications Assistance for Law Enforcement Act, which requires covered entities and their equipment suppliers to deploy equipment that law enforcement officials can access readily for lawful wiretap purposes.

Table of Contents

*Universal Service.* The FCC has determined that interconnected VoIP service providers must contribute to the U.S. Federal Universal Service Fund (the "USF"). The amount of a company's USF contribution is based on a percentage of revenues earned from end-user interstate and international interconnected VoIP services. We are permitted to recover these contributions from our customers. In October 2011, the FCC adopted an order and new rules intended to transition the USF so that it supports the build out of broadband, rather than telecommunications facilities. The order principally addressed the manner in which universal service funds will be distributed to network operators for broadband build out. In April 2012, the FCC initiated a proceeding that focused on reforming the nature and manner in which entities should contribute to the USF and at what levels. We cannot predict whether and how such reform will occur and the extent to which it may affect providers of VoIP services, including us and our competitors. The FCC's 2011 universal service reform order was subject to both reconsideration requests and appeals, and in May 2014, the U.S. Court of Appeals for the Tenth Circuit upheld the order in its entirety. A number of parties filed petitions with the U.S. Supreme Court seeking review of that decision, but the Supreme Court declined to review the case. In November 2010, the FCC determined that states may impose state USF fees on interconnected VoIP service providers subject to certain limitations and requirements. State USF contributions are based on a percentage of revenues earned from end-user intrastate interconnected VoIP services, and we are typically permitted to recover these contributions from our customers. We cannot predict whether or how the imposition of such state-based universal service fees will affect our operations and business. In addition, the FCC has focused on subsidizing broadband deployment, and this shift could help some of our competitors. For example, the FCC substantially revised the program that provides universal service support for services to schools and libraries to shift support from voice services to broadband services and the deployment of Wi-Fi networks. Similarly, the FCC has expanded its Lifeline subsidy program for low-income consumers to include broadband services in addition to voice services. However, the newly-constituted FCC may revisit these subsidy programs and how they are funded. We cannot predict whether or how these programs will be changed.

*Intercarrier Compensation.* The order and new rules adopted by the FCC in October 2011 in connection with universal service reform also addressed intercarrier compensation and specified that "VoIP-PSTN traffic," that is, traffic exchanged over public switched telephone network facilities that originates and/or terminates in IP format, which includes interconnected VoIP traffic, is subject to intercarrier compensation obligations either on the basis of specified default charges or through negotiated rates. The FCC's order was subject to both reconsideration requests and appeals, and the U.S. Court of Appeals for the Tenth Circuit upheld the order in its entirety. A number of parties filed petitions with the U.S. Supreme Court seeking review of that decision, but the Supreme Court declined to review the case. Future FCC determinations regarding the rates, terms and conditions for transporting and terminating such traffic could have a profound and material effect on the profitability of providing voice and data services.

*Customer Proprietary Network Information.* In 2007, the FCC adopted rules expanding the protection of Customer Proprietary Network Information ("CPNI") and extending CPNI protection requirements to providers of interconnected VoIP service. CPNI is information about the quantity, technical configuration, type, location and amount of a voice customer's use. These requirements generally have increased the cost of providing interconnected VoIP service, as providers now must implement various safeguards to protect CPNI from unauthorized disclosure. In its November 2016 decision applying privacy requirements to broadband Internet access services, the FCC also revised the CPNI rules applied to interconnected VoIP services.

*Access for Persons with Disabilities.* FCC regulations require providers of interconnected VoIP services to comply with all disability access requirements that apply to telecommunications carriers, including the provision of telecommunications relay services for persons with speech or hearing impairments. The FCC also has adopted reporting requirements associated with disability access obligations. We and other interconnected VoIP service providers must also contribute to the interstate Telecommunications Relay Service Fund to support such access. These requirements generally have had the effect of increasing the cost of providing VoIP services.

*Service Discontinuance and Outage Obligations.* In 2009, the FCC adopted rules subjecting providers of interconnected VoIP services to the same service discontinuance requirements applicable to providers of wireline telecommunication services. In 2012, the FCC adopted mandatory outage reporting requirements for interconnected VoIP service providers, which apply when customers of interconnected VoIP service lose service or connectivity and, as a result, are unable to access 911 service. Along with other FCC actions described in this section, which impose legacy telecom obligations on interconnected VoIP providers, this development will subject our interconnected VoIP services to greater regulation and, therefore, greater burdens and costs.

*Regulatory Fees.* The FCC requires interconnected VoIP service providers to contribute to shared costs of FCC regulation through an annual regulatory fee assessment. These fees have increased our cost of providing VoIP services. The FCC from time to time revises its regulatory fees and sometimes creates new fees. We cannot predict when or the extent to which the FCC will adopt new rules or regulatory fees affecting VoIP service providers, which could affect our cost of doing business.



Table of Contents

*Local Number Portability.* Providers of interconnected VoIP services and their “numbering partners” must ensure that their subscribers have the ability to port their telephone numbers when changing service providers. We, along with other providers of interconnected VoIP service, must contribute funds to cover the shared costs of local number portability and the costs of North American Numbering Plan Administration. In June 2015, the FCC adopted rules requiring additional numbering requirements, such as allowing consumers access to abbreviated dialing codes like 211 and 311 in certain circumstances, to be applied to interconnected VoIP service providers. Although consumers’ ability to port their existing telephone numbers to interconnected VoIP service has created additional opportunities for us to gain voice customers, the local number portability and associated rules overall have had the effect of increasing the cost of providing VoIP service.

*Rural Calling Issues.* In October 2013, the FCC adopted new rules to combat problems with the completion of long-distance calls to rural areas. The new rules apply detailed record keeping, record retention and reporting requirements on all voice providers, including VoIP service providers, subject to certain exceptions. The rules also prohibit VoIP service providers (and other voice providers) from using false audible ringing when originating calls. Compliance with these new rules could have the effect of increasing the cost of providing VoIP services.

**State and Local Taxes**

The Internet Tax Freedom Act prohibits most states and localities from imposing taxes on Internet access service charges. Legislative and administrative proceedings in some states and localities have imposed or are considering adopting changes to general business taxes, central assessments for property tax and new taxes and fees applicable to our services. Often, DBS and other competitors that deliver their services over the Internet do not face similar state tax and fee burdens. In addition, the FCC’s reclassification of broadband Internet access services as Title II telecommunications services may cause or allow, directly or indirectly, some states and localities to seek to impose additional taxes and fees on our data service.

**ITEM 1A. RISK FACTORS**

You should carefully consider all of the information in this Annual Report on Form 10-K and each of the risks described below, which we believe are the principal risks that we face. Some of the risks relate to our business, others to the spin-off. Some risks relate principally to the securities markets and ownership of our common stock.

Any of the following risks could materially and adversely affect our business, financial condition and results of operations and the actual outcome of matters as to which forward-looking statements are made in this Annual Report on Form 10-K.

**Risks Relating to Our Business**

*We face significant competition from other cable companies and telephone companies, as well as other well-capitalized entrants in the video and data services industry, which could reduce our market share and lower our profits.*

We operate in highly competitive, subscriber-driven and rapidly changing environments and compete with a growing number of companies that provide a broad range of communications products, services and content to subscribers. Our competitors have historically included, and we expect will continue to include, over-the-air reception providers; DBS providers; telephone companies that offer data and video services through DSL or fiber-to-the-node networks; and other cable companies that have been granted a franchise to operate in a geographic market in which we are already operating.

Substantially all of our cable systems are in markets in which CenturyLink or AT&T is the established local telephone company and our primary competitor. The remainder of our cable systems are in markets where we compete with various other companies. Our cable systems generally operate pursuant to franchises, permits and similar authorizations issued by LFAs, and these franchises are typically non-exclusive. Accordingly, LFAs can grant additional franchises to our competitors and create competition in our markets where none existed previously, resulting in overbuilds. In some cases, the FCC has adopted rules that streamline entry for new competitors (particularly those affiliated with telephone companies) and reduce franchising burdens for these new entrants. Although as a general matter Internet service providers have upgraded their data networks to enable faster upload and download speeds for their customers in metropolitan markets before upgrading their data networks in our markets, CenturyLink, AT&T (through its U-verse brand) and other companies have overbuilt approximately 28% of our homes passed with fiber-to-the-node or other high-speed networks, such that they are able to offer data, video and voice services, including data services with high access speeds, albeit generally lower when compared to those that we offer. Further overbuilding could cause more of our customers to purchase data and video services from our competitors instead of from us. In our other markets, some of our telephone company competitors have entered into strategic partnerships or other arrangements with DBS operators that permit these telephone companies to package the

video services of DBS operators with their own DSL, landline voice and wireless voice services. An example of such arrangement is the merger of AT&T and DirecTV. We also face increasing competition for residential voice services from wireless telephone companies, as some of our customers are replacing our landline voice service completely with wireless voice service.

Table of Contents

In addition, new entrants with significant financial resources may compete on a larger scale with our video and data services. For example, several years ago, Alphabet launched Google Fiber, which offers data and video services in several areas of the country. Google Fiber's infrastructure consists of fiber optic wirelines, which is technologically superior to the DSL technology of a number of our competitors. Given its financial resources, Alphabet may further expand into regions in which we compete, as well as prompt our competitors to continue to upgrade their own networks in order to be able to offer increased download and upload speeds necessary to remain competitive. Alphabet's size and financial resources may enable it to continue to upgrade its infrastructure. Although Alphabet announced in the fourth quarter of 2016 that it was pausing its Google Fiber expansion in most of its potential Google Fiber cities, if Alphabet expands its Google Fiber offerings into our markets, it may be able to offer our current customers attractive pricing and technology, increasing competition in our markets.

A number of municipalities have also announced plans to construct their own data networks with access speeds that match or exceed those of our own through the use of fiber optic technology. In some cases, local government entities and municipal utilities may legally compete with us without obtaining a franchise from an LFA, reducing their barriers to entry into our markets. The entrance of municipalities as competitors in our markets would add to the competition we face and could lead to additional customer attrition.

Our video business also faces substantial and increasing competition from other forms of in-home entertainment and recreational activities, including video games, mobile apps and the Internet, as well as from other media companies. Internet and other media companies, including Alphabet, Amazon, Apple, Sling TV, Hulu and Netflix, increasingly offer video programming via OTT streaming on the Internet. Because of the significant size and financial resources of such companies, we anticipate that they will continue to invest resources in increasing the availability of video content on the Internet, which may result in less demand for the video services we provide. In addition, companies that offer OTT content in certain markets also provide data services, such as Alphabet, and they may seek to increase sales of their streaming content by lowering the cost of data services for their customers, which would further increase price competition for the data services we offer. In addition to creating competition for our video services business, OTT content also significantly increases the volume of traffic on our data networks, which can lead to decreases in access speeds for all users if data networks are not upgraded so that their broadband capacity can keep pace with increased traffic. Any of these events could have a material negative impact on our operations, business, financial results and financial condition.

*Our business is characterized by rapid technological change, and if we do not adapt to technological changes and respond appropriately to changes in consumer demand, our competitive position may be harmed.*

Our success is, to a large extent, dependent on our ability to acquire, develop, adopt, upgrade and exploit new and existing technologies to address consumers' changing demands and distinguish our services from those of our competitors. We may not be able to accurately predict technological trends or the success of new products and services. If we choose technologies or equipment that are less effective, cost-efficient or attractive to our customers than those chosen by our competitors, or if we offer services that fail to appeal to consumers, that are not available at competitive prices or that do not function as expected, our competitive position could deteriorate, and our business and financial results could suffer.

The ability of some of our competitors to introduce new technologies, products and services more quickly than we can may adversely affect our competitive position. Furthermore, advances in technology, decreases in the cost of existing technologies or changes in competitors' product and service offerings may require us in the future to make additional research and development expenditures or to offer at no additional charge or at a lower price certain products and services that we currently offer to customers separately or at a premium.

In addition, we seek to leverage overall industry experience before rolling out new technology in order to avoid investing in technology that has not been proven successful in other markets. We implement this approach to avoid costly mistakes made by early adopters of new technology that does not provide expected returns, and it exposes us to the risk that one of our competitors will adopt successful new technology before us, and leverage this new technology to attract our customers, increasing the level of customer attrition we experience and adversely affecting our business.

Table of Contents***Business services sales increasingly contribute to our results of operations, and we face risks as we attempt to further focus on sales to our business customers.***

Growth in revenue from sales to our business customers has exceeded 13% for each year since we started focusing on business services sales in 2011, and we may encounter challenges as we continue our initiative to expand sales of data, voice and video services to our business customers. To accommodate this expansion, we expect to commit a greater proportion of our expenditures on technology, equipment and personnel focused on our business customers. If we are unable to sufficiently maintain the necessary infrastructure and internal support functions necessary to service these customers, potential future growth of our business services revenues would be limited. In many cases, business customers have service level agreements that require us to provide higher standards of service and reliability. If we are unable to meet these service level requirements, or more broadly, the expectations of our business customers, we would no longer expect business sales to increase and our results of operations may be materially negatively affected.

***The increase in programming costs and retransmission fees may continue in the future, resulting in lower margins than we anticipate.***

Over the past few years, the sales margins on our residential video services, which accounted for 36.0%, 41.2% and 44.4% of our total revenues in 2016, 2015 and 2014, respectively, have decreased as a result of increased programming costs and retransmission fees and customer cord-cutting. Programming costs and retransmission fees paid to major programmers may continue to increase as programmers are expected to ask for higher fees. Moreover, programming cost increases have caused us, and may in the future cause us, to cease carrying channels offered by certain programmers, which may result in attrition of video subscribers as well as customers who subscribe to double-play or triple-play packages that include video service. These customer losses and increased costs could result in further decreases in our residential video margins and adversely impact our business.

***We may not be able to obtain necessary hardware, software and operational support.***

We depend on a limited number of third-party suppliers and licensors to supply some of the hardware and software necessary to provide some of our services, including our access to the network backbone and the set-top boxes and modems that we lease to our customers. Some of these vendors represent our sole source of supply or have, either through contract or as a result of intellectual property rights, a position of some exclusivity. If any of these parties breaches or terminates its agreement with us or otherwise fails to perform its obligations in a timely manner, demand exceeds these vendors' capacity, they experience operating or financial difficulties, they significantly increase the amount we pay for necessary products or services or they cease production of any necessary product due to lack of demand, profitability, a change in their ownership or otherwise, our ability to provide some services may be materially adversely affected. Any of these events could adversely affect our ability to retain and attract subscribers and have a material negative impact on our operations, business, financial results and financial condition.

***We may make acquisitions, which could involve inherent risks and uncertainties.***

We may make acquisitions, which could involve inherent risks and uncertainties, including:

- the difficulty in integrating newly acquired businesses and operations in an efficient and effective manner;
- the challenge in achieving strategic objectives, cost savings and other anticipated benefits;
- the potential loss of key employees of the acquired businesses;
- the potential diversion of senior management's attention from our ongoing operations;
- the risks associated with integrating financial reporting and internal control systems;
- the difficulty in expanding information technology systems and other business processes to incorporate the acquired businesses;
- potential future impairments of goodwill associated with the acquired businesses; and
- in some cases, the potential for increased regulation.

If an acquired business fails to operate as anticipated, cannot be successfully integrated with our existing business or one or more of the other risks and uncertainties identified above occur in connection with our acquisitions, our operations, business, results of operations and financial condition could be materially negatively affected.

Table of Contents***Adverse conditions in the U.S. economy could impact our results of operations.***

Unfavorable general economic conditions, such as a recession or economic slowdown in the United States, could negatively affect the affordability of and demand for some of our products and services. In difficult economic conditions, consumers may seek to reduce discretionary spending by forgoing purchases of our products, electing to use fewer higher margin services or obtaining lower cost products and services offered by other companies. Similarly, under these conditions the business customers that we serve in the United States may delay purchasing decisions, delay full implementation of service offerings or reduce their use of services. In addition, adverse economic conditions may lead to an increased number of our residential and business customers that are unable to pay for services. Such conditions could also inhibit or prevent our third-party suppliers and licensors from supplying some of the hardware and software necessary to provide some of our services. If any of these events were to occur, it could have a material negative effect on our operations, business, financial condition and results of operations.

***We rely on network and information systems and other technology, and a disruption or failure of such networks, systems or technology as a result of computer viruses, "cyber attacks," misappropriation of data or other malfeasance, as well as outages, natural disasters (including extreme weather), terrorist attacks, accidental releases of information or similar events, may disrupt our business.***

Network and information systems and other technologies are critical to our operating activities, both to internal uses and in supplying data, video and voice services to customers. Network or information system shutdowns or other service disruptions caused by events such as computer hacking, dissemination of computer viruses, worms and other destructive or disruptive software, "cyber attacks," process breakdowns, denial of service attacks and other malicious activity pose increasing risks. Both unsuccessful and successful "cyber attacks" on companies have continued to increase in frequency, scope and potential harm in recent years and, because the techniques used in such attacks have become more sophisticated and change frequently, we may be unable to anticipate these techniques or implement adequate preventative measures. From time to time third parties make malicious attempts to access our network. Any successful attempts could result in an unauthorized release of information, degradation to our network and information systems or disruption to our data, video and voice services, all of which could adversely affect our results of operations.

Our network and information systems are also vulnerable to damage or interruption from power outages, natural disasters (including extreme weather arising from short-term weather patterns or any long-term changes), terrorist attacks and similar events. For example, the damage to our network infrastructure caused by Hurricane Katrina and the Joplin, Missouri tornado each created a significant disruption in our ability to provide services in affected areas. Any of these events could have an adverse impact on us and our customers in the future, including degradation of service, service disruption, excessive call volume to call centers and damage to our plant, equipment, data and reputation. Such an event also could result in large expenditures necessary to repair or replace such networks or information systems or to protect them from similar events in the future. Further, the impacts associated with extreme weather or any long-term changes, such as intensified storm activity, may cause increased business interruptions.

Furthermore, our operating activities could be subject to risks caused by misappropriation, misuse, leakage, falsification or accidental release or loss of information maintained in our information technology systems and networks and those of third-party vendors, including customer, personnel and vendor data. We provide certain confidential, proprietary and personal information to third parties in connection with our business, and there is a risk that this information may be compromised. Any such compromise could require us to implement costly remediation measures.

Various U.S. Federal, state and international laws and regulations govern the collection, use, retention, sharing and security of consumer data. This area of the law is evolving, and interpretations of applicable laws and regulations differ. Legislative and regulatory activity in the privacy area may result in new laws that are relevant to our operations, for example, use of consumer data for marketing or advertising. Claims of failure to comply with our privacy policies or applicable laws or regulations could form the basis of governmental or private-party actions against us. Such claims and actions may cause damage to our reputation and could have an adverse effect on our business.

Table of Contents

***Intellectual property and proprietary rights of others could prevent us from using necessary technology to provide our services or subject us to expensive intellectual property litigation.***

We periodically receive claims from third parties alleging that our network and information technology infrastructure infringes the intellectual property rights of others. We are generally named as joint defendants in these suits together with other providers of data, video and voice services. Typically these claims allege that aspects of our cable system architecture, electronic program guides, cable modem technology and VoIP services infringe on process patents held by third parties. It is likely that we will continue to be subject to similar claims as they relate to our cable business. Addressing these claims is a time-consuming and expensive endeavor, regardless of the merits of the claims. In order to resolve such a claim, we could determine the need to change our method of doing business, enter into a licensing agreement or incur substantial monetary liability. It is also possible that our business could be enjoined from using the intellectual property at issue, causing us to significantly alter our operations. If any such claims are successful, then the outcome would likely affect our services utilizing the intellectual property at issue and could have a material adverse effect on our operating results.

***If we are unable to retain key employees, our ability to manage our business could be adversely affected.***

Our operational results have depended, and our future results will depend, upon the retention and continued performance of our management team. The competitive environment for management talent in the broadband communications industry could adversely impact our ability to retain and hire new key employees for management positions. The loss of the services of key members of management and the inability or delay in hiring new key employees could adversely affect our ability to manage our business and our future operational and financial results.

**Risks Relating to Regulation and Legislation**

***The profitability of our data services offerings may be impacted by legislative or regulatory efforts to impose "net-neutrality" and other new requirements on cable operators.***

The majority of our current Adjusted EBITDA less capital expenditures comes from residential data services, and we expect that a majority of our residential customers will be data-only in the future. We have aligned our resources to emphasize increased sales of data services, as well as sales to business customers. In order to continue to generate Adjusted EBITDA less capital expenditures at our desired level from data services, we need the continued flexibility to develop and refine business models that respond to changing consumer uses and demands and to manage data usage efficiently, including by charging our data subscribers higher rates based on the overall bandwidth capacity available to, or used by, them, referred to as "usage-based billing." Our ability to implement usage-based billing or other network management initiatives in the future may be restricted by the FCC's "net-neutrality" requirements on cable operators.

To the extent the FCC in the future limits our ability to price our data services, we may not be able to generate the margins on our data services that we anticipated in shifting our focus from video to data services, and our business could be materially negatively impacted. While the FCC forbore from requirements that would require cable companies to contribute a portion of their revenues from data services to the USF, the FCC also ruled that it may revisit this determination in the future. Current rules only require that a portion of revenues from VoIP services be contributed to the USF. The changes brought about by how USF monies are distributed may provide funding and subsidies to those who either compete with us or seek to compete with us and therefore put us at a competitive disadvantage. Moreover, if the FCC imposes USF fees on broadband services, bundled services or a larger portion of VoIP services, it would increase the cost of our services and harm our ability to compete.

Given that the scope of the FCC's network neutrality regulations is not fully defined and given that the rules create procedural mechanisms for parties to complain of violations, it is reasonable to expect litigation to resolve ambiguities, which could lead to yet further regulation. It also is possible that the FCC's network neutrality regulations will be reduced or eliminated entirely as a result of the new administration and the newly-constituted FCC. The regulation of broadband activities and any related court decisions could restrict our ability to profit from our existing broadband network and limit the return we can expect to achieve on past and future investments in our broadband networks. We cannot predict what, if any, proposals might be adopted or what effect they might have on our business.

***Our video and voice services are subject to additional regulation by U.S. Federal, state and local authorities, which may impose additional costs and restrictions on our businesses.***

Our video services business operates in a highly regulated environment. Our cable systems generally operate pursuant to franchises, permits and similar authorizations issued by LFAs controlling the public rights-of-way, which typically are non-exclusive

and limited in time, contain various conditions and limitations and provide for the payment of fees to the local authority, determined generally as a percentage of revenues. Failure to comply with all of the terms and conditions of a franchise may give rise to rights of termination by the franchising authority.

We have the ability, pursuant to the Copyright Act, under certain terms and conditions, to retransmit the signals of television stations pursuant to a compulsory copyright license. From time to time, revisions to the cable compulsory copyright rules are considered. It is possible that changes in the rules or copyright compulsory license fee computations or compliance procedures could have an adverse effect on our business by, for example, increasing copyright compulsory license fee costs or by causing us to reduce or discontinue carriage of certain broadcast signals that we currently carry on a discretionary basis.

Table of Contents

In addition, Congress, the FCC and other government agencies have implemented regulations that affect the types of set-top boxes that we can lease or deploy to our subscribers, and we expect these regulations to change in the future. Most recently, in January 2013, the U.S. Department of Energy tentatively designated set-top boxes and network equipment as covered consumer products and proposed to adopt a new test procedure for set-top boxes as part of its Energy Conservation Program for Consumer Products and Certain Commercial and Industry Equipment. In December 2013, the Department of Energy withdrew its proposed rules to designate set-top boxes and network equipment as a covered product and to establish a test procedure for set-top boxes, but stated that it would consider reinitiating the rulemaking. Imposing energy conservation regulations on the hardware products we provide to our customers could impede innovation and require mandatory upgrades in our set-top boxes and be costly to us. In February 2016, the FCC announced a notice of proposed rulemaking that would allow any manufacturer to create cable boxes that can access pay-TV services so that consumers are not required to lease set-top boxes from cable and satellite providers, but the newly-constituted FCC has removed this item from review by the FCC for now. We cannot predict when, whether or to what extent any of these proposals will be resolved or how they will affect our operations.

Our voice services business is also subject to a growing degree of regulation. Complying with these regulations may increase the costs we incur and decrease the revenues we derive from our voice business. While the compliance costs associated with the current regulatory structure applicable to our voice services business are manageable, changes in this regulatory structure are unpredictable and have the potential to further negatively impact our voice services business by increasing compliance costs and/or taxes.

***Our cable system franchises are subject to non-renewal or termination. The failure to renew a franchise in one or more markets could adversely affect our business.***

Many of the LFAs from whom we have obtained franchises, permits and similar authorizations required to operate our video services business have established comprehensive facilities and service requirements, as well as specific customer service standards and monetary penalties for non-compliance. In many cases, our franchises are terminable if we fail to comply with significant provisions set forth in the applicable franchise agreement governing our video operations. Franchises are generally granted for fixed terms and must be periodically renewed. LFAs may resist granting a renewal if either past performance or the prospective operating proposal is considered inadequate. LFAs often demand concessions or other commitments as a condition to renewal. The traditional cable franchising regime has recently undergone significant change as a result of various federal and state actions. Some state franchising laws do not allow us to immediately opt into favorable statewide franchising. In many cases, state franchising laws will result in fewer franchise imposed requirements for our competitors who are new entrants than for us, until we are able to opt into the applicable state franchise. We cannot assure that we will be able to comply with all significant provisions of our franchise agreements and certain of our franchisers have from time to time alleged that we have not complied with these agreements. Additionally, although historically we have renewed our franchises without incurring significant costs, we cannot assure that we will be able to renew, or to renew as favorably, our franchises in the future. A termination of or a sustained failure to renew a franchise in one or more markets could materially negatively affect our business in the affected geographic area.

In addition, certain of our franchise agreements require that the applicable LFA approve a transfer of control of our Company. Although FCC rules provide that a transfer application shall be deemed granted if it is not acted upon within a 120 days after submission, as a practical matter, cable operators often waive the deadline if the LFA has not completed its review to facilitate discussions and thereby avoid an LFA denying the transfer of control. Failure to obtain such consents on commercially reasonable and satisfactory terms may impair our entitlement to the benefit of these franchise agreements in the future and could materially negatively affect our business.

Table of Contents***We may encounter increased pole attachment costs.***

Under U.S. Federal law, we have the right to attach cables carrying video and other services to telephone and similar poles and underground conduits owned by utility companies. In addition, U.S. Federal law requires most telephone and power utilities to charge reasonable rates to cable operators for utilizing space on utility poles or in underground conduits in order to transmit video services to customers. However, because these cables may carry services other than video services, such as voice services, some utility pole owners have sought to impose on cable companies a telecommunications rate for utilizing pole space for voice services, which is higher than the statutory rate charged to cable operators for video services. In May 2010 and again in April 2011, the FCC adopted new requirements relating to pole access and construction practices that were expected to improve the ability of cable operators to attach to utility poles on a timely basis and to lower the pole attachment rate for voice services. In October 2013, the U.S. Supreme Court declined to review a lower court's decision to uphold the FCC's pole attachment regulations. The FCC further revised its pole attachment rules in November 2015 to adjust the formula for calculating pole rental rates, which resulted in similar rates for telecommunications attachments and cable attachments, and eliminated the ability of utility companies to justify higher rates for pole attachments used to provide broadband Internet access service. Those rules are being challenged in a U.S. Federal court by the utility companies, where the matter is pending. In the meantime, the appropriate method for calculating pole attachment rates for cable operators that provide VoIP services remains unclear, although the FCC's recent rule revisions to equalize pole attachment rates make this issue less significant. We cannot predict the extent to which regulatory changes may affect our ability over time to secure timely access to poles at reasonable rates for our data, voice and video services. As a general matter, changes to our pole attachment rate structure could significantly increase our annual pole attachment costs and materially negatively impact our operations, business, financial condition and results of operations.

***LFA's have the ability to impose additional regulatory constraints on our business, which could further increase our expenses.***

In addition to the franchise agreement, LFAs in some jurisdictions have adopted cable regulatory ordinances that further regulate the operation of cable systems, and the services we provide in the jurisdiction. This additional regulation increases the cost of operating our business. LFAs may impose new and more restrictive requirements. LFAs who are certified to regulate rates in their communities generally have the power to reduce rates and order refunds on the rates charged for basic video service and equipment.

***Changes in broadcast carriage regulations could impose significant additional costs.***

Although we would likely choose to carry all primary video feeds of local broadcast stations in the markets in which we operate voluntarily, so-called "must carry" rules could, in the future, require us to carry some local broadcast television signals on some of our cable systems that we might not otherwise carry. If the FCC seeks to revise or expand the "must carry" rules, such as to require carriage of multicast streams, we would be forced to carry video programming that we would not otherwise carry and potentially drop other, more popular programming in order to free capacity for the required programming, which could make us less competitive. Moreover, if the FCC adopts rules that are not competitively neutral, cable operators could be placed at a disadvantage versus other video providers. Any of these events could adversely affect our business.

**Risks Related to Our Spin-Off from GHC**

***The spin-off could result in significant tax liability to GHC and its stockholders, and we could have an indemnification obligation to GHC if the Distribution were determined not to qualify for non-recognition treatment, which could materially adversely affect our financial condition.***

Completion of the spin-off required GHC's receipt of a written opinion of Cravath, Swaine & Moore LLP to the effect that the Distribution should qualify for non-recognition of gain and loss under Section 355 of the Internal Revenue Code of 1986, as amended (the "Code").

The opinion of counsel did not address any U.S. state or local or foreign tax consequences of the spin-off. The opinion assumed that the spin-off was completed according to the terms of the Separation and Distribution Agreement and the Tax Matters Agreement with GHC and relied on the facts as stated in the Separation and Distribution Agreement, the Tax Matters Agreement, the other ancillary agreements, the Information Statement included in our registration statement on Form 10 and a number of other documents. In addition, the opinion was based on certain representations as to factual matters from GHC, us and Donald E. Graham. The opinion cannot be relied on if any of the assumptions, representations or covenants are incorrect, incomplete or inaccurate or are violated in any material respect.

The opinion of counsel is not binding on the Internal Revenue Service (the "IRS") or the courts, and there can be no assurance that the IRS or a court will not take a contrary position. GHC has not requested, and does not intend to request, a ruling from the IRS

regarding the U.S. Federal income tax consequences of the spin-off.

Table of Contents

If the Distribution were determined not to qualify for non-recognition of gain and loss, "U.S. Holders" (defined as a beneficial owner of GHC common stock that is a United States person for purposes of the Code) could be subject to tax. In this case, each U.S. Holder who received our common stock in the Distribution would generally be treated as receiving a distribution in an amount equal to the fair market value of our common stock received, which would generally result in (1) a taxable dividend to the U.S. Holder to the extent of that U.S. Holder's pro rata share of GHC's current and accumulated earnings and profits; (2) a reduction in the U.S. Holder's basis (but not below zero) in GHC common stock to the extent the amount received exceeds the stockholder's share of GHC's earnings and profits; and (3) a taxable gain from the exchange of GHC common stock to the extent the amount received exceeds the sum of the U.S. Holder's share of GHC's earnings and profits and the U.S. Holder's basis in its GHC common stock.

If, due to any of our representations being untrue or our covenants being breached, it were determined that the Distribution did not qualify for non-recognition of gain and loss under Section 355 of the Code, we could be required to indemnify GHC for the resulting taxes and related expenses. Any such indemnification obligation could materially adversely affect our financial condition.

In addition, Section 355(e) of the Code generally creates a presumption that the Distribution would be taxable to GHC, but not to stockholders, if we or our stockholders were to engage in transactions that result in a 50% or greater change by vote or value in the ownership of our stock during the four-year period beginning on the date that begins two years before the date of the Distribution, unless it were established that such transactions and the Distribution were not part of a plan or series of related transactions giving effect to such a change in ownership. If the Distribution were taxable to GHC due to such a 50% or greater change in ownership of our stock, GHC would recognize gain equal to the excess of the fair market value of our common stock distributed to GHC stockholders over GHC's tax basis in our common stock and we generally would be required to indemnify GHC for the tax on such gain and related expenses. Any such indemnification obligation could materially adversely affect our financial condition.

*We agreed to numerous restrictions to preserve the non-recognition treatment of the Distribution, which may reduce our strategic and operating flexibility.*

We agreed in the Tax Matters Agreement to covenants and indemnification obligations that address compliance with Section 355 of the Code. These covenants and indemnification obligations may limit our ability to pursue strategic transactions or engage in new businesses or other transactions that may maximize the value of our business and might discourage or delay a strategic transaction that our stockholders may consider favorable.

*We have limited operating history as an independent, publicly traded company, and our historical financial information is not necessarily representative of the results we would have achieved as an independent, publicly traded company and may not be a reliable indicator of our future results.*

Our historical financial information does not necessarily reflect the results of operations and financial position we would have achieved as an independent, publicly traded company during the periods prior to the spin-off, or those that we will achieve in the future. This is primarily because of the following factors:

- Prior to the spin-off, we operated as part of GHC's broader corporate organization and GHC performed various corporate functions for us, including finance, human resources, legal, information technology, general insurance, risk management and other corporate functions. Our historical financial information reflects allocations of corporate expenses from GHC for these and similar functions. These allocations may not reflect the costs we will incur for similar services in the future as an independent, publicly traded company.
- We entered into transactions with GHC that did not exist prior to the spin-off, such as GHC's provision of transition services, which caused and may continue to cause us to incur new costs.
- Our historical financial information does not reflect all changes that we expect to experience in the future as a result of our separation from GHC, including changes in our cost structure, personnel needs, tax structure, financing and business operations. As part of GHC, we enjoyed certain benefits from GHC's operating diversity, size, purchasing power, borrowing leverage and available capital for investments, and we have lost those benefits after the spin-off. As an independent entity, we may be unable to purchase goods, services and technologies, such as insurance and health care benefits and computer software licenses, or access capital markets on terms as favorable to us as those we obtained as part of GHC prior to the spin-off.

Following the spin-off, we are responsible for the additional costs associated with being an independent, publicly traded company, including costs related to corporate governance, investor and public relations and public reporting. For example, we are now required to comply with Section 404 of the Sarbanes-Oxley Act of 2002, which requires annual management assessments of the

effectiveness of our internal controls over financial reporting and a report by our independent registered public accounting firm as to whether we maintained, in all material respects, effective internal controls over financial reporting as of the last day of the year. Any failure to achieve and maintain effective internal controls could have a material adverse effect on our financial condition, results of operations or cash flows.

Table of Contents

***We may have been able to receive better terms from unaffiliated third parties than the terms we received in our agreements with GHC.***

We have entered into agreements with GHC related to our separation from GHC, including the Separation and Distribution Agreement, Transition Services Agreement, Tax Matters Agreement and Employee Matters Agreement, while we were still part of GHC. Accordingly, these agreements may not reflect terms that would have resulted from arm's-length negotiations among unaffiliated third parties. The terms of these agreements relate to, among other things, allocations of assets, liabilities, rights, indemnifications and other obligations between GHC and us. We may have received better terms from third parties.

**Risks Relating to Our Indebtedness**

***We incurred indebtedness in connection with the spin-off, and the degree to which we are now leveraged may have a material adverse effect on our business, financial condition or results of operations and cash flows.***

In connection with the spin-off, we incurred indebtedness in an aggregate principal amount of \$550 million, of which \$450 million was distributed to GHC prior to the consummation of the spin-off. We historically relied upon GHC for working capital and other cash requirements, including in connection with our previous acquisitions. We are no longer able to rely on the earnings, assets or cash flow of GHC, and GHC will not provide funds to finance our working capital or other cash requirements. We are responsible for servicing our own debt, and obtaining and maintaining sufficient working capital and other funds to satisfy our cash requirements. Our access to and cost of debt financing may be different from our historical access to and cost of debt financing under GHC. Differences in access to and cost of debt financing may result in differences in the interest rate charged to us on financings, as well as the amount of indebtedness, types of financing structures and debt markets that may be available to us now that we are an independent, publicly traded company.

Our ability to make payments on and to refinance our indebtedness, including the debt incurred in connection with the spin-off, as well as any future debt that we may incur, will depend on our ability to generate cash in the future from operations, financings or asset sales. Our ability to generate cash is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control.

***The terms of our indebtedness restricts our current and future operations, particularly our ability to incur debt that we may need to fund initiatives in response to changes in our business, the industries in which we operate, the economy and governmental regulations.***

The terms of our indebtedness include a number of restrictive covenants that impose significant operating and financial restrictions on us and limit our ability to engage in actions that may be in our long-term best interests. These may restrict our ability to take some or all of the following actions:

- incur or guarantee additional indebtedness or sell disqualified or preferred stock;
- pay dividends on, make distributions in respect of, repurchase or redeem, capital stock;
- make investments or acquisitions;
- sell, transfer or otherwise dispose of certain assets;
- create liens;
- enter into sale/leaseback transactions;
- enter into agreements restricting the ability to pay dividends or make other intercompany transfers;
- consolidate, merge, sell or otherwise dispose of all or substantially all of our or our subsidiaries' assets;
- enter into transactions with affiliates;

Table of Contents

- prepay, repurchase or redeem certain kinds of indebtedness;
- issue or sell stock of our subsidiaries; and/or
- significantly change the nature of our business.

As a result of all of these restrictions, we may be:

- limited in how we conduct our business and pursue our strategy;
- unable to raise additional debt financing to operate during general economic or business downturns; or
- unable to compete effectively or to take advantage of new business opportunities.

A breach of any of these covenants, if applicable, could result in an event of default under the terms of our indebtedness. If an event of default occurs, the lenders would have the right to accelerate the repayment of such debt and the event of default or acceleration may result in the acceleration of the repayment of any other of our debt to which a cross-default or cross-acceleration provision applies. Furthermore, the lenders of this indebtedness may require that we pledge our assets as collateral as security for our repayment obligations. If we were unable to repay any amount of this indebtedness when due and payable, the lenders could proceed against the collateral that secures this indebtedness. In the event our creditors accelerate the repayment of our borrowings, we may not have sufficient assets to repay such indebtedness and our financial condition will be materially negatively affected.

*We have variable rate indebtedness that subjects us to interest rate risk, which could cause our debt service obligations to increase significantly.*

As of the end of 2016, we had \$95.0 million of outstanding term loans and an additional \$197.2 million of undrawn revolving credit facilities with variable rates of interest that expose us to interest rate risks. If interest rates increase, our debt service obligations on the variable rate indebtedness would increase even though the amount borrowed remains the same, and our net income and cash flows will correspondingly decrease. In addition, we will be exposed to the risk of rising interest rates to the extent that we fund our operations with short-term or variable-rate borrowings. Even if we enter into interest rate swaps in the future in order to reduce future interest rate volatility, we may not elect to maintain such interest rate swaps with respect to our variable rate indebtedness, if any, and any swaps we enter into may not fully mitigate our interest rate risk. As a result, our financial condition could be materially negatively affected.

*Our ability to incur future indebtedness, whether for general corporate purposes or for acquisitions and strategic investments, may not be available on favorable terms, or at all.*

We may need to seek additional financing for our general corporate purposes or for acquisitions and strategic investments in the future. For example, we expect to finance the acquisition of NewWave with \$650 million of senior secured loans and cash on hand. In connection with the entry into the Merger Agreement, we entered into a commitment letter on January 17, 2017, as amended and restated on February 13, 2017, with the Lenders. Pursuant to the amended and restated commitment letter, and subject to the terms and conditions set forth therein, the Lenders have committed to provide us with \$300 million of incremental five-year term "A" loans and \$350 million of incremental seven-year term "B" loans to finance the transaction.

We may be unable to obtain additional indebtedness on terms favorable to us, or at all, including because of the terms of our current indebtedness. If adequate funds are not available on acceptable terms, we may be unable to fund our future activities, which could negatively affect our business. If we raise additional funds through the issuance of equity securities, our stockholders could experience dilution of their ownership interest. If we raise additional funds by issuing debt, we may be subject to limitations on our operations due to restrictive covenants.

#### **Risks Relating to Our Common Stock and the Securities Market**

*Our stock price may fluctuate significantly, depending on many factors, some of which may be beyond our control.*

The market price of our common stock may fluctuate significantly, depending on many factors, some of which may be beyond our control, including:

-----

Table of Contents

- actual or anticipated fluctuations in our operating results due to factors related to our business;
- success or failure of our business strategies;
- our quarterly or annual earnings, or those of other companies in our industry;
- our ability to obtain financing as needed;
- announcements by us or our competitors of significant acquisitions or dispositions;
- changes in accounting standards, policies, guidance, interpretations or principles;
- the failure of securities analysts to cover, or maintain coverage of, our common stock;
- changes in earnings estimates by securities analysts or our ability to meet those estimates;
- the operating and stock price performance of other comparable companies;
- investor perception of our Company and the cable industry;
- overall market fluctuations;
- results from any material litigation or government investigation;
- changes in laws and regulations (including tax laws and regulations) affecting our business;
- changes in capital gains taxes and taxes on dividends affecting stockholders; and
- general economic conditions and other external factors.

Low trading volume for our stock, which may occur if an active trading market is not sustained, among other reasons, would amplify the effect of the above factors on our stock price volatility.

Stock markets in general have experienced volatility that has often been unrelated to the operating performance of a particular company. These broad market fluctuations could adversely affect the trading price of our common stock.

***We cannot assure you that we will continue to pay dividends on our common stock, and our indebtedness limits our ability to pay dividends on our common stock.***

The timing, declaration, amount and payment of future dividends to stockholders falls within the discretion of our Board. Our Board's decisions regarding the amount and payment of future dividends will depend on many factors, including our financial condition, earnings, capital requirements of our business and covenants associated with debt obligations, as well as legal requirements, regulatory constraints, industry practice and other factors that our Board deems relevant. There can be no assurance that we will continue to pay any dividend in the future.

***Your percentage ownership in our Company may be diluted in the future.***

Your percentage ownership in our Company may be diluted in the future because of equity awards granted, and that we expect to grant in the future, to our directors, officers and other employees. In addition, we may issue equity as all or part of the consideration paid for acquisitions and strategic investments that we may make in the future or as necessary to finance our ongoing operations.

***Certain provisions in our Amended and Restated Certificate of Incorporation and Amended and Restated By-laws and Delaware law may discourage takeovers and the concentration of ownership of our common stock will affect the voting results of matters submitted for stockholder approval.***

Several provisions of our Amended and Restated Certificate of Incorporation, Amended and Restated By-laws and Delaware law may discourage, delay or prevent a merger or acquisition that is opposed by our Board or certain stockholders holding a significant percentage of the voting power of our outstanding voting stock. These include provisions that:



Table of Contents

- divide our Board into three classes of directors, standing for election on a staggered basis, such that only approximately one-third of the directors constituting our Board may change each year;
- do not permit our stockholders to act by written consent and require that stockholder action must take place at an annual or special meeting of our stockholders;
- provide that only our Chief Executive Officer and a majority of our directors, and not our stockholders, may call a special meeting of our stockholders;
- require the approval of our Board or the affirmative vote of stockholders holding at least 66 <sup>2</sup>/<sub>3</sub>% of the voting power of our capital stock to amend our Amended and Restated By-laws; and
- limit our ability to enter into business combination transactions with certain stockholders.

These and other provisions of our Amended and Restated Certificate of Incorporation, Amended and Restated By-laws and Delaware law may discourage, delay or prevent certain types of transactions involving an actual or a threatened acquisition or change in control of our Company, including unsolicited takeover attempts, even though the transaction may offer our stockholders the opportunity to sell their shares of our common stock at a price above the prevailing market price.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

Not applicable.

**ITEM 2. PROPERTIES**

Our headquarters, which we purchased in 2012, and other corporate offices are located in Phoenix, Arizona. Our call-center operations are housed at our headquarters. The majority of the offices and headend facilities of our individual cable systems are located in buildings owned by us. Most of the tower sites used by us are leased.

**ITEM 3. LEGAL PROCEEDINGS**

In the ordinary course of business, we periodically receive claims from third parties alleging that our network and information technology infrastructure infringes the intellectual property rights of others. We are generally named as joint defendants in these suits together with other providers of data, video and voice services. Typically these claims allege that aspects of our cable system architecture, electronic program guides, cable modem technology and VoIP services infringe on process patents held by third parties. In addition, we have been subject to various civil lawsuits in the ordinary course of business, including contract disputes, actions alleging negligence, invasion of privacy, violations of applicable wage and hour laws and statutory and common law claims involving various other matters. We do not view any of these proceedings as material to our business, and are currently not subject to any other material legal proceedings.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

Table of Contents**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES****Market Information**

Our common stock began trading on the New York Stock Exchange under the ticker symbol "CABO" on July 1, 2015 after completion of the spin-off. Prior to that date, there was no public market for our common stock. The following table sets forth the high and low sales prices for our common stock for the quarterly periods indicated as reported by the New York Stock Exchange.

	2016		2015	
	High	Low	High	Low
First Quarter	\$ 459.40	\$ 390.00	\$ -	\$ -
Second Quarter	\$ 518.31	\$ 430.21	\$ -	\$ -
Third Quarter	\$ 589.76	\$ 506.43	\$ 450.48	\$ 365.00
Fourth Quarter	\$ 635.85	\$ 559.83	\$ 492.81	\$ 413.64

**Holdings**

As of February 21, 2017, there were approximately 458 holders of record of our common stock and 5,719,502 shares of our common stock outstanding.

**Dividends**

The following table sets forth the dividends declared on our common stock for the quarterly periods indicated.

	2016	2015
First Quarter	\$ 1.50	\$ -
Second Quarter	\$ 1.50	\$ -
Third Quarter	\$ 1.50	\$ -
Fourth Quarter	\$ 1.50	\$ 1.50
Total	\$ 6.00	\$ 1.50

We expect to continue to pay quarterly dividends, although the timing, declaration, amount and payment of future dividends to stockholders falls within the discretion of our Board.

**Securities Authorized for Issuance Under Equity Compensation Plans**

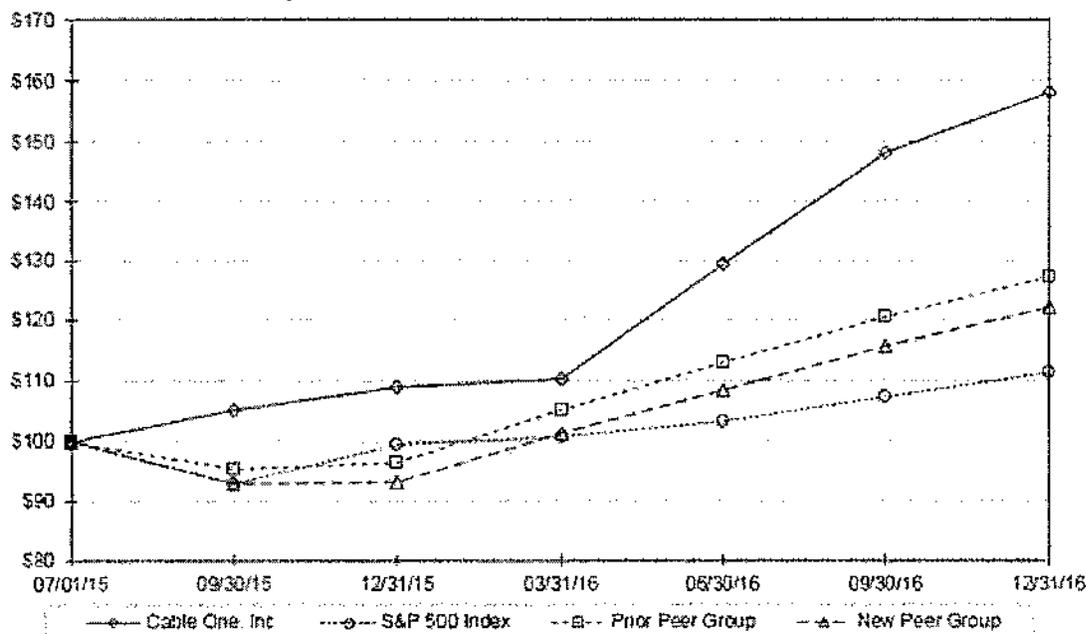
For equity compensation plan information, refer to Item 12 in Part III of this Annual Report on Form 10-K.

Table of Contents

**Performance Graph**

The following graph compares the cumulative total stockholder return of our common stock between July 1, 2015 (the date our stock began trading on the New York Stock Exchange) and December 31, 2016 with the cumulative total returns of the Standard & Poor's 500 Stock Index, a new custom peer group index (the "New Peer Group"), which was created because of merger and acquisition activity that impacted our prior peer group index, and our prior peer group index (the "Prior Peer Group"). For purposes of this graph, it assumes a hypothetical \$100 investment on July 1, 2015 and that dividends, if any, were reinvested. The New Peer Group of data, video and voice services companies includes Charter Communications, Inc.; Comcast Corporation; General Communication, Inc.; and our Company. The Prior Peer Group of data, video and voice services companies includes Cablevision Systems Corp.; Charter Communications, Inc.; Comcast Corporation; Time Warner Cable Inc.; and our Company.

**Comparison of 18 Month Cumulative Total Return**



	07/01/15	09/30/15	12/31/15	03/31/16	06/30/16	09/30/16	12/31/16
Cable One, Inc.	100.00	105.12	109.03	110.32	129.46	148.25	158.24
S&P 500 Index	100.00	92.89	99.44	100.78	103.25	107.23	111.33
Prior Peer Group	100.00	95.45	96.36	105.14	112.97	120.66	127.29
New Peer Group	100.00	92.87	93.14	101.32	108.36	116.69	122.13

Source : SHL Financial, an offering of S&P Global Market Intelligence  
© 2017

The stock price performance shown on this graph is based on historical results and is not necessarily indicative of future stock price performance. The graph is furnished solely to accompany this Annual Report on Form 10-K and is not being filed for purposes of Section 18 of the Exchange Act or otherwise subject to the liabilities under that section, and shall not be deemed to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Exchange Act.

Table of Contents**Purchases of Equity Securities by the Issuer**

The following table sets forth certain information relating to the purchases of our common stock by us and any affiliated purchasers within the meaning of Rule 10b-18(a)(3) under the Exchange Act during the three months ended December 31, 2016 (dollars in thousands, except per share data):

Period	Total # of Shares Purchased	Average Price Paid Per Share	Total # of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>(1)</sup>	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
October 1 to 31, 2016	-	\$ -	-	\$ 177,493
November 1 to 30, 2016	401	\$ 570.00	401	\$ 177,264
December 1 to 31, 2016 <sup>(2)</sup>	3,616	\$ 605.86	-	\$ 177,264
<b>Total</b>	<u>4,017</u>	<u>\$ 602.28</u>	<u>401</u>	

(1) On July 1, 2015, the Board authorized up to \$250 million of share repurchases (subject to a total cap of 600,000 shares of Company common stock), which was announced on August 7, 2015. Purchases under the stock repurchase program may be made from time to time on the open market and in privately negotiated transactions. The size and timing of these purchases will be based on a number of factors, including price and business market conditions.

(2) Represents shares withheld from employees to satisfy estimated tax withholding obligations in connection with the vesting of restricted shares under the Cable One, Inc. 2015 Omnibus Incentive Compensation Plan. The average price paid per share for the common stock withheld was based on the closing price of our common stock on the applicable vesting date.

**ITEM 6. SELECTED FINANCIAL DATA**

The following table presents selected historical financial information. The selected historical financial information as of December 31, 2016, 2015, 2014, 2013 and 2012, and for each of the fiscal years in the five-year period ended December 31, 2016, are derived from our historical audited Consolidated Financial Statements included elsewhere in this Annual Report on Form 10-K or in our registration statement on Form 10.

The selected historical financial data presented below should be read in conjunction with our audited Consolidated Financial Statements and the accompanying notes thereto, and "Management's Discussion and Analysis of Financial Condition and Results of Operations," included elsewhere in this Annual Report on Form 10-K. For each of the periods presented, except for the period from July 1, 2015 through December 31, 2016, we were a separate wholly owned subsidiary of GHC. The financial information included herein may not necessarily reflect our financial position, results of operations and cash flows in the future or what our financial position, results of operations and cash flows would have been had we been an independent, publicly traded company during the periods presented. The historical financial information includes allocations of certain GHC corporate expenses. We believe the assumptions and methodologies underlying the allocation of these expenses were reasonable. However, such expenses may not be indicative of the actual level of expense that we would have incurred if we had operated as an independent, publicly traded company or of the costs expected to be incurred in the future.

Table of Contents

	Year Ended December 31,				
	2016	2015	2014	2013	2012
<b>Statement of Operations Information</b>					
<b>(in thousands, except per share data)</b>					
Revenues	\$ 819,625	\$ 807,266	\$ 814,812	\$ 825,707	\$ 804,992
Net income	\$ 98,939	\$ 89,033	\$ 147,309	\$ 104,511	\$ 93,911
Net income per common share:					
Basic	\$ 17.23	\$ 15.21	\$ 25.21	\$ 17.89	\$ 16.07
Diluted	\$ 17.14	\$ 15.19	\$ 25.21	\$ 17.89	\$ 16.07
Cash dividends declared per share	\$ 6.00	\$ 1.50	\$ -	\$ -	\$ -
<b>Balance Sheet Information</b>					
<b>(in thousands)</b>					
Cash and cash equivalents	\$ 138,040	\$ 119,199	\$ 6,410	\$ 6,238	\$ 7,300
Total assets	\$ 1,397,271	\$ 1,398,805	\$ 1,262,040	\$ 1,248,344	\$ 1,216,827
Total debt, including capital lease obligations and excluding debt issuance costs	\$ 545,284	\$ 549,051	\$ -	\$ -	\$ -
Total liabilities	\$ 942,760	\$ 963,459	\$ 408,752	\$ 413,085	\$ 391,651
Total stockholders' equity	\$ 454,511	\$ 435,346	\$ 853,288	\$ 835,259	\$ 825,176

## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### Forward-Looking Statements

You should read the following discussion of our financial condition and results of operations in conjunction with our accompanying audited Consolidated Financial Statements and related notes included in this Annual Report on Form 10-K, as well as the discussion in the section of this Annual Report on Form 10-K entitled "Business." This discussion contains forward-looking statements that involve risks and uncertainties. These statements can be identified by the fact that they do not relate strictly to historical or current facts, but rather are based on current expectations, estimates, assumptions and projections about the cable industry and our business and financial results. Forward-looking statements often include words such as "anticipates," "estimates," "expects," "projects," "intends," "plans," "believes" and words and terms of similar substance in connection with discussions of future operating or financial performance. Accordingly, undue reliance should not be placed on any forward-looking statement made by us or on our behalf. Our actual results may vary materially from those expressed or implied by these forward-looking statements due to a number of factors, including those discussed in the sections of this Annual Report on Form 10-K entitled "Risk Factors" and "Cautionary Statement Concerning Forward-Looking Statements."

### Overview

#### *Spin-Off*

On July 1, 2015, Cable One became an independent company traded under the ticker symbol "CABO" on the New York Stock Exchange. The spin-off was effected through the distribution by GHC of 100% of the outstanding shares of common stock of Cable One to GHC stockholders as of the record date for the distribution in a pro rata dividend. In connection with the spin-off, approximately 5.84 million shares of Cable One's common stock were issued and outstanding on July 1, 2015, based on approximately 0.96 million shares of GHC Class A Common Stock and 4.88 million shares of GHC Class B Common Stock outstanding as of June 30, 2015. No preferred stock was issued or outstanding.

#### *Our Business*

We are a fully integrated provider of data, video and voice services in 19 Western, Midwestern and Southern states. We provide these broadband services to residential and business customers in more than 35 cable systems covering over 400 cities and towns. The markets we serve are primarily non-metropolitan, secondary markets, with 76% of our customers located in five states: Arizona, Idaho, Mississippi, Oklahoma and Texas. Our biggest customer concentrations are in the Mississippi Gulf Coast region and in the

greater Boise, Idaho region. We are the seventh-largest cable system operator in the United States based on customers and revenues in 2016, making services available to approximately 1.7 million homes in the United States as of December 31, 2016.

Table of Contents

As of December 31, 2016, we provided service to 657,222 residential and business customers out of approximately 1.7 million homes passed. Of these customers, 513,908 subscribed to data services, 320,246 subscribed to video services and 115,811 to voice services.

We generate revenues through five primary products. Ranked by share of our total revenues in 2016, they are residential data (42.0%), residential video (36.0%), business services (data, voice and video – 12.2%), residential voice (5.2%) and advertising sales (3.4%). The profit margins, growth rates and capital intensity of our five primary products vary significantly due to competition, product maturity and relative costs. In 2016, our Adjusted EBITDA margins for residential data and business services were approximately four and five times greater, respectively, than for residential video. We define Adjusted EBITDA margin for a product line as Adjusted EBITDA attributable to that product line divided by revenue attributable to that product line (see “Use of Adjusted EBITDA” below for the definition of Adjusted EBITDA and a reconciliation of Adjusted EBITDA to net income, which is the most directly comparable GAAP measure). This margin disparity is largely the result of significant programming costs and retransmission fees incurred to deliver residential video services, which in each of the last three years represented between 50% and 60% of total residential video revenues (in addition to the other material direct and indirect costs associated with residential video). None of our other product lines has direct costs representing as substantial a portion of revenues as programming costs and retransmission fees represent for residential video, and indirect costs are allocated equally on a per PSU basis. Programming costs and retransmission fees have a meaningfully lower impact on business services margins than residential video because business services include data, voice and video, diminishing the relative impact of programming costs and retransmission fees on that product line as a whole.

Prior to 2012, we were focused on growing revenues through subscriber retention and growth in overall PSUs. To that end, our strategies consisted of, among others, offering promotional discounts to new and existing subscribers adding new services and to subscribers purchasing more than one service offering.

Since 2012, we have adapted our strategy to face the trend, which has affected the entire cable industry, of declining profitability of residential video and declining revenues from residential voice services. We believe the declining profitability of residential video services is primarily due to competition from other content providers and increasing programming costs and retransmission fees, and the declining revenues from residential voice services is primarily due to the increasing use of wireless voice services in addition to, or instead of, landline voice service. Beginning in 2013, we shifted our focus away from maximizing customer PSUs and towards growing and maintaining our higher margin businesses, namely residential data and business services. Separately, we have also focused on retaining customers with a high expected LTV, who are less attracted by discounting, require less support and churn less. This strategy focuses on increasing Adjusted EBITDA, Adjusted EBITDA less capital expenditures and margins.

The trends described above have impacted our four largest product lines in the following ways:

- *Residential data.* We experienced growth in the number of and revenues from our residential data customers every year since 2013. We expect this growth to continue due to projected increases in the number of potential customers for us to serve, as there are still a number of households in our markets that do not subscribe to data services from any provider. We expect to capture a portion of these customers and anticipate capturing additional market share from existing data subscribers due to our recent upgrades in broadband capacity and our ability to offer higher access speeds than many of our competitors.
- *Residential video.* Residential video service is a competitive and highly-penetrated business. As we focus on the higher-margin businesses of residential data and business services, we are de-emphasizing our residential video business and, as a result, expect residential video revenues to continue to decline in the future.
- *Residential voice.* We have experienced declines in residential voice customers as a result of homes in the United States deciding to terminate their landline voice service and exclusively use wireless voice service. We believe this trend will continue because of competition from wireless voice service. Revenues from residential voice customers have declined over recent years, and we expect this decline will continue.
- *Business services.* We have experienced significant growth in business data and voice customers and revenues and expect this to continue. We attribute this growth to our strategic focus shift on increasing sales to business customers. More recently, we have expanded our efforts to attract enterprise business customers. Margins in products sold to business customers have remained attractive, and we expect this trend to continue.

Table of Contents

We continue to experience increased competition, particularly from telephone companies, cable overbuilders, OTT video providers and DBS television providers. Because of the levels of competition we face, we believe it is important to make investments in our infrastructure. We made elevated levels of capital investments between 2012 and 2015 to increase our cable plant capacities and reliability, launch all-digital video services, which has freed up approximately three-fourths of average plant bandwidth for data services, and increase data capacity by moving from four-channel bonding to 32-channel bonding. We expect to continue devoting financial resources to infrastructure improvements because we believe these investments are necessary to remain competitive.

The spin-off provided us the opportunity to further tailor our strategies to achieve greater operational focus and drive our return on investment. Our goals are to continue to grow residential data and business services and to maintain profit margins to deliver strong Adjusted EBITDA. To achieve these goals, we intend to continue our industrial engineering-driven cost management, remain focused on customers with high LTV and follow through with further planned investments in broadband plant upgrades and new data services offerings for residential and business services customers.

Our business is subject to extensive governmental regulation. Such regulation has led to increases in our operational and administrative expenses. In addition, we could be significantly impacted by changes to the existing regulatory framework, whether triggered by legislative, administrative or judicial rulings. In 2015, the FCC used its Title II authority to regulate broadband Internet access services in the Order. According to the Order, under this regime, the FCC will forbear from systematic rate regulation of Internet access service at the subscriber level, which we believe will permit us to continue to manage data usage efficiently by establishing appropriate rates. However, the Order also imposes on all providers of broadband Internet access service, including us, obligations that limit the ways we can manage certain types of traffic. In June 2016, the U.S. Court of Appeals for the D.C. Circuit upheld the Order in its entirety. A petition for an *en banc* rehearing of the June 2016 decision upholding the Order is currently pending in the U.S. Court of Appeals for the D.C. Circuit. In addition, the change in administration and the newly-constituted FCC may take steps to revise the Order and the resulting rules. We cannot predict whether or not future changes to the regulatory framework that are inconsistent with the Order will occur, whether the petition for an *en banc* rehearing will be granted, or whether the decision of the U.S. Court of Appeals for the D.C. Circuit will be appealed, and if any such rehearing or appeal would be successful. See "*Risk Factors—Risks Relating to Regulation and Legislation—The profitability of our data services offerings may be impacted by legislative or regulatory efforts to impose "net-neutrality" and other new requirements on cable operators.*"

**Results of Operations*****Basis of Presentation***

The accompanying Consolidated Financial Statements have been prepared in accordance with GAAP in the United States and the rules and regulations of the SEC. They reflect the historical Consolidated Statements of Operations and Comprehensive Income, Consolidated Balance Sheets, Consolidated Statements of Stockholders' Equity and Consolidated Statements of Cash Flows of the Company for the years presented.

Prior to the spin-off, the accompanying Consolidated Financial Statements were derived from the consolidated financial statements and accounting records of GHC. These Consolidated Financial Statements were prepared solely to present the Company's historical results of operations, financial position and cash flows for the periods prior to the spin-off as it was historically managed. The impact of transactions between the Company and GHC was included in these Consolidated Financial Statements and was considered to be effectively settled for cash in the Consolidated Financial Statements at the time the transaction was recorded. The total net effect of the settlement of these intercompany transactions was reflected in the Consolidated Statements of Cash Flows as a financing activity and in the Consolidated Balance Sheets as Additional GHC investment (deficit).

Prior to the spin-off, we functioned as part of the larger group of companies controlled by GHC, and, accordingly, GHC provided certain support and overhead functions to us. These functions included finance, human resources, legal, information technology, general insurance, risk management and other corporate functions. The costs of such services were allocated to us based on the most relevant allocation methods to the service provided. Management believed such allocations were reasonable and were consistently applied; however, they may not be indicative of the actual expense that would have been incurred had we been operating on a stand-alone basis. See Notes 12 and 16 of the Notes to our Consolidated Financial Statements for details on these allocations.

Table of Contents

Prior to the spin-off, we participated in a centralized approach to cash management and in financing its operations managed by GHC. Cash was transferred to GHC and GHC funded our operating and investing activities as needed. Accordingly, cash and cash equivalents at the GHC level were not allocated to us in the Consolidated Financial Statements included elsewhere in this Annual Report on Form 10-K. Cash transfers to and from GHC's cash management accounts are included within net transfers to GHC in the Consolidated Statements of Stockholders' Equity. GHC third-party debt and the related interest expense were not allocated to us for any of the periods presented as we were not the legal obligor on the debt, and GHC borrowings were not directly attributable to our business.

Prior to the spin-off, certain of our eligible employees participated in the pension, post-retirement and deferred compensation plans of GHC. Although we are a stand-alone, independent entity after the spin-off, these employees remain entitled to the benefits under these plans accrued prior to the spin-off, but no longer accrue additional benefits under these plans. In addition, the liabilities in respect of the accrued benefits of certain of our employees under these plans remain at GHC (to the extent such liabilities were not already held by us at the time of the spin-off). Therefore, the allocation of related expenses to us in respect of these employees has not been reflected in our financial statements in the periods following the spin-off. Allocations were equal to \$2.0 million and \$3.6 million for the years ended December 31, 2015 and 2014, respectively. However, deferred compensation and unfunded Supplemental Executive Retirement Plan benefits for a number of our executives were assumed by us following the spin-off, and have been reflected in our financial statements for post spin-off periods.

The obligation for U.S. Federal and certain state income taxes attributable to the tax period prior to the spin-off were retained by us, along with related deferred tax assets and liabilities. With respect to general insurance and workers' compensation liabilities, we assumed financial responsibility.

Also, in connection with the spin-off, on June 29, 2015, we distributed \$450 million to GHC, which was funded by our senior unsecured notes. See "*Financial Condition: Liquidity and Capital Resources—Financing Activity*" for more information on our capitalization activities.

Our results of operations for the years ended December 31, 2016 and 2015 may not be indicative of our future results. In addition, as we did not operate as a stand-alone entity prior to July 1, 2015, the financial information included in this Annual Report on Form 10-K may not necessarily be indicative of our future performance and may not necessarily reflect what our financial position, results of operations or cash flows would have been had we operated as a stand-alone entity during all of the periods presented.

***PSUs and Customer Counts and PSUs by Primary Products***

During 2016, we had a reduction of 48,544 residential PSUs, representing a 5.3% decline. Including business customers, we had a reduction of 42,520 PSUs, representing a 4.3% decline, and a reduction of 7,382 total customer relationships, representing a 1.1% decline, for the year ended December 31, 2016. The declines in residential PSUs and total customer relationships were primarily the result of residential video and residential voice customer losses due to our shift in focus, as described above.

During 2015, we had a reduction of 95,260 residential PSUs, representing a 9.4% decline. Including business customers, we had a reduction of 96,699 PSUs, representing an 8.9% decline, and a reduction of 22,067 total customer relationships, representing a 3.2% decline, for the year ended December 31, 2015. The decline in business voice customers in 2015 was primarily attributable to converting data into our new billing system, which counts each business customer relationship at a unique business address as a single customer, whereas our prior billing system calculated multiple relationships based on revenue generated at an address.

Table of Contents

The following tables provides an overview of selected customer data for our cable systems for the time periods specified:

Customer Counts and PSUs	As of December 31,		
	2016	2015	2014
Residential data customers <sup>(1)</sup>	469,053	460,977	449,839
Residential video customers <sup>(2)</sup>	306,563	349,879	436,370
Residential voice customers <sup>(3)</sup>	97,724	111,028	130,935
Total residential <sup>(4)</sup>	873,340	921,884	1,017,144
Business data customers <sup>(5)</sup>	44,855	40,264	38,615
Business video customers <sup>(6)</sup>	13,683	14,271	14,847
Business voice customers <sup>(7)(8)</sup>	18,087	16,066	18,578
Total business <sup>(8)(9)</sup>	76,625	70,601	72,040
Total PSUs	949,965	992,485	1,089,184
Total residential customer relationships	605,699	617,220	643,938
Total business customer relationships	51,523	47,384	42,733
Total customer relationships	657,222	664,604	686,671

Annual Net Gain/(Loss)	Year Ended December 31,		% Change	
	2016	2015	2016	2015
Residential data customers <sup>(1)</sup>	8,076	11,138	1.8	2.5
Residential video customers <sup>(2)</sup>	(43,316)	(86,491)	(12.4)	(19.8)
Residential voice customers <sup>(3)</sup>	(13,304)	(19,907)	(12.0)	(15.2)
Total residential <sup>(4)</sup>	(48,544)	(95,260)	(5.3)	(9.4)
Business data customers <sup>(5)</sup>	4,591	1,649	11.4	4.3
Business video customers <sup>(6)</sup>	(588)	(576)	(4.1)	(3.9)
Business voice customers <sup>(7)(8)</sup>	2,021	(2,512)	12.6	(13.5)
Total business <sup>(8)(9)</sup>	6,024	(1,439)	8.5	(2.0)
Total PSUs	(42,520)	(96,699)	(4.3)	(8.9)
Total residential customer relationships	(11,521)	(26,718)	(1.9)	(4.1)
Total business customer relationships	4,139	4,651	8.7	10.9
Total customer relationships	(7,382)	(22,067)	(1.1)	(3.2)

- (1) Residential data customers include all residential customers who subscribe to our data service.
- (2) Residential video customers include all basic residential customers who receive video services and may have one or more digital set-top boxes or cable cards deployed. Residential bulk multi-dwelling accounts are included in our video customers.
- (3) Residential voice customers include all residential customers who subscribe to our voice service. Residential customers who take multiple voice lines are only counted once in the total.
- (4) Total residential PSUs represents the sum of residential data, residential video and residential voice customers, not counting additional outlets within one household.
- (5) Business data customers include commercial accounts that receive data service via a cable modem and commercial accounts that receive broadband service optically, via fiber connections.
- (6) Business video customers include commercial accounts.
- (7) Business voice customers include commercial accounts that subscribe to our voice service.
- (8) The decrease in business voice customers and total business PSUs for the year ended December 31, 2015 was primarily attributable to converting data into our new billing system, which counts each business customer relationship at a unique business address as a single customer; whereas our prior billing system calculated multiple relationships based on revenue generated at an address.
- (9) Total business PSUs represent the sum of business data, business video and business voice customer.

In recent years, our customer mix has shifted, causing subscribers to move from triple-play packages to single and double-play. This is because some residential video customers have defected to DBS services and OTT offerings in lieu of video and more households have discontinued landline voice service. In addition, we have focused on selling data-only packages to new customers rather than on cross-selling video to these customers.

.....

Table of Contents**2016 Compared to 2015***Revenues*

Revenues increased \$12.4 million, or 1.5%, due primarily to increases in residential data and business services revenues of \$49.7 million and \$11.6 million, respectively, partially offset by decreases in residential video and residential voice revenues of \$37.9 million and \$7.2 million, respectively. The declines in residential video and residential voice revenues were primarily attributable to residential video customer losses of 12.4% and residential voice customer losses of 12.0% during 2016.

Revenues by service offering were as follows for 2016 and 2015, together with the percentages of revenues that each item represented for the years presented (dollars in thousands):

	Year Ended December 31,					
	2016		2015		2016 vs. 2015	
	Revenues	% of Revenues	Revenues	% of Revenues	\$ Change	% Change
Residential data	\$ 344,184	42.0	\$ 294,486	36.5	\$ 49,698	16.9
Residential video	294,781	36.0	332,716	41.2	(37,935)	(11.4)
Residential voice	42,949	5.2	50,148	6.2	(7,199)	(14.4)
Business services	100,311	12.2	88,741	11.0	11,570	13.0
Advertising sales	27,496	3.4	31,034	3.8	(3,538)	(11.4)
Other	9,904	1.2	10,141	1.3	(237)	(2.3)
Total revenues	\$ 819,625	100.0	\$ 807,266	100.0	\$ 12,359	1.5

Average monthly revenue per unit for the indicated service offerings were as follows for 2016 and 2015:

	Year Ended December 31,					
	2016		2015		2016 vs. 2015	
	\$	%	\$	%	\$ Change	% Change
Residential data <sup>(1)</sup>	\$ 61.68	53.89	\$ 53.89	53.89	\$ 7.79	14.5
Residential video <sup>(1)</sup>	74.84	70.53	70.53	70.53	4.31	6.1
Residential voice <sup>(1)</sup>	34.29	34.54	34.54	34.54	(0.25)	(0.7)
Business services <sup>(2)</sup>	169.03	164.12	164.12	164.12	4.91	3.0
Total customers <sup>(2)</sup>	103.35	99.57	99.57	99.57	3.78	3.8

<sup>(1)</sup> Average monthly per unit values represent the applicable residential service revenues divided by the corresponding average number of customers at the beginning and end of each period.

<sup>(2)</sup> Average monthly per unit values represent the applicable business services or total revenues divided by the corresponding average number of customer relationships at the beginning and end of each period.

Residential data service revenues increased \$49.7 million, or 16.9%, due primarily to a rate adjustment taken in the fourth quarter of 2015, an increase in residential data customers of 1.8%, a reduction in package discounting and increased subscriptions to premium tiers by residential customers.

Residential video service revenues declined \$37.9 million, or 11.4%, due primarily to residential video customer losses of 12.4%, partially offset by a broadcast television surcharge imposed in the second quarter of 2016.

Residential voice service revenues decreased \$7.2 million, or 14.4%, due primarily to a decline in residential voice customers of 12.0% as more residential customers have discontinued landline voice service.

Business services revenues increased \$11.6 million, or 13.0%, due primarily to growth in our business data and voice services to both small and medium-sized businesses and enterprise customers. Total business customer relationships increased 8.7% in 2016. Overall, business services represented 12.2% for 2016, compared to 11.0% of our total revenues for 2015.

Advertising sales revenues declined \$3.5 million, or 11.4%, due primarily to the negative impact of decreased video customers on the number of viewers available to be reached by advertising spots.



Table of Contents

Other revenues decreased \$0.2 million, or 2.3%, due primarily to a decrease in late charges and installation fees, partially offset by an increase in reconnect fees.

*Operating Costs and Expenses*

Operating expenses (excluding depreciation and amortization) declined \$6.5 million, or 2.1%, due primarily to a 12.4% reduction in residential video customers, which significantly reduced programming costs. In total, programming costs declined \$9.9 million and non-programming operating expenses increased \$3.4 million. The increase in non-programming operating expenses was primarily attributable to increases in backbone and Internet connectivity fees of \$1.9 million; group insurance of \$1.2 million; loss on disposal of property, plant and equipment of \$1.1 million; and increased software maintenance costs of \$0.7 million, partially offset by a decrease in franchise fees of \$1.5 million due to the decrease in video revenues subject to franchise fees. Operating expenses (excluding depreciation and amortization) as a percentage of revenues were 37.1% and 38.5% for 2016 and 2015, respectively.

Selling, general and administrative expenses declined \$9.2 million, or 4.7%, due primarily to decreases in processing costs for customer billing following the completion of our billing system conversion of \$11.4 million; salaries, wages and benefits costs of \$7.3 million due to decreased headcount and lower group insurance costs; general and workers' compensation insurance expense of \$2.9 million; property taxes of \$1.5 million and software maintenance of \$1.1 million. The decrease was partially offset by increases in incentive compensation expense of \$4.8 million; acquisition-related costs of \$4.7 million; advertising and marketing expense of \$3.2 million and professional services expense of \$2.2 million. Selling, general and administrative expenses as a percentage of revenues were 22.5% and 24.0% for 2016 and 2015, respectively.

Depreciation and amortization increased \$1.5 million, or 1.1%, due primarily to new assets placed in service in 2016 and 2015, partially offset by assets that became fully depreciated during those years.

*Interest Expense*

Interest expense was \$30.2 million and \$16.1 million for 2016 and 2015, respectively. The increase was due to the issuance of our long-term debt in June 2015 in conjunction with the spin-off.

*Other Income (Expense)*

Other income (expense) increased \$5.4 million due primarily to a \$4.1 million net gain on the sale of a cable system and higher interest income.

*Provision for Income Taxes*

Provision for income taxes increased \$7.8 million, or 13.8%, due primarily to an increase in taxable income of \$17.7 million, or 12.2%. Our effective tax rate was 39.3% and 38.8% for 2016 and 2015, respectively.

*Net Income*

As a result of the factors described above, our net income was \$98.9 million for 2016, compared to \$89.0 million for 2015.

**2015 Compared to 2014***Revenues*

Revenues declined \$7.5 million, or 0.9%, due primarily to declines in residential video and residential voice revenues of \$29.0 million and \$12.2 million, respectively, partially offset by increases in residential data and business services revenues of \$28.8 million and \$11.9 million, respectively. The declines in residential video and residential voice revenues were primarily attributable to residential video customer losses of 19.8% and residential voice customer losses of 15.2%.

Table of Contents

Revenues by service offering were as follows for the years ended December 31, 2015 and 2014, together with the percentages of revenues that each item represented for the years presented (dollars in thousands):

	Year Ended December 31,					
	2015		2014		2015 vs. 2014	
	Revenues	% of Revenues	Revenues	% of Revenues	\$ Change	% Change
Residential data	\$ 294,486	36.5	\$ 265,718	32.6	\$ 28,768	10.8
Residential video	332,716	41.2	361,668	44.4	(28,952)	(8.0)
Residential voice	50,148	6.2	62,396	7.7	(12,248)	(19.6)
Business services	88,741	11.0	76,829	9.4	11,912	15.5
Advertising sales	31,034	3.8	35,362	4.3	(4,328)	(12.2)
Other	10,141	1.3	12,839	1.6	(2,698)	(21.0)
Total revenues	<u>\$ 807,266</u>	<u>100.0</u>	<u>\$ 814,812</u>	<u>100.0</u>	<u>\$ (7,546)</u>	<u>(0.9)</u>

Average monthly revenue per unit for the indicated service offerings were as follows for 2015 and 2014:

	Year Ended December 31,		2015 vs. 2014	
	2015	2014	\$ Change	% Change
Residential data <sup>(1)</sup>	\$ 53.89	\$ 49.82	\$ 4.07	8.2
Residential video <sup>(1)</sup>	70.53	62.70	7.83	12.5
Residential voice <sup>(1)</sup>	34.54	36.46	(1.92)	(5.3)
Business services <sup>(2)</sup>	164.12	154.32	9.80	6.4
Total customers <sup>(2)</sup>	99.57	97.03	2.54	2.6

<sup>(1)</sup> Average monthly per unit values represent the applicable residential service revenues divided by the corresponding average number of customers at the beginning and end of each period. Certain residential data, video and voice service revenues used in the calculation of average monthly revenue per unit for 2015 and 2014 have been reclassified to conform to the 2016 presentation.

<sup>(2)</sup> Average monthly per unit values represent the applicable business services or total revenues divided by the corresponding average number of customer relationships at the beginning and end of each period.

Residential data service revenues rose \$28.8 million, or 10.8%, due primarily to an increase in residential data customers of 2.5%, a reduction in price discounting, a rate adjustment in the fourth quarter of 2015 and increased subscriptions to premium tiers by residential customers.

Residential video service revenues declined \$29.0 million, or 8.0%, due primarily to residential video customer losses of 19.8% and digital customers purchasing fewer digital tiers of service, partially offset by video rate adjustments and a reduction in promotional discounts.

Residential voice service revenues declined \$12.2 million, or 19.6%, due primarily to a decline in residential voice customers of 15.2% as more residential customers have discontinued landline voice service.

Business services revenues rose \$11.9 million, or 15.5%, due to growth in our business data and voice services to small and medium-sized businesses. Total business customer relationships increased 10.9%. The decline in business voice customers and total business PSUs was primarily attributable to converting data into our new billing system in 2015, which counts each business customer relationship at a unique business address as a single customer, whereas our prior billing system calculated multiple relationships based on revenue generated at an address. Overall, business services comprised 11.0% of our total revenues for 2015, compared to 9.4% of our total revenues for 2014.

Advertising sales revenues declined \$4.3 million, or 12.2%, due primarily to the negative impact of decreased video customers on the number of viewers available to be reached by advertising spots.

Other revenues declined \$2.7 million, or 21.0%, due primarily to the impact of decreased number of residential video and residential voice customers on installation, reconnects and late charges.



Table of Contents*Operating Costs and Expenses*

Operating expenses (excluding depreciation and amortization) declined \$17.0 million, or 5.2%, due primarily to a 19.8% reduction in residential video customers, which significantly reduced programming costs. Also, effective April 1, 2014, we elected not to renew our contract for certain networks. In total, programming costs declined 8.5%. Operating expenses were also down from lower voice service expense, partially offset by modest increases in technical, Internet and information technology expenses. Operating expenses (excluding depreciation and amortization) as a percentage of revenues were 38.5% and 40.3% for 2015 and 2014, respectively.

Selling, general and administrative costs increased \$5.1 million, or 2.7%, due primarily to an aggregate increase of \$6.5 million in group insurance, development of internal use software (primarily our new billing system), repairs and maintenance and salaries and wages, partially offset by an aggregate decrease of \$1.6 million in GHC overhead and pension costs due to the spin-off. Selling, general and administrative expenses as a percentage of revenues were 24.0% and 23.2% for 2015 and 2014, respectively.

Depreciation and amortization increased \$6.5 million, or 4.8%, due primarily to new assets placed in service in 2015 and 2014, partially offset by assets that became fully depreciated during those years.

*Interest Expense*

Interest expense was \$16.1 million, attributable to our long-term debt incurred in connection with the spin-off. No interest expense was incurred in 2014.

*Other Income (Expense)*

Other income (expense) in 2014 consisted primarily of a \$75.2 million gain associated our sale of certain wireless spectrum licenses during the year.

*Provision for Income Taxes*

Provision for income taxes decreased \$34.3 million, or 37.8%, due primarily to a \$75.2 million gain from the sale of wireless spectrum licenses. Our effective tax rate was 38.8% and 38.1% for 2015 and 2014, respectively.

*Net Income*

As a result of the factors described above, our net income was \$89.0 million for 2015, compared to \$147.3 million for 2014.

*Use of Adjusted EBITDA*

We use certain measures that are not defined by GAAP to evaluate various aspects of our business. Adjusted EBITDA is a non-GAAP financial measure and should be considered in addition to, not as a substitute for, net income reported in accordance with GAAP. This term, as defined by us, may not be comparable to similarly titled measures used by other companies. Adjusted EBITDA is reconciled to net income below.

Adjusted EBITDA is defined as net income plus net interest expense, provision for income taxes, depreciation and amortization, equity- and pre-spin cash-based incentive compensation expense, loss (gain) on deferred compensation, other (income) expense, net, acquisition-related costs, loss on disposal of fixed assets and other unusual operating expenses, as defined in the table below. As such, it eliminates the significant non-cash depreciation and amortization expense that results from the capital-intensive nature of our business as well as other non-cash or special items and is unaffected by our capital structure or investment activities. This measure is limited in that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenues and our cash cost of financing. These costs are evaluated through other financial measures.

Table of Contents

We use Adjusted EBITDA to assess our performance. In addition, Adjusted EBITDA generally correlates to the leverage ratio calculation under our Senior Credit Facilities and outstanding Notes (each as defined under “*Financial Condition: Liquidity and Capital Resources—Financing Activity*” below) to determine compliance with the covenants contained in the Senior Credit Facilities and Notes. For the purpose of calculating compliance with leverage covenants, we use a measure similar to Adjusted EBITDA, as presented. Adjusted EBITDA is also a significant performance measure used by us in our annual incentive compensation program. Adjusted EBITDA does not take into account cash used for mandatory debt service requirements or other non-discretionary expenditures, and thus does not represent residual funds available for discretionary uses.

(in thousands)	Year Ended December 31,		
	2016	2015	2014
Net income	\$ 98,939	\$ 89,033	\$ 147,309
Plus: Interest expense, net	30,221	16,090	-
Provision for income taxes	64,168	56,387	90,700
Depreciation and amortization	142,183	140,635	134,167
Equity- and pre-spin cash-based incentive compensation expense	12,298	9,739	3,542
Loss (gain) on deferred compensation	312	(1,141)	1,119
Other (income) expense, net	(5,121)	232	(74,196)
Acquisition-related costs	4,719	-	-
Loss on disposal of fixed assets	2,821	1,735	933
Billing system implementation costs	-	5,007	1,887
Adjusted EBITDA	<u>\$ 350,540</u>	<u>\$ 317,717</u>	<u>\$ 305,461</u>

We believe Adjusted EBITDA is useful to investors in evaluating the operating performance of our Company. Adjusted EBITDA and similar measures with similar titles are common measures used by investors, analysts and peers to compare performance in our industry, although our measure of Adjusted EBITDA may not be directly comparable to similar measures reported by other companies.

**Financial Condition: Liquidity and Capital Resources***Liquidity*

Prior to the spin-off, our cash flows from operations were historically distributed to GHC on a periodic basis, and we historically relied on GHC to fund our working capital requirements and other cash requirements. In contemplation of the spin-off and the related dividend, we recapitalized our Company through a series of financing transactions described below. We believe that existing cash balances, our Senior Credit Facilities and operating cash flows will provide adequate funds to support our current operating plan, make planned capital expenditures and quarterly dividend payments for the next 12 months, and fund the acquisition of NewWave. However, our ability to fund operations and acquisitions and make planned capital expenditures and quarterly dividend payments depends on future operating performance and cash flows, which, in turn, are subject to prevailing economic conditions and to financial, business and other factors, some of which are beyond our control.

The following table shows a summary of our cash flows for the years indicated (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Net cash provided by operating activities	\$ 251,831	\$ 246,413	\$ 205,833
Net cash used in investing activities	(136,317)	(155,225)	(78,400)
Net cash (used in) provided by financing activities	(96,673)	21,601	(127,261)
Change in cash and cash equivalents	18,841	112,789	172
Cash and cash equivalents, beginning of period	119,199	6,410	6,238
Cash and cash equivalents, end of period	<u>\$ 138,040</u>	<u>\$ 119,199</u>	<u>\$ 6,410</u>

At December 31, 2016 and 2015, we had a working capital surplus of \$74.8 million and \$37.9 million, respectively. In connection with the spin-off in 2015, we incurred indebtedness in an aggregate principal amount of \$550 million, of which \$450 million was distributed to GHC prior to the consummation of the spin-off.



Table of Contents

Our net cash provided by operating activities was \$251.8 million, \$246.4 million and \$205.8 million in 2016, 2015, and 2014, respectively. The change in operating cash flows in 2016 compared to 2015 was primarily attributable to higher net income and a favorable change in deferred taxes compared to 2015, partially offset by unfavorable changes in operating assets and liabilities. Operating cash flows increased in 2015 compared to 2014 due to improvements in favorable changes in operating assets and liabilities, partially offset by lower net income.

Our net cash used in investing activities was \$136.3 million, \$155.2 million and \$78.4 million in 2016, 2015 and 2014, respectively. The lower use of cash for investing activities in 2016 compared to 2015 was driven by lower capital expenditures coupled with increases in proceeds received from the sale of a cable system and the sale of fixed assets, partially offset by cash outflows to acquire a cable system. The lower investing cash outflows in 2014 compared to 2015 was driven primarily by proceeds from the cable wireless spectrum license sale in 2014.

Our net cash used in financing activities was \$96.7 million and \$127.3 million in 2016 and 2014, respectively, and our net cash provided by financing activities was \$21.6 million in 2015. Cash outflows in 2016 primarily consisted of \$56.4 million to repurchase our common stock, \$34.4 million in dividends payment to stockholders, \$3.8 million of long-term debt repayment as well as a \$2.2 million of withholding tax payments for vested restricted stock awards. Cash inflows in 2015 were primarily due to \$541.1 million of proceeds from senior notes issuance and borrowings under our Term Loan, net of issuance costs. The net proceeds were utilized primarily to fund the \$450 million distribution to GHC in conjunction with the spin-off. Cash outflows in 2014 reflect amounts transferred to GHC as our financing activities were limited to capital distributions to our prior corporate parent prior to the spin-off.

On July 1, 2015, the Board authorized up to \$250 million of share repurchases (subject to a total cap of 600,000 shares of Company common stock). We plan to make purchases under the stock repurchase program from time to time on the open market and in privately negotiated transactions. The size and timing of these purchases will be based on a number of factors, including price and business and market conditions. Since the beginning of the stock repurchase program through the end of 2016, we repurchased 164,933 shares at an aggregate cost of \$72.7 million. In 2016, we repurchased 126,797 shares at an aggregate cost of \$56.4 million. Additionally, we currently expect to pay quarterly cash dividends on shares of our common stock, subject to approval of the Board. During the fourth quarter of 2016, the Board approved a quarterly dividend of \$1.50 per share of common stock, which was paid on December 2, 2016. During the first quarter of 2017, the Board approved a quarterly dividend of \$1.50 per share of common stock, which will be payable to holders of record as of February 21, 2017 with payment scheduled for early March 2017.

*Financing Activity*

On June 17, 2015, we issued \$450 million aggregate principal amount of 5.750% senior unsecured notes due 2022 (the "Notes"). The Notes were issued pursuant to an indenture (the "Indenture"), dated as of June 17, 2015, among the Company, the Guarantors (as defined below) and the Bank of New York Mellon Trust Company, N.A. The Notes mature on June 15, 2022 and bear interest at a rate of 5.75% per year. Interest on the Notes is payable on June 15 and December 15 of each year. The Notes are jointly and severally guaranteed (the "Guarantees") on a senior unsecured basis by each of our existing and future domestic subsidiaries that initially guaranteed (the "Guarantors") the Senior Credit Facilities (as defined below). The Notes are unsecured and senior obligations of the Company. The Guarantees are unsecured and senior obligations of the Guarantors. At our option, the Notes may be redeemed in whole or in part, at any time prior to June 15, 2018, at a price equal to 100% of the aggregate principal amount of the Notes plus accrued and unpaid interest, if any, to, but excluding, the redemption date plus a "make-whole" premium. We may also redeem the Notes, in whole or in part, at any time on or after June 15, 2018, at the redemption prices specified in the Indenture, plus accrued and unpaid interest, if any, to (but excluding) the redemption date. Additionally, at any time prior to June 15, 2018, we may redeem up to 35% of the aggregate principal amount of the Notes with the net cash proceeds from certain equity offerings at a price equal to 105.75% of the principal amount of the Notes, plus accrued and unpaid interest, if any, to, but excluding, the redemption date. The Indenture includes certain covenants relating to debt incurrence, liens, restricted payments, assets sales and transactions with affiliates, changes in control and mergers or sales of all or substantially all of our assets.

On June 30, 2015, we entered into a Credit Agreement (the "Credit Agreement") among the Company, as borrower, the lenders party thereto, JPMorgan, as administrative agent, and the other agents party thereto. The Credit Agreement provides for a five-year revolving credit facility in an aggregate principal amount of \$200 million (the "Revolving Credit Facility") and a five-year term loan facility in an aggregate principal amount of \$100 million (the "Term Loan Facility" and, together with the Revolving Credit Facility, and as further amended as described below, the "Senior Credit Facilities"). Concurrently with our entry into the Credit Agreement, we borrowed the full amount of the Term Loan Facility (the "Term Loan"). The obligations under the Senior Credit Facilities are obligations of the Company and are guaranteed by the Subsidiary. The obligations under the Senior Credit Facilities are secured, subject to certain exceptions, by substantially all of the assets of the Company and the Subsidiary. Borrowings under the Senior Credit Facilities bear interest, at our option, at a rate per annum determined by reference to either the LIBOR or an adjusted base rate, in each case plus an applicable interest rate margin. The applicable interest rate margin with respect to LIBOR borrowings is a rate

per annum between 1.50% and 2.25% and the applicable interest rate margin with respect to adjusted base rate borrowings is a rate per annum between 0.50% and 1.25%, in each case determined on a quarterly basis by reference to a pricing grid based upon our total net leverage ratio. The Senior Credit Facilities may be prepaid at any time without premium. The Term Loan Facility amortizes in equal quarterly installments at a rate of 2.5% per annum in the first year after funding, 5.0% per annum in the second year after funding, 7.5% per annum in the third year after funding, 10.0% per annum in the fourth year after funding and 15.0% per annum in the fifth year after funding, with the outstanding balance of the Term Loan Facility to be paid on the fifth anniversary of funding. Outstanding borrowings under the Term Loan Facility were \$95.0 million at December 31, 2016. We had \$197.2 million available for borrowing under the Revolving Credit Facility at December 31, 2016.

Table of Contents

The Revolving Credit Facility also gives us the ability to issue letters of credit, which reduce the amount available for borrowing under the Revolving Credit Facility. Letter of credit issuances under the Revolving Credit Facility of \$2.8 million at December 31, 2016 were held for the benefit of certain general and liability insurance matters and bore interest at a rate of 1.625% per annum.

On February 13, 2017, we entered into an amendment to the Credit Agreement to permit, among other things, the incurrence of the \$650 million of senior secured loans expected to be used to finance the acquisition of NewWave and the other transactions contemplated by the Merger Agreement.

*Capital Expenditures*

We have significant ongoing capital expenditure requirements. Capital expenditures are funded primarily by cash on hand and cash flows from operating activities.

We have adopted capital expenditure disclosure guidance as supported by the National Cable & Telecommunications Association ("NCTA"). These disclosures are not required under GAAP, nor do they impact our accounting for capital expenditures under GAAP. The amounts of "capital expenditures" reported in this Annual Report on Form 10-K are calculated in accordance with NCTA disclosure guidelines, which include assets acquired during the relevant periods.

For 2016, 2015 and 2014, capital expenditures were \$125.5 million, \$166.4 million, and \$165.8 million, respectively.

The following table presents our major capital expenditure categories in accordance with NCTA disclosure guidelines for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Customer Premise Equipment	\$ 22,248	\$ 31,459	\$ 38,122
Commercial	8,257	7,147	4,165
Scalable Infrastructure	41,017	57,452	61,567
Line Extensions	10,470	8,505	7,064
Upgrade/Rebuild	17,575	25,572	23,318
Support Capital	25,967	36,226	31,551
Total	<u>\$ 125,534</u>	<u>\$ 166,361</u>	<u>\$ 165,787</u>

*Contractual Obligations and Contingent Commitments*

The following is a summary of our contractual obligations as of December 31, 2016 (in thousands):

Years ending December 31,	Programming purchase commitments (1)	Operating leases	Total debt, including capital lease	Other purchase obligations (2)	Total
2017	\$ 171,995	\$ 1,038	\$ 6,250	\$ 24,162	\$ 203,445
2018	150,830	728	8,767	15,731	176,056
2019	124,507	564	12,517	8,988	146,576
2020	83,621	452	67,517	3,990	155,580
2021	19,244	360	17	2,507	22,128
Thereafter	-	741	450,216	4,060	455,017
Total	<u>\$ 550,197</u>	<u>\$ 3,883</u>	<u>\$ 545,284</u>	<u>\$ 59,438</u>	<u>\$ 1,158,802</u>

(1) Includes commitments to purchase programming to be produced in future years.

(2) Includes purchase obligations related to capital projects and other legally binding commitments. Other purchase orders made in the ordinary course of business are excluded from the table above. Any amounts for which we are liable under purchase orders are reflected in our Consolidated Balance Sheets as Accounts payable and accrued liabilities.



Table of Contents

Programming and content purchases represent contracts that we have with cable television networks and broadcast stations to provide programming services to our subscribers. The amounts included above represent estimates of the future programming costs for these contract requirements and commitments based on subscriber numbers and tier placement as of December 31, 2016 applied to the per-subscriber rates contained in these contracts. Actual amounts due under such contracts may differ from the amounts above based on the actual subscriber numbers and tier placements. In addition, programming purchases sometimes occur pursuant to non-binding commitments, which are not reflected in the summary above.

Long-term debt relates to principal repayment obligations as defined by the agreements described in the "Financing Activity" section above.

The following items are not included as contractual obligations due to various factors discussed below. However, we incur these costs as part of our operations:

- We rent utility poles used in our operations. Generally, pole rentals are cancellable on short notice, but we anticipate that such rentals will recur. Rent expense for pole attachments was approximately \$5.7 million, \$5.7 million and \$5.5 million in 2016, 2015 and 2014, respectively.
- We pay franchise fees under multi-year franchise agreements based on a percentage of revenues generated from video service per year. Franchise fees and other franchise-related costs included in the Consolidated Statements of Operations and Comprehensive Income were \$14.2 million, \$15.7 million and \$16.7 million in 2016, 2015 and 2014, respectively.
- We have cable franchise agreements requiring the construction of cable plant and the provision of services to customers within the franchise areas. In connection with these obligations under existing franchise agreements, we obtain surety bonds or letters of credit guaranteeing performance to municipalities and public utilities and payment of insurance premiums. Such surety bonds and letters of credit as of December 31, 2016 and 2015 totaled \$5.1 million and \$4.6 million, respectively. Payments under these arrangements are required only in the event of nonperformance. We do not expect that these contingent commitments will result in any amounts being paid in the foreseeable future.

*Off-Balance Sheet Arrangements*

With the exception of surety bonds and letters of credit noted above, we do not have any off-balance-sheet arrangements or financing activities with special-purpose entities. Transactions with related parties, as discussed in Note 16 to our Consolidated Financial Statements included elsewhere in this Annual Report on Form 10-K, pertain to the spin-off, and these arrangements may not reflect terms that would have resulted from arm's-length negotiations among unaffiliated third parties.

**Critical Accounting Policies and Estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and judgments that affect the amounts reported in the financial statements. On an ongoing basis, we evaluate our estimates and assumptions. We base our estimates on historical experience and other assumptions believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates.

An accounting policy is considered to be critical if it is important to our financial condition and results and if it requires management's most difficult, subjective and complex judgments in its application. For a summary of all of our significant accounting policies, see Note 2 of the Notes to our Consolidated Financial Statements included elsewhere in this Annual Report on Form 10-K.

Table of Contents*Long-lived Assets*

A long-lived asset or asset group is tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Indicators of impairment may include:

- a significant decrease in the market value of the asset;
- a significant change in the extent or manner in which an asset is used or a significant change in the physical condition of the asset;
- a significant adverse change in legal factors or in the business climate that could affect the value of an asset, including an adverse action or assessment by a regulator;
- an accumulation of costs significantly in excess of the amount originally expected to acquire or construct an asset;
- a current period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with an asset; and
- a current expectation that, more likely than not, an asset will be sold or otherwise disposed of significantly before the end of its estimated useful life.

When an indicator of impairment is determined, the first step is to identify the future intent of the asset or asset group: hold for continued use, hold for sale, or dispose by a means other than sale. If the asset is held for continued use and the carrying amount exceeds the undiscounted sum of cash flows expected from the use and eventual disposition of the property, the impairment loss is recognized as the difference between the carrying amount and the estimated fair value of the asset or asset group, and the new cost basis is depreciated over the remaining useful life of the asset. If the intent is to hold the asset for sale and certain other criteria are met (e.g., the asset can be disposed of currently, appropriate levels of authority have approved the sale, and there is an active program to locate a buyer), the impairment test involves comparing the asset's carrying value to its estimated fair value. To the extent the carrying value is greater than the asset's estimated fair value, an impairment charge is recognized for the difference. If the asset is to be disposed by a means other than sale, the depreciation estimates are revised to reflect the use of the asset over its shortened useful life.

Significant judgments in this area involve determining whether an event has occurred, determining the future cash flows for the assets involved and selecting the appropriate discount rate to be applied in determining estimated fair value.

*Goodwill and Other Intangible Assets*

We have a significant amount of goodwill and indefinite-lived intangible assets that are reviewed at least annually for possible impairment. For 2016, we did not enter into any material transactions that would change the carrying amount of goodwill and indefinite-lived intangible; therefore, these balances were as follows:

(dollars in millions)	As of December 31,	
	2016	2015
Goodwill and indefinite-lived intangible assets	\$ 582.1	\$ 581.8
Total assets	\$ 1,397.3	\$ 1,398.8
Percentage of goodwill and indefinite-lived intangible assets to total assets	42%	42%

*Goodwill*

We test goodwill for impairment as of November 30 of each year or more frequently as warranted by events or changes in circumstances. Accounting guidance also permits an optional qualitative assessment for goodwill to determine whether it is more likely than not that the carrying value of a reporting unit exceeds its fair value. If, after this qualitative assessment, we determine that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount then no further quantitative testing would be necessary. If management elects or is required to perform the two-step test under the accounting guidance, the first step involves a comparison of the estimated fair value of the reporting unit to its carrying amount. If the estimated fair value of the reporting unit exceeds its carrying amount, goodwill of the reporting unit is not considered impaired and the second step of the goodwill impairment is not necessary. If the carrying amount of a reporting unit exceeds its estimated fair value, then the second step of the goodwill impairment test must be performed, and a comparison of the implied fair value of the reporting unit's goodwill is compared to its carrying amount to determine the amount of impairment, if any. The fair value of the reporting unit, when performing

the second step of the goodwill impairment test, is determined using both an income approach and market approach. The income approach model used for goodwill valuation is consistent with that used for the franchise valuation noted below except that cash flows from the entire business enterprise are used for the goodwill valuation. The market approach model estimates the fair value of the reporting unit based on market prices in actual precedent transactions of similar businesses and market valuations of guideline public companies. In 2016, we elected to perform a qualitative goodwill impairment assessment and concluded that goodwill is not impaired.

Table of Contents*Indefinite-Lived Intangible Assets*

Our \$497.1 million and \$496.3 million of intangible assets with an indefinite life as of December 31, 2016 and 2015, respectively, are principally from franchise agreements. These franchise agreements result from agreements we have with state and local governments that allow us to contract and operate a cable business within a specified geographic area. We expect our cable franchise agreements to provide us with substantial benefit for a period that extends beyond the foreseeable horizon, and we have historically obtained renewals and extensions of such agreements for nominal costs and without material modifications to the agreements. We grouped the recorded values of our various cable franchise agreements into regional cable systems or units of account.

For our goodwill impairment testing in 2016, we elected to perform a qualitative impairment assessment that indicated the fair value of the franchise assets in each unit of accounting exceeds the carrying value of such assets and thus resulted in no impairment. For each franchise unit of accounting, the estimated fair value of the franchise assets exceeds the carrying value. Based on our qualitative impairment assessment and sensitivity analyses, none of our franchise assets are considered at risk of impairment.

Periodically, we will elect to perform a quantitative analysis of impairment. If we elect or are required to perform a quantitative analysis to test our franchise assets for impairment, we determine the estimated fair value of franchises utilizing a discounted cash flow model, and in certain cases, a market value approach is also utilized to supplement the discounted cash flow model to determine the estimated fair value of the indefinite-lived intangible assets. We make estimates and assumptions regarding future cash flows, discount rates, long-term growth rates and other market values to determine the estimated fair value of the indefinite-lived intangible assets.

This approach makes use of unobservable factors, such as projected revenues, expenses, capital expenditures, customer trends and a discount rate applied to the estimated cash flows. The determination of the discount rate is derived from our weighted average cost of capital, which uses a market participant's cost of equity and after-tax cost of debt and reflects the risks inherent in the cash flows. We estimate discounted future cash flows using reasonable and appropriate assumptions, including, among others, penetration rates for data, video and voice; revenue growth rates; operating margins; and capital expenditures. The assumptions are based on our Company's and our peers' historical operating performance adjusted for current and expected competitive and economic factors surrounding the cable industry. The estimates and assumptions made in our valuations are inherently subject to significant uncertainties, many of which are beyond our control, and there is no assurance that these results can be achieved. The primary assumptions for which there is a reasonable possibility of the occurrence of a variation that would significantly affect the measurement value include the assumptions regarding revenue growth, programming expense growth rates, the amount and timing of capital expenditures, actual customer trends and the discount rate utilized.

*Property, Plant and Equipment*

The cable industry is capital intensive, and a significant portion of our resources is spent on capital activities associated with extending, rebuilding, and upgrading our cable network. The following table presents certain information regarding our net property, plant and equipment, including as a percentage of total assets, and our cash paid for property, plant and equipment for the periods indicated.

(dollars in millions)	As of December 31,	
	2016	2015
Property, plant and equipment	\$ 619.6	\$ 640.6
Total assets	\$ 1,397.3	\$ 1,398.8
Percentage of property, plant and equipment to total assets	44%	46%

Table of Contents

(dollars in millions)	For the Year ended December 31,	
Cash paid for property, plant and equipment		
2016	\$	141.7
2015	\$	156.1
2014	\$	177.4

Costs incurred with network construction, initial customer installations, installations of refurbishments and the addition of network equipment necessary to provide new or advanced video services, are capitalized. These costs consist of materials, subcontractor labor, direct consulting fees, and internal labor and related costs associated with the construction activities. These costs are depreciated over the estimated life of the plant (10 to 12 years) and headend facilities (10 years). Costs of operating the plant and the technical facilities, including repairs and maintenance, are expensed as incurred.

Costs incurred to connect businesses or residences that have not been previously connected to the infrastructure or digital platform are also capitalized. These costs include materials, subcontractor labor, internal labor, and other related costs associated with the connection activities. New connections are amortized over the estimated useful lives of 10 years. The costs related to reconnection, programming service up- and down- grade, repair and maintenance, and disconnection activities are expensed as incurred.

The estimated useful lives assigned to our property, plant and equipment are reviewed on an annual basis or more frequently if circumstances warrant and such lives are revised to the extent necessary due to changing facts and circumstances. Any changes in estimated useful lives are reflected prospectively.

In the first quarter of 2017 we changed our accounting estimate related to the capitalization of certain internal labor and related costs associated with construction and customer installation activities. Historically, we did not have adequate information to identify and calculate all of the capitalizable labor and related costs, and therefore these costs were expensed as incurred. In the first quarter of 2017, we have implemented systems and processes that allow us to more accurately estimate the amount of directly identifiable labor costs incurred on construction and installation activities. We anticipate that this change in estimate will result in an increase of capitalized labor costs in the range of \$28 million to \$33 million on an annual basis, resulting in an equivalent decrease in expenses and increase in capital expenditures beginning in 2017.

#### Recently Adopted and Issued Accounting Pronouncements

Recent accounting pronouncements which may be applicable to us are described in Note 2 to our Consolidated Financial Statements.

#### ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the potential gain/loss arising from changes in market rates and prices, such as interest rates. As described under "Management's Discussion and Analysis of Financial Condition and Results of Operations—Financial Condition: Liquidity and Capital Resources—Financing Activity," our long-term debt at December 31, 2016 consisted of \$450 million of the Notes and \$95.0 million of borrowings under the Senior Credit Facilities, which bear interest, at our option, at a rate per annum determined by reference to either the LIBOR or an adjusted base rate, in each case plus an applicable interest rate margin. Based on the principal outstanding under our Senior Credit Facilities as of December 31, 2016, assuming, hypothetically, that the LIBOR rate applicable to the Senior Credit Facilities was 100 basis points higher would result in a change in interest expense of approximately \$1.0 million annually. At December 31, 2016, the aggregate fair value of the Notes, based upon quoted market prices, was \$463.5 million. An increase in the market rate of interest applicable to the Notes would not increase our interest expense with respect to the Notes since the rate of interest we are required to pay on the Notes is fixed.

#### ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Our consolidated financial statements, the related notes thereto, and the reports of independent accountants are included in this Annual Report on Form 10-K beginning on page F-1.

-----

Table of Contents**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

**ITEM 9A. CONTROLS AND PROCEDURES****Disclosure Controls and Procedures**

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of December 31, 2016, the end of the period covered by this Annual Report on Form 10-K. Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures were effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act and were effective in ensuring that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

**Management's Report on Internal Control Over Financial Reporting**

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). The Company's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

The Company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Company's management conducted an assessment of the effectiveness of internal control over financial reporting as of December 31, 2016. In making this assessment, management used the criteria set forth in *Internal Control – Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on the results of this assessment, management has concluded that, as of December 31, 2016, the Company's internal control over financial reporting was effective based on these criteria.

The effectiveness of the Company's internal control over financial reporting as of December 31, 2016, has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report on page F-2 of this Annual Report on Form 10-K.

**Changes in Internal Control Over Financial Reporting**

There has been no change in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended December 31, 2016 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

.....

Table of Contents**ITEM 9B. OTHER INFORMATION**

None.

**PART III****ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

The information required by this item will be included in our Definitive Proxy Statement to be filed pursuant to Regulation 14A within 120 days after our year ended December 31, 2016 in connection with our 2017 Annual Meeting of Stockholders (the "2017 Proxy Statement"), or in amendment to this Annual Report on Form 10-K, and is incorporated herein by reference.

**ITEM 11. EXECUTIVE COMPENSATION**

The information required by this item will be included in the 2017 Proxy Statement, or in amendment to this Annual Report on Form 10-K, and is incorporated herein by reference.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The information required by this item will be included in the 2017 Proxy Statement, or in amendment to this Annual Report on Form 10-K, and is incorporated herein by reference.

**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

The information required by this item will be included in the 2017 Proxy Statement, or in amendment to this Annual Report on Form 10-K, and is incorporated herein by reference.

**ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

The information required by this item will be included in the 2017 Proxy Statement, or in amendment to this Annual Report on Form 10-K, and is incorporated herein by reference.

Table of Contents**PART IV****ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES**

## (a) Documents filed as part of this report:

- (1) *Financial Statements.* The consolidated financial statements listed on the index set forth on page F-1 of this Annual Report on Form 10-K are filed as a part of this Annual Report on Form 10-K.
- (2) *Financial Statement Schedules.* All financial statement schedules have been omitted since the information is either not applicable or required or is included in the financial statements or notes thereof.

## (b) Exhibits.

**Exhibit   Description**  
**No.**

- |      |   |
|------|---|
| 2.1  | Separation and Distribution Agreement, dated as of June 16, 2015, by and between Graham Holdings Company and Cable One, Inc. (incorporated herein by reference to Exhibit 2.1 to the Current Report on Form 8-K of Cable One, Inc. filed on July 18, 2015).   |
| 2.2  | Agreement and Plan of Merger, dated as of January 17, 2017, by and among Cable One, Inc., RBI Holding LLC, Frequency Merger Sub, LLC, RBI Blocker Corp., RBI Blocker Holdings LLC, and GTCR-RBI, LLC, solely in its capacity as the equityholder representative (incorporated herein by reference to Exhibit 2.1 to the Current Report on Form 8-K/A of Cable One, Inc. filed on January 20, 2017). |
| 3.1  | Amended and Restated Certificate of Incorporation of Cable One, Inc. (incorporated herein by reference to Exhibit 3.1 to the Current Report on Form 8-K of Cable One, Inc. filed on July 1, 2015).  |
| 3.2  | Amended and Restated By-laws of Cable One, Inc. (incorporated herein by reference to Exhibit 3.2 to the Current Report on Form 8-K of Cable One, Inc. filed on July 1, 2015).   |
| 4.1  | Indenture, dated as of June 17, 2015, among Cable One, Inc., the Guarantors named therein and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated herein by reference to Exhibit 4.1 to the Current Report on Form 8-K of Cable One, Inc. filed on June 18, 2015).  |
| 10.1 | Credit Agreement, dated as of June 30, 2015, by and among Cable One, Inc., as borrower, the lenders party thereto, JPMorgan Chase Bank, N.A., as administrative agent, and the other agents party thereto (incorporated herein by reference to Exhibit 10.1 to the Current Report on Form 8-K of Cable One, Inc. filed on July 1, 2015).  |
| 10.2 | Tax Matters Agreement, dated as of June 16, 2015, by and between Graham Holdings Company and Cable One, Inc. (incorporated herein by reference to Exhibit 10.2 to the Current Report on Form 8-K of Cable One, Inc. filed on June 18, 2015).  |
| 10.3 | Employee Matters Agreement, dated as of June 16, 2015, by and between Graham Holdings Company and Cable One, Inc. (incorporated herein by reference to Exhibit 10.3 to the Current Report on Form 8-K of Cable One, Inc. filed on June 18, 2015).+  |
| 10.4 | Individual Deferred Compensation Arrangement between Cable One, Inc. and Thomas O. Might, dated June 25, 1999 (incorporated herein by reference to Exhibit 10.4 to Amendment No. 2 to Form 10 of Cable One, Inc. filed on May 15, 2015).+   |
| 10.5 | Cable One, Inc. 2015 Omnibus Incentive Compensation Plan (incorporated herein by reference to Exhibit 10.4 to the Current Report on Form 8-K of Cable One, Inc. filed on June 11, 2015).+   |
| 10.6 | Cable One, Inc. Supplemental Executive Retirement Plan (incorporated herein by reference to Exhibit 10.5 to the Current Report on Form 8-K of Cable One, Inc. filed on June 11, 2015).+   |

TABLE OF CONTENTS

Table of Contents**Exhibit Description****No.**

- 10.7 Cable One, Inc. Deferred Compensation Plan (incorporated herein by reference to Exhibit 10.6 to the Current Report on Form 8-K of Cable One, Inc. filed on June 11, 2015).+
- 10.8 Form of Restricted Stock Award Agreement for restricted stock grants on July 8, 2015 (incorporated herein by reference to Exhibit 10.4 to the Quarterly Report on Form 10-Q of Cable One, Inc. filed on August 7, 2015).+
- 10.9 Form of Director Restricted Stock Unit Agreement for restricted stock unit grants on August 4, 2015 (incorporated herein by reference to Exhibit 10.1 to the Current Report on Form 8-K of Cable One, Inc. filed on August 10, 2015).+
- 10.10 Form of Stock Appreciation Right Agreement for stock appreciation right grants on September 1, 2015 (incorporated herein by reference to Exhibit 10.2 to the Current Report on Form 8-K of Cable One, Inc. filed on August 10, 2015).+
- 10.11 Form of Restricted Stock Award Agreement for restricted stock grants on January 4, 2016 (incorporated herein by reference to Exhibit 10.11 to the Annual Report on Form 10-K of Cable One, Inc. filed on March 7, 2016).+
- 10.12 Form of Stock Appreciation Right Agreement for stock appreciation right grants on or after January 3, 2017.\*\*
- 10.13 Form of Restricted Stock Award Agreement for performance-based restricted stock grants on or after January 3, 2017.\*\*
- 10.14 Form of Restricted Stock Award Agreement for time-based restricted stock grants on or after January 3, 2017.\*\*
- 10.15 Amendment No. 1 to Credit Agreement, dated as of February 13, 2017, among Cable One, Inc., the lenders party thereto and JPMorgan Chase Bank, N.A., as administrative agent (incorporated herein by reference to Exhibit 10.1 to the Current Report on Form 8-K of Cable One, Inc. filed on February 14, 2017).
- 21.1 List of subsidiaries of Cable One, Inc. (incorporated herein by reference to Exhibit 21.1 to Amendment No. 1 to Form 10 of Cable One, Inc. filed on April 17, 2015).
- 23.1 Consent of PricewaterhouseCoopers LLP.\*
- 24.1 Power of Attorney (included on Signatures page of this Annual Report on Form 10-K).\*
- 31.1 Principal Executive Officer Certification required by Rules 13a-14 and 15d-14 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- 31.2 Principal Financial Officer Certification required by Rules 13a-14 and 15d-14 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- 32 Certification of Principal Executive Officer and Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*\*
- 101.INS XBRL Instance Document.\*
- 101.SCH XBRL Taxonomy Extension Schema Document.\*
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document.\*
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document.\*
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document.\*
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.\*

\* Filed herewith.

\*\* Furnished herewith.



Table of Contents

**ITEM 16. FORM 10-K SUMMARY**

None.

Table of Contents**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

CABLE ONE, INC.  
(Registrant)

Date: March 1, 2017

By: /s/ Julia M. Laulis  
Julia M. Laulis  
President and Chief Executive Officer

**POWER OF ATTORNEY**

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Kevin P. Coyle and Alan H. Silverman, and each of them, his or her true and lawful attorneys-in-fact and agents, with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign any and all amendments to this Report, and to file the same, with all exhibits thereto, and all other documents in connection therewith, with the Securities and Exchange Commission, granting unto each said attorney-in-fact and agent full power and authority to do and perform each and every act in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or either of them or their or his or her substitute or substitutes may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ Julia M. Laulis</u> Julia M. Laulis	President and Chief Executive Officer (Principal Executive Officer) and Director	March 1, 2017
<u>/s/ Kevin P. Coyle</u> Kevin P. Coyle	Senior Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	March 1, 2017
<u>/s/ Thomas O. Might</u> Thomas O. Might	Executive Chairman and Chairman of the Board	March 1, 2017
<u>/s/ Naomi M. Bergman</u> Naomi M. Bergman	Director	March 1, 2017
<u>/s/ Brad D. Brian</u> Brad D. Brian	Director	March 1, 2017
<u>/s/ Thomas S. Gayner</u> Thomas S. Gayner	Director	March 1, 2017
<u>/s/ Deborah J. Kissire</u> Deborah J. Kissire	Director	March 1, 2017
<u>/s/ Alan G. Spoon</u> Alan G. Spoon	Director	March 1, 2017
<u>/s/ Wallace R. Weitz</u> Wallace R. Weitz	Director	March 1, 2017
<u>/s/ Katharine B. Weymouth</u> Katharine B. Weymouth	Director	March 1, 2017



Table of Contents**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

<b>Cable One, Inc.</b>	<b>Page</b>
Report of Independent Registered Public Accounting Firm	<u>F-2</u>
Consolidated Balance Sheets as of December 31, 2016 and 2015	<u>F-3</u>
Consolidated Statements of Operations and Comprehensive Income for the Years Ended December 31, 2016, 2015 and 2014	<u>F-4</u>
Consolidated Statements of Stockholders' Equity for the Years Ended December 31, 2016, 2015 and 2014	<u>F-5</u>
Consolidated Statements of Cash Flows for the Years Ended December 31, 2016, 2015 and 2014	<u>F-6</u>
Notes to Consolidated Financial Statements	<u>F-7</u>

F-1

Table of Contents**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders of Cable One, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and comprehensive income, of stockholders' equity and of cash flows present fairly, in all material respects, the financial position of Cable One, Inc. and its subsidiary at December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control Over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our audits (which was an integrated audit in 2016). We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

Phoenix, Arizona

March 1, 2017

Table of Contents

**CABLE ONE, INC.**  
**CONSOLIDATED BALANCE SHEETS**

<u>(in thousands, except par value and share data)</u>	<u>December 31,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
<b>Assets</b>		
Current Assets:		
Cash and cash equivalents	\$ 138,040	\$ 119,199
Accounts receivable, net	37,073	34,705
Prepaid assets	10,824	10,824
Total Current Assets	<u>185,937</u>	<u>164,728</u>
Property, plant and equipment, net	619,621	640,567
Intangibles, net	497,480	496,770
Goodwill	84,928	85,488
Other assets	9,305	11,252
Total Assets	<u>\$ 1,397,271</u>	<u>\$ 1,398,805</u>
<b>Liabilities and Stockholders' Equity</b>		
Current Liabilities:		
Accounts payable and accrued liabilities	\$ 82,703	\$ 95,288
Deferred revenue	22,190	22,363
Income taxes payable	-	5,431
Long-term debt - current portion	6,250	3,750
Total Current Liabilities	<u>111,143</u>	<u>126,832</u>
Long-term debt	530,886	535,511
Accrued compensation and related benefits	24,157	24,399
Other liabilities	277	90
Deferred income taxes	276,297	276,627
Total Liabilities	<u>942,760</u>	<u>963,459</u>
Commitments and contingencies (see Note 17)		
Stockholders' Equity		
Common stock (\$0.01 par value; 40,000,000 shares authorized; 5,887,899 and 5,879,925 shares issued, and 5,708,223 and 5,833,442 shares outstanding as of December 31, 2016 and 2015, respectively)	59	59
Additional paid-in capital	17,669	4,929
Retained earnings	511,776	447,282
Accumulated other comprehensive loss	(446)	(557)
Treasury stock, at cost (179,676 and 46,483 shares held as of December 31, 2016 and 2015, respectively)	(74,547)	(16,367)
Total Stockholders' Equity	<u>454,511</u>	<u>435,346</u>
Total Liabilities and Stockholders' Equity	<u>\$ 1,397,271</u>	<u>\$ 1,398,805</u>

See accompanying notes to consolidated financial statements.

Table of Contents

**CABLE ONE, INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME**

<u>(in thousands, except per share and share data)</u>	<b>Year Ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
Revenues	\$ 819,625	\$ 807,266	\$ 814,812
Costs and Expenses			
Operating (excluding depreciation and amortization)	304,438	310,925	327,974
Selling, general and administrative	184,797	193,964	188,858
Depreciation and amortization	142,183	140,635	134,167
Total operating costs and expenses	631,418	645,524	650,999
Income from operations	188,207	161,742	163,813
Interest expense	(30,221)	(16,090)	-
Other income (expense), net	5,121	(232)	74,196
Income before income taxes	163,107	145,420	238,009
Provision for income taxes	64,168	56,387	90,700
Net income	\$ 98,939	\$ 89,033	\$ 147,309
Other comprehensive gain (loss), net of tax	111	(557)	-
Comprehensive income	\$ 99,050	\$ 88,476	\$ 147,309
Net income per common share: (a)			
Basic	\$ 17.23	\$ 15.21	\$ 25.21
Diluted	\$ 17.14	\$ 15.19	\$ 25.21
Weighted average common shares outstanding: (a)			
Basic	5,743,568	5,853,283	5,843,313
Diluted	5,770,960	5,860,089	5,843,313

(a) On July 1, 2015, Graham Holdings Company distributed 5,843,313 shares of Cable One, Inc. common stock to existing holders of Graham Holdings Company common stock. Basic and diluted net income per common share for the year ended December 31, 2014 are calculated using the number of shares distributed on July 1, 2015.

See accompanying notes to consolidated financial statements.

Table of Contents

**CABLE ONE, INC.**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**

(in thousands, except share data)	Common Stock		Additional Paid-In	Retained	Additional GHC Investment	Treasury Stock,	Accumulated Other Comprehensive	Total
	Shares	Amount	Capital	Earnings	(Deficit)	at cost	Loss	Stockholders' Equity
<b>Balance at December 31, 2013</b>	5,843,313	58	-	1,178,610	(343,409)	-	-	835,259
Net income	-	-	-	147,309	-	-	-	147,309
Net transfers to GHC	-	-	-	-	(129,280)	-	-	(129,280)
<b>Balance at December 31, 2014</b>	5,843,313	58	-	1,325,919	(472,689)	-	-	853,288
Dividends paid to GHC	-	-	-	(450,000)	-	-	-	(450,000)
Net income	-	-	-	89,033	-	-	-	89,033
Net transfers to GHC	-	-	-	-	(36,199)	-	-	(36,199)
Reclassification of Additional GHC investment (deficit) in connection with spin-off	-	-	-	(508,888)	508,888	-	-	-
Changes in pension, net of tax	-	-	-	-	-	-	(557)	(557)
Equity-based compensation	36,612	1	4,929	-	-	-	-	4,930
Forfeiture of restricted stock	(8,347)	-	-	-	-	-	-	-
Repurchase of common stock	(38,136)	-	-	-	-	(16,367)	-	(16,367)
Dividends paid to stockholders	-	-	-	(8,782)	-	-	-	(8,782)
<b>Balance at December 31, 2015</b>	5,833,442	59	4,929	447,282	-	(16,367)	(557)	435,346
Net income	-	-	-	98,939	-	-	-	98,939
Changes in pension, net of tax	-	-	-	-	-	-	111	111
Equity-based compensation	-	-	12,298	-	-	-	-	12,298
Issuance of common stock under restricted stock unit awards	947	-	(380)	-	-	380	-	-
Issuance of restricted stock awards, net of forfeitures	4,247	-	-	-	-	-	-	-
Repurchase of common stock	(126,797)	-	-	-	-	(56,370)	-	(56,370)
Withholding tax for	(3,616)	-	-	-	-	(2,190)	-	(2,190)

restricted stock awards							
Excess income tax benefits for equity-based compensation activities	-	822	-	-	-	-	822
Dividends paid to stockholders	-	-	(34,445)	-	-	-	(34,445)
<b>Balance at December 31, 2016</b>	<u>5,708,223</u>	<u>59</u>	<u>17,669</u>	<u>511,776</u>	<u>-</u>	<u>(74,547)</u>	<u>454,511</u>

See accompanying notes to consolidated financial statements.

Table of Contents

**CABLE ONE, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

Year Ended December 31,

<u>(in thousands)</u>	2016	2015	2014
<b>Cash flows from operating activities:</b>			
Net income	\$ 98,939	\$ 89,033	\$ 147,309
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	142,183	140,635	134,167
Amortization of deferred financing costs	1,642	902	-
Equity-based compensation	12,298	9,213	1,997
Excess income tax benefits for equity-based compensation activities	(822)	-	-
Gain on sale of cable system	(4,096)	-	-
Deferred income taxes	(403)	(11,282)	4,276
Net loss on sales of property, plant and equipment	2,821	602	858
Net gain on sale of intangible assets	-	-	(75,249)
Changes in operating assets and liabilities:			
Accounts receivable, net	(2,251)	(4,976)	627
Prepaid assets	243	1,763	(3,429)
Accounts payable and accrued liabilities	4,052	15,417	(4,800)
Deferred revenue	(173)	1,359	3,200
Income taxes payable	(4,609)	2,231	(322)
Other assets and other liabilities, net	2,007	1,516	(2,801)
Net cash provided by operating activities	<u>251,831</u>	<u>246,413</u>	<u>205,833</u>
<b>Cash flows from investing activities:</b>			
Capital expenditures	(125,534)	(166,361)	(165,787)
Change in accrued expenses related to capital expenditures	(16,190)	10,225	(11,613)
Proceeds from sales of intangible assets	-	-	97,399
Proceeds from sale of cable system	6,752	-	-
Acquisition of cable system	(2,672)	-	-
Proceeds from sales of property, plant and equipment and other	1,327	911	1,601
Net cash used in investing activities	<u>(136,317)</u>	<u>(155,225)</u>	<u>(78,400)</u>
<b>Cash flows from financing activities:</b>			
Net transfers to GHC	-	(42,665)	(131,277)
Proceeds from issuance of long-term debt, net of issuance costs	-	541,114	-
Payments of debt issue costs	-	(1,768)	-
Payments on long-term debt	(3,767)	(1,250)	-
Repurchase of common stock	(56,370)	(16,367)	-
Payment of withholding tax for restricted shares	(2,190)	-	-
Dividends paid to stockholders	(34,445)	(8,782)	-
Dividends paid to GHC	-	(450,000)	-
Excess income tax benefits for equity-based compensation activities	822	-	-
Cash overdraft	(723)	1,319	4,016
Net cash (used in) provided by financing activities	<u>(96,673)</u>	<u>21,601</u>	<u>(127,261)</u>
Change in cash and cash equivalents	18,841	112,789	172
Cash and cash equivalents, beginning of period	119,199	6,410	6,238
Cash and cash equivalents, end of period	<u>\$ 138,040</u>	<u>\$ 119,199</u>	<u>\$ 6,410</u>
<b>Supplemental cash flow disclosures:</b>			
Cash paid for interest expense	28,628	14,038	-
Cash paid for income taxes	<u>\$ 73,007</u>	<u>\$ 29,970</u>	<u>\$ 5,629</u>
<b>Non-cash investing and financing activity:</b>			
Equipment financed with capital lease	\$ -	\$ 301	\$ -

---

---

See accompanying notes to consolidated financial statements.

F-6

---

Table of Contents

## CABLE ONE, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**1. SEPARATION FROM GRAHAM HOLDINGS COMPANY AND DESCRIPTION OF BUSINESS**

On July 1, 2015, Cable One, Inc. ("Cable One") became an independent company traded under the ticker symbol "CABO" on the New York Stock Exchange after completion of its spin-off from Graham Holdings Company ("GHC"). The spin-off was effected through the distribution by GHC of 100% of the outstanding shares of common stock of Cable One to GHC stockholders as of the record date for the distribution (the "spin-off") in a pro rata dividend. In connection with the spin-off, approximately 5.84 million shares of Cable One's common stock were issued and outstanding on July 1, 2015, based on approximately 0.96 million shares of GHC Class A Common Stock and 4.88 million shares of GHC Class B Common Stock outstanding as of June 30, 2015. No preferred stock was issued or outstanding.

The financial statements included herein have been retroactively restated, including share and per share amounts, to reflect the effects of the spin-off.

Cable One owns and operates cable systems that provide data, video and voice services to residential and commercial subscribers in 19 Western, Midwestern and Southern states of the United States of America. At the end of 2016, Cable One provided service to 513,908 data customers, 320,246 video customers and 115,811 voice customers.

Unless otherwise stated or the context otherwise indicates, all references in the Consolidated Financial Statements and the accompanying Notes to Consolidated Financial Statements in this Annual Report on Form 10-K to "Cable One," "us," "our," "we" or the "Company" means Cable One, Inc. and its wholly owned subsidiary, Cable One VoIP LLC (the "Subsidiary"). References in the Consolidated Financial Statements and the accompanying Notes to Consolidated Financial Statements in this Annual Report on Form 10-K to "GHC" refer to Graham Holdings Company.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation.** The accompanying Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") and the rules and regulations of the Securities and Exchange Commission (the "SEC").

Prior to the spin-off, the Company's financial statements were derived from the consolidated financial statements and accounting records of GHC. The impact of transactions between the Company and GHC was included in the Consolidated Financial Statements and was considered to be effectively settled for cash in the Consolidated Financial Statements at the time the transaction was recorded. The total net effect of the settlement of these intercompany transactions was reflected in the Consolidated Statements of Cash Flows as a financing activity at the time of settlement.

The Company functioned as part of the larger group of subsidiary companies controlled by GHC prior to the spin-off, and accordingly, GHC provided certain support and overhead functions to the Company. These functions included finance, human resources, legal, information technology, general insurance, risk management and other corporate functions. The costs of such services were allocated to the Company based on the most relevant allocation methods to the service provided. Management believed such allocations were reasonable and were consistently applied; however, they may not have been indicative of the actual expense that would have been incurred had the Company been operating on a stand-alone basis. See Notes 12 and 16 for details on these allocations prior to the spin off.

Additionally, prior to the spin-off, the Company participated in a centralized approach to cash management and in financing its operations managed by GHC. Cash was transferred to GHC and GHC funded the Company's operating and investing activities as needed. Accordingly, cash and cash equivalents at GHC were not allocated to the Company in the Consolidated Financial Statements. GHC's third-party debt, and the related interest expense, were not allocated to the Company for any of the periods presented as the Company was not the legal obligor on the debt and GHC borrowings were not directly attributable to the Company's business.

Prior to the spin-off, the Company's operations were historically included in GHC's consolidated U.S. Federal and certain state tax returns. The Company did not maintain taxes payable to/from GHC and was deemed to settle the annual current tax balances immediately with the legal tax-paying entities in the respective jurisdictions.



Table of Contents

The Company's results of operations for the years ended December 31, 2016 and 2015 may not be indicative of the Company's future results. In addition, as the Company did not operate as a stand-alone entity prior to July 1, 2015, the Consolidated Financial Statements included herein may not necessarily be indicative of the Company's future performance and may not necessarily reflect what its financial position, results of operations or cash flows would have been had it operated as a stand-alone entity during all of the periods presented.

Certain reclassifications have been made to prior period amounts to conform to the current year presentation.

**Principles of Consolidation.** The accompanying Consolidated Financial Statements include the accounts of the Company and the Subsidiary. All significant intercompany accounts and transactions have been eliminated in consolidation.

**Segment Reporting.** ASC 280 - *Segment Reporting* ("ASC 280") requires the disclosure of factors used to identify an enterprise's reportable segments. Our operations are organized and managed on the basis of cable systems within our geographic regions. Each cable system derives revenues from the delivery of similar products and services to a customer base that is also similar. Each cable system deploys similar technology to deliver our products and services, operates within a similar regulatory environment and has similar economic characteristics. Management evaluated the criteria for aggregation under ASC 280 and believes that we meet each of the respective criteria set forth. Accordingly, management has identified one reportable segment.

**Use of Estimates in the Preparation of the Consolidated Financial Statements.** The preparation of the Consolidated Financial Statements in conformity with GAAP requires management to make estimates and judgments that affect the amounts reported herein. Management bases its estimates and assumptions on historical experience and on various other factors that are believed to be reasonable under the circumstances. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be affected by changes in those estimates.

**Revenue Recognition.** Revenue is recognized when persuasive evidence of an arrangement exists, the fees are fixed or determinable, the product or service has been delivered and collectability is reasonably assured. Revenues are primarily derived from subscriber fees for data, video, and voice services, and from the sale of advertising.

The Company recognizes subscriber revenue as each service is provided. Revenue received from subscribers who purchase bundled services (e.g., the Company sells data, video and voice services to a customer) at a discounted rate is allocated to each product in a pro-rata manner based on the individual product's selling price on a standalone basis. The Company typically bills customers in advance on a monthly basis. The Company manages credit risk by screening applicants through the use of internal customer information, identification verification tools and credit bureau data. Various measures are used to collect outstanding amounts when a customer's account is delinquent, including termination of the customer's cable services. Installation revenue is recognized when the connection of the customer to the Company's cable system is completed, as installation revenue is less than the related direct selling costs.

The Company generally receives an allocation of scheduled advertising time as part of its distribution agreements with cable networks, which the Company sells to local, regional and national advertisers. The Company recognizes advertising revenue when the commercials are aired. In most cases, the available advertising time is sold by the Company's internal sales force. Since the Company is acting as a principal in these arrangements, the advertising that is sold is reported as revenue on a gross basis. In cases where advertising time is sold by agencies, the Company is not acting as a principal and the advertising sold is reported net of agency fees.

Under the terms of the Company's cable franchise agreements, the Company is generally required to pay to the franchising authority an amount based on the gross amount billed to the customer. The Company normally passes these fees to its customers and reports the fees on a gross basis as a component of revenue with the corresponding costs included in operating expense. The franchise authority assesses the Company directly for these fees and it is the Company's obligation to pay the fees. The amount of such fees recorded on a gross basis was \$14.2 million, \$15.7 million and \$16.7 million in 2016, 2015 and 2014, respectively.

**Concentrations of Credit Risk.** Financial instruments that potentially subject the Company to concentrations of credit risk are primarily cash and accounts receivable. Concentration of credit risk with respect to the Company's cash balance is limited. The Company maintains or invests its cash with highly qualified financial institutions. With respect to the Company's receivables, credit risk is limited due to the large number of customers, individually small balances and short payment terms.

Table of Contents

**Programming Costs.** The Company's programming costs are fees paid to license the programming that is distributed to video customers and are recorded in the period the services are provided. Programming costs are recorded based on the Company's contractual agreements with its programming vendors, which are generally multi-year agreements that provide for the Company to make payments to the programming vendors at agreed upon rates based on the number of subscribers to which the Company provides the programming service. From time to time, these agreements expire and programming continues to be distributed to customers while the parties negotiate new contractual terms. While payments are typically made under the prior agreement's terms, the amount of programming costs recorded during these interim periods is based on the Company's estimates of the ultimate contractual terms expected to be negotiated. Differences between actual amounts determined upon resolution of negotiations and amounts recorded during these interim periods are recorded in the period of resolution.

**Advertising Costs.** The Company expenses advertising costs as incurred. The total amount of such advertising expense recorded was \$25.9 million, \$22.5 million and \$22.9 million in 2016, 2015 and 2014, respectively.

**Cash and Cash Equivalents.** For financial reporting purposes, the Company considers all highly liquid investments with original maturities at purchase of three months or less to be cash equivalents. These investments are carried at cost, which approximates market value.

**Allowance for Doubtful Accounts.** Accounts receivable have been reduced by an allowance for amounts that may be uncollectible in the future. This estimated allowance is based primarily on the aging category, historical collection experience and management's evaluation of the financial condition of the customer. The Company generally considers an account past due or delinquent when a customer misses a scheduled payment. The Company writes off accounts receivable balances deemed uncollectible against the allowance for doubtful accounts generally when the account is turned over for collection to an outside collection agency.

**Fair Value Measurements.** Fair value measurements are determined based on the assumptions that a market participant would use in pricing an asset or liability based on a three-tiered hierarchy that draws a distinction between market participant assumptions based on (i) observable inputs, such as quoted prices in active markets (Level 1); (ii) inputs other than quoted prices in active markets that are observable either directly or indirectly (Level 2); and (iii) unobservable inputs that require the Company to use present value and other valuation techniques in the determination of fair value (Level 3). Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measure. The Company's assessment of the significance of a particular input to the fair value measurements requires judgment and may affect the valuation of the assets and liabilities being measured and their placement within the fair value hierarchy.

For assets that are measured using quoted prices in active markets, the total fair value is the published market price per unit multiplied by the number of units held, without consideration of transaction costs. Assets and liabilities that are measured using significant other observable inputs are primarily valued by reference to quoted prices of similar assets or liabilities in active markets, adjusted for any terms specific to that asset or liability.

The Company measures certain assets including goodwill, intangible assets and property, plant and equipment at fair value on a nonrecurring basis when they are deemed to be impaired. The fair value of these assets is determined with valuation techniques using the best information available and may include quoted market prices, market comparables and discounted cash flow models.

**Fair Value of Financial Instruments.** The carrying amounts reported in the Company's financial statements for cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities approximate fair value because of the short-term nature of these financial instruments.

**Property, Plant and Equipment.** Property, plant and equipment is recorded at cost. Replacements and major improvements are capitalized; maintenance and repairs are expensed as incurred. Depreciation is calculated using the straight-line method over the following estimated useful lives of the property, plant and equipment (in years):

Cable distribution systems	5 - 12
Customer premise equipment	5
Other equipment, vehicles and fixtures	3 - 10
Capitalized software	3 - 7
Buildings and improvements	20

The costs of leasehold improvements are amortized over the lesser of their useful lives or the terms of the respective leases.

The Company capitalizes certain internal and external costs incurred to acquire or develop internal-use software, including costs associated with coding, software configuration, upgrades and enhancements.

Table of Contents

The Company capitalizes costs associated with the construction of cable transmission and distribution facilities and new cable service installations. Costs include all direct labor and materials, as well as certain indirect costs. The cost of subsequent disconnects and reconnects are expensed as they are incurred.

**Evaluation of Long-Lived Assets.** The recoverability of property, plant and equipment and amortized intangible assets is assessed whenever adverse events or changes in circumstances indicate that recorded values may not be recoverable. A long-lived asset is considered to not be recoverable when the undiscounted estimated future cash flows are less than the asset's recorded value. An impairment charge is measured based on estimated fair market value, determined primarily using estimated future cash flows on a discounted basis. Losses on long-lived assets to be disposed of are determined in a similar manner, but the fair market value would be reduced for estimated costs to dispose.

**Goodwill and Indefinite-Lived Intangible Assets.** Goodwill is the excess of purchase price over the fair value of identified net assets of businesses acquired. The Company's intangible assets with an indefinite life are principally from franchise agreements, as the Company expects its cable franchise agreements to provide the Company with substantial benefit for a period that extends beyond the foreseeable horizon, and the Company historically has obtained renewals and extensions of such agreements for nominal costs and without any material modifications to the agreements.

The Company reviews goodwill and indefinite-lived intangible assets at least annually, as of November 30, for possible impairment. Goodwill and indefinite-lived intangible assets are reviewed for possible impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of the reporting unit or indefinite-lived intangible asset below its carrying value. The Company tests its goodwill at the reporting unit level, which is an operating segment or one level below an operating segment. The reporting unit level is at a regional basis. In reviewing the carrying value of indefinite-lived intangible assets, the Company aggregates its cable systems on a regional basis. The Company initially assesses qualitative factors to determine if it is necessary to perform the two-step goodwill impairment review or indefinite-lived intangible asset quantitative impairment review. The Company reviews the goodwill for impairment using the two-step process and the indefinite-lived intangible assets using the quantitative process if, based on its assessment of the qualitative factors, it determines that it is more likely than not that the fair value of a reporting unit or indefinite-lived intangible asset is less than its carrying value, or if it decides to bypass the qualitative assessment. The Company reviews the carrying value of goodwill and indefinite-lived intangible assets utilizing a discounted cash flow model, and, where appropriate, a market value approach is also utilized to supplement the discounted cash flow model. The Company makes assumptions regarding estimated future cash flows, discount rates, long-term growth rates and market values to determine each reporting unit's and indefinite-lived intangible asset's estimated fair value. If these estimates or related assumptions change in the future, the Company may be required to record impairment charges.

**Pension and Other Postretirement Benefits.** The Company maintains various pension and incentive savings plans. The Company recognizes the overfunded or underfunded status of the defined benefit SERP (as defined in Note 14) as an asset or liability in its statement of financial position and recognizes change in that funded status in the year in which the changes occur through comprehensive income. The Company measures changes in the funded status of its plans using the projected unit credit method and several actuarial assumptions, the most significant of which are the discount rate, the long-term rate of asset return and the rate of compensation increase. The Company uses a measurement date of December 31 for its pension and other postretirement benefit plans.

**Self-Insurance.** The Company uses a combination of insurance and self-insurance for a number of risks, including claims related to employee medical and dental care, disability benefits, workers' compensation, general liability, property damage and business interruption. Liabilities associated with these plans are estimated based on, among other things, the Company's historical claims experience, severity factors and other actuarial assumptions. Accruals for expected loss are based on estimates, and, while the Company believes that the amounts accrued are adequate, the ultimate loss may differ from the amounts provided.

**Equity-Based Compensation.** The Company measures compensation expense for awards settled in shares based on the grant date fair value of the award. The Company measures compensation expense for awards settled in cash, or that may be settled in cash, based on the fair value at each reporting date. The Company recognizes the expense over the requisite service period, which is generally the vesting period of the award.

**Income Taxes.** During the periods presented, the Company's income taxes have been prepared on a separate return basis as if the Company was a stand-alone entity. Prior to the spin-off, the Company's operations were historically included in GHC's consolidated U.S. Federal and certain state tax returns. The results from being included in the consolidated tax returns were included in Additional GHC investment (deficit) for the applicable periods. The Company did not maintain taxes payable to/from GHC and was deemed to settle the annual current tax balances immediately with the legal tax-paying entities in the respective jurisdictions. These settlements were reflected as net transfer to/from GHC within Additional GHC investment (deficit).

F-10

Table of Contents

The Company accounts for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statements and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

The Company records net deferred tax assets to the extent that it believes these assets will more likely than not be realized. In making such determination, the Company considers all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent financial operations. This evaluation is made on an ongoing basis. In the event the Company were to determine that it was not able to realize net deferred income tax assets in the future, the Company would record a valuation allowance, which would increase the provision for income taxes.

The Company recognizes a tax benefit from an uncertain tax position when it is more likely than not that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes, based on the technical merits. The Company records a liability for the difference between the benefit recognized and measured for financial statement purposes and the tax position taken or expected to be taken on the tax return. Changes in the estimate are recorded in the period in which such determination is made.

**Asset Retirement Obligations.** Certain of the Company's cable franchise agreements and lease agreements contain provisions requiring the Company to restore facilities or remove property in the event that the franchise or lease agreement is not renewed. The Company expects to continually renew its cable franchise agreements and therefore cannot reasonably estimate any liabilities associated with such agreements. A remote possibility exists that franchise agreements could be terminated unexpectedly, which could result in the Company incurring significant expense in complying with restoration or removal provisions. The Company does not have any significant liabilities related to asset retirements recorded in the financial statements.

**Recently Adopted and Issued Accounting Pronouncements.** In May 2014, the Financial Accounting Standards Board (the "FASB") issued comprehensive new guidance that supersedes all existing revenue recognition guidance. The new guidance requires revenue to be recognized when the Company transfers promised goods or services to customers in an amount that reflects the consideration to which the Company expects to be entitled in exchange for those goods or services. The new guidance also significantly expands the disclosure requirements for revenue recognition. This guidance, as amended, is effective for interim and fiscal years beginning after December 15, 2017. Early adoption is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. The standard permits two implementation approaches, one requiring retrospective application of the new guidance with a restatement of prior years and one requiring prospective application of the new guidance with disclosure of results under the old guidance. The Company is in the process of evaluating the impact of this new guidance on its financial statements.

In August 2014, the FASB issued new guidance that requires management to assess the Company's ability to continue as a going concern and to provide related disclosures in certain circumstances. This guidance is effective for interim and fiscal years ending after December 15, 2016. The adoption of this guidance did not have a significant impact on the Company's financial statements.

In April 2015, the FASB issued new guidance to simplify the presentation of debt issuance costs. This guidance requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by this guidance. The new guidance should be applied on a full retrospective basis to all periods presented. This guidance is effective for interim and fiscal years beginning after December 15, 2015. In accordance with the provisions of the new guidance, the Company has recorded unamortized debt issuance costs net of the long-term debt liability in the accompanying Consolidated Balance Sheets as of December 31, 2016 and 2015. This resulted in a reclassification of deferred financing costs, which caused a reduction of \$9.8 million to Long-term debt, \$1.6 million to Current Assets and \$8.2 million to Other assets in the accompanying Consolidated Balance Sheet as of December 31, 2015.

Table of Contents

In September 2015, the FASB issued new guidance requiring an acquirer to retrospectively adjust provisional amounts reflected in its financial statements arising from a business combination during the measurement period. To simplify the accounting for adjustments made to provisional amounts, the guidance requires that the acquirer reflect adjustments to provisional amounts that are identified during the measurement period in the financial statements for the reporting period in which the adjustment amount is determined. The acquirer is required to also record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the adjustment had been completed at the acquisition date. In addition, an entity is required to present separately on the face of the income statement or disclose in the notes to the financial statements the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. This guidance is effective for fiscal years beginning after December 15, 2016 and interim periods within fiscal years beginning after December 15, 2017. The amendments in this guidance should be applied prospectively to adjustments to provisional amounts that occur after the effective date of this guidance. The Company does not expect this guidance to have an impact on its financial statements unless an acquisition is made.

In November 2015, the FASB issued new guidance that eliminates the requirement to bifurcate deferred taxes between current and noncurrent on the balance sheet and requires that deferred tax liabilities and assets be classified as noncurrent on the balance sheet. This guidance can be either applied prospectively to all deferred tax liabilities and assets or retrospectively to all periods presented and early adoption is permitted. We early-adopted this guidance on a prospective basis as of December 31, 2015, and the Consolidated Balance Sheet as of December 31, 2015 reflects the revised classification of current deferred tax assets and liabilities as noncurrent. Adoption of this guidance resulted in an immaterial reclassification between current deferred tax assets and noncurrent deferred tax assets as of December 31, 2015. There is no other impact on the financial statements due to early-adopting this guidance.

In February 2016, the FASB issued new guidance that requires a lessee to record a right-of-use asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. This guidance is effective for interim and fiscal years beginning after December 15, 2018. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is in the process of evaluating the impact of its pending adoption of this new guidance on its financial statements.

In March 2016, the FASB issued new guidance affecting several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. This guidance is effective for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. The Company does not expect this guidance to have a significant impact on its financial statements.

In August 2016, the FASB issued new guidance affecting the classification of certain cash receipts and cash payments, including debt prepayments or debt extinguishments costs, settlement of zero-coupon debt instruments, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims and corporate-owned life insurance policies, distributions received from equity method investees, beneficial interests in securitization transactions, and separately identifiable cash flows and application of the predominance principle. This guidance is effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years, with early adoption permitted. If an entity early adopts this guidance in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. The Company does not expect this guidance to have a significant impact on its financial statements.

### 3. REVENUES

The Company's revenues by product line were as follows (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Residential			
Data	\$ 344,184	\$ 294,486	\$ 265,718
Video	294,781	332,716	361,668
Voice	42,949	50,148	62,396
Business services	100,311	88,741	76,829
Advertising sales	27,496	31,034	35,362
Other	9,904	10,141	12,839

**Total revenues**

\$ 819,625   \$ 807,266   \$ 814,812

F-12

Table of Contents

The amount of franchise fees recorded on a gross basis was \$14.2 million, \$15.7 million and \$16.7 million for 2016, 2015, and 2014, respectively.

**4. ACCOUNTS RECEIVABLE, ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**

Accounts receivable consisted of the following:

<u>(in thousands)</u>	As of December 31,	
	2016	2015
Accounts receivable, net	\$ 28,924	\$ 30,715
Other receivables <sup>(1)</sup>	8,149	3,990
Total accounts receivable, net	<u>\$ 37,073</u>	<u>\$ 34,705</u>

<sup>(1)</sup> Includes \$4.5 million of federal and state income tax overpayments.

The change in allowance for doubtful accounts was as follows:

<u>(in thousands)</u>	Allowance for Doubtful Accounts			
	Balance at Beginning of Period	Additions – Charged to Costs and Expenses	Deductions	Balance at End of Period
2016	\$ 864	\$ 2,839	\$ (2,675)	\$ 1,028
2015	\$ 621	\$ 3,294	\$ (3,051)	\$ 864
2014	\$ 1,207	\$ 3,907	\$ (4,493)	\$ 621

Accounts payable and accrued liabilities consisted of the following:

<u>(in thousands)</u>	As of December 31,	
	2016	2015
Accounts payable	\$ 17,079	\$ 30,925
Programming costs	13,787	13,451
Accrued compensation and related benefits	18,084	16,146
Accrued sales and other operating taxes	4,747	5,672
Cash overdrafts	7,980	8,703
Franchise fees	4,196	4,760
Subscriber deposits	5,289	4,491
Other accrued expenses	11,541	11,140
Total accounts payable and accrued liabilities	<u>\$ 82,703</u>	<u>\$ 95,288</u>

**5. PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment consisted of the following (in thousands):

	As of December 31,	
	2016	2015
Cable distribution systems	\$ 1,048,790	\$ 1,017,250
Customer premise equipment	181,852	259,678
Other equipment and fixtures	359,957	317,696
Buildings and leasehold improvements	88,592	84,503
Capitalized software	83,815	75,027
Construction in progress	64,822	89,742
Land	9,612	9,482
	<u>1,837,440</u>	<u>1,853,378</u>
Less accumulated depreciation	<u>(1,217,819)</u>	<u>(1,212,811)</u>
Total property, plant and equipment, net	<u>\$ 619,621</u>	<u>\$ 640,567</u>



Table of Contents

The cable industry is capital intensive, and a significant portion of our resources is spent on capital activities associated with extending, rebuilding, and upgrading our cable network. For the years ended December 31, 2016, 2015 and 2014, cash paid for property, plant and equipment was \$141.7 million, \$156.1 million and \$177.4 million, respectively.

Depreciation and amortization expense was \$142.2 million, \$140.6 million and \$134.2 million in 2016, 2015 and 2014, respectively.

The Company's previous headquarters building and adjoining property were held for sale at December 31, 2016. The property's carrying value of \$8.1 million was included in Other assets at December 31, 2016. In January 2017, we sold certain of these assets for \$10.5 million. We expect to complete the sale of the remaining assets within the next two years.

## 6. GOODWILL AND INTANGIBLE ASSETS

The carrying amount of goodwill at December 31, 2016 and 2015 was \$84.9 million and \$85.5 million, respectively. Historically, the Company has not recorded any impairment of goodwill. During 2016, we sold the assets of a cable system, which resulted in disposed goodwill of \$0.6 million.

Intangible assets consisted of the following (in thousands):

	<u>December 31, 2016</u>			
	<u>Useful Life Range (years)</u>	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>
<b>Amortized Intangible Assets</b>				
Cable franchise renewals and access rights	1 - 25	4,138	3,794	344
<b>Indefinite-Lived Intangible Assets</b>				
Franchise agreements		<u>\$ 497,136</u>		

	<u>December 31, 2015</u>			
	<u>Useful Life Range (years)</u>	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>
<b>Amortized Intangible Assets</b>				
Cable franchise renewals and access rights	1 - 25	4,127	3,678	449
<b>Indefinite-Lived Intangible Assets</b>				
Franchise agreements		<u>\$ 496,321</u>		

Amortization of intangible assets was less than \$0.1 million, \$0.1 million and \$0.2 million in 2016, 2015 and 2014, respectively. Amortization of intangible assets is estimated to be approximately \$0.1 million in each of the next three years through 2019 and less than \$0.1 million thereafter.

In July 2014, the Company sold wireless spectrum licenses that were purchased in 2006 and recorded a pre-tax non-operating gain of \$75.2 million included in Other income (expense), net in the Consolidated Statements of Operations and Comprehensive Income.

## 7. LONG-TERM DEBT

**5.750% Senior Unsecured Notes Due 2022.** On June 17, 2015, the Company issued \$450 million aggregate principal amount of 5.750% senior unsecured notes due 2022 (the "Notes"). The Company used the proceeds from the Notes offering to pay a special one-time cash dividend to GHC of \$450 million on June 29, 2015 in connection with the spin-off.

The Notes have not been, and will not be, registered under the Securities Act of 1933, as amended (the "Securities Act"), or the securities laws of any state or other jurisdiction and may not be offered or sold in the United States absent registration or an applicable exemption from the registration requirements of the Securities Act and any other applicable securities laws. The Notes were offered in the United States only to persons reasonably believed to be qualified institutional buyers in reliance on the exemption

from registration set forth in Rule 144A under the Securities Act and outside the United States to non-U.S. persons in reliance on the exemption from registration set forth in Regulation S under the Securities Act.

F-14

Table of Contents

The Notes were issued pursuant to an indenture (the "Indenture"), dated as of June 17, 2015, among the Company, the Guarantors (as defined below) and the Bank of New York Mellon Trust Company, N.A., as trustee (the "Trustee").

The Notes mature on June 15, 2022 and bear interest at a rate of 5.750% per year. Interest on the Notes is payable on June 15 and December 15 of each year, beginning on December 15, 2015. The Notes are jointly and severally guaranteed (the "Guarantees") on a senior unsecured basis by each of the Company's existing and future domestic subsidiaries that initially guaranteed (the "Guarantors") the Senior Credit Facilities (as defined below). The Notes are unsecured and senior obligations of the Company. The Guarantees are unsecured and senior obligations of the Guarantors.

At the option of the Company, the Notes are redeemable, in whole or in part, at any time prior to June 15, 2018 at a price equal to 100% of the aggregate principal amount of the Notes plus accrued and unpaid interest, if any, to, but excluding, the redemption date plus a "make-whole" premium. The Company may also redeem the Notes, in whole or in part, at any time on or after June 15, 2018 at the redemption prices specified in the Indenture, plus accrued and unpaid interest, if any, to, but excluding, the redemption date.

Additionally, at any time prior to June 15, 2018, the Company may redeem up to 35% of the aggregate principal amount of the Notes with the net cash proceeds from certain equity offerings at a price equal to 105.75% of the principal amount of the Notes, plus accrued and unpaid interest, if any, to, but excluding, the redemption date.

The Indenture includes certain covenants relating to debt incurrence, liens, restricted payments, assets sales and transactions with affiliates, changes in control and mergers or sales of all or substantially all of the Company's assets. The Indenture also provides for customary events of default (subject, in certain cases, to customary grace periods), which include nonpayment on the Notes, breach of covenants in the Indenture, payment defaults or acceleration of other indebtedness over a specified threshold, failure to pay certain judgments over a specified threshold and certain events of bankruptcy and insolvency. Generally, if an event of default occurs, the Trustee under the Indenture or holders of at least 25% of the aggregate principal amount of the then outstanding Notes may declare the principal of, and accrued but unpaid interest, if any, on the then outstanding Notes to be due and payable immediately.

**Senior Credit Facilities Due 2020.** On June 30, 2015, the Company entered into a Credit Agreement (the "Credit Agreement") among the Company, as borrower, the lenders party thereto, JPMorgan Chase Bank, N.A., as administrative agent, and the other agents party thereto. The Credit Agreement provides for a five-year revolving credit facility in an aggregate amount of \$200 million (the "Revolving Credit Facility") and a five-year term loan facility in an aggregate amount of \$100 million (the "Term Loan Facility" and, together with the Revolving Credit Facility, the "Senior Credit Facilities"). Concurrently with its entry into the Credit Agreement, the Company borrowed the full amount of the Term Loan Facility (the "Term Loan").

The obligations under the Senior Credit Facilities are obligations of the Company and are guaranteed by the Subsidiary. The obligations under the Senior Credit Facilities are secured, subject to certain exceptions, by substantially all of the assets of the Company and the Subsidiary.

Borrowings under the Senior Credit Facilities bear interest, at the Company's option, at a rate per annum determined by reference to either the London Interbank Offered Rate ("LIBOR") or an adjusted base rate, in each case plus an applicable interest rate margin. The applicable interest rate margin with respect to LIBOR borrowings is a rate per annum between 1.50% and 2.25% and the applicable interest rate margin with respect to adjusted base rate borrowings is a rate per annum between 0.50% and 1.25%, in each case determined on a quarterly basis by reference to a pricing grid based upon the Company's total net leverage ratio. As of December 31, 2016, borrowings under the Senior Credit Facilities bore interest at a rate of 2.34% per annum. In addition, the Company is required to pay commitment fees on any unused portion of the Revolving Credit Facility at a rate between 0.25% per annum and 0.40% per annum, determined by reference to the pricing grid. As of December 31, 2016, the commitment fee accrues at a rate of 0.25% per annum. Outstanding borrowings under the Term Loan Facility were \$95.0 million at December 31, 2016. The Company had \$197.2 million available for borrowing under the Revolving Credit Facility at December 31, 2016.

The Senior Credit Facilities may be prepaid at any time without premium. The Term Loan Facility amortizes in equal quarterly installments at a rate of 2.5% per annum in the first year after funding, 5.0% per annum in the second year after funding, 7.5% per annum in the third year after funding, 10.0% per annum in the fourth year after funding and 15.0% per annum in the fifth year after funding, with the outstanding balance of the Term Loan Facility to be paid on the fifth anniversary of funding.

Table of Contents

The Revolving Credit Facility also gives the Company the ability to issue letters of credit, which reduce the amount available for borrowing under the Revolving Credit Facility. Letter of credit issuances under the Revolving Credit Facility of \$2.8 million at December 31, 2016 were held for the benefit of certain general and liability insurance matters and bore interest at a rate of 1.625% per annum.

The Company may, subject to the terms and conditions of the Credit Agreement, obtain additional credit facilities of up to \$300 million under the Credit Agreement pursuant to an uncommitted incremental facility.

The Credit Agreement contains customary representations, warranties and affirmative and negative covenants, including limitations on indebtedness, liens, restricted payments, prepayments of certain indebtedness, investments, dispositions of assets, restrictions on subsidiary distributions and negative pledge clauses, fundamental changes, transactions with affiliates and amendments to organizational documents. The Credit Agreement also requires the Company to maintain specified ratios of total net leverage and first lien net leverage to consolidated operating cash flow. The Credit Agreement also contains customary events of default, including non-payment of principal, interest, fees or other amounts, material inaccuracy of any representation or warranty, failure to observe or perform any covenant, default in respect of other material debt of the Company and its restricted subsidiaries, bankruptcy or insolvency, the entry against the Company or any of its restricted subsidiaries of a material judgment, the occurrence of certain ERISA events, impairment of the loan documentation and the occurrence of a change of control.

The Company was in compliance with all debt covenants as of December 31, 2016.

Long-term debt consisted of the following (in thousands):

	<b>As of December 31,</b>	
	<b>2016</b>	<b>2015</b>
Senior Unsecured Notes	\$ 450,000	\$ 450,000
Senior Credit Facilities	95,000	98,750
Capital lease obligation	284	301
Total debt	<u>545,284</u>	<u>549,051</u>
Less unamortized debt issuance costs	(8,148)	(9,790)
Less current portion long-term debt	(6,250)	(3,750)
Total long-term debt	<u>\$ 530,886</u>	<u>\$ 535,511</u>

The Company recorded \$1.6 million and \$0.9 million of debt issuance costs for the years ended December 31, 2016 and 2015, respectively. These amounts are reflected in Interest expense in the Consolidated Statements of Operations and Comprehensive Income.

As of December 31, 2016, the future maturities of long-term debt were as follows (in thousands):

	<b>Amount</b>
2017	\$ 6,250
2018	8,767
2019	12,517
2020	67,517
2021	17
Thereafter	450,216
Total	<u>\$ 545,284</u>

On February 13, 2017, the Company entered into an amendment to the Credit Agreement to permit, among other things, the incurrence of the \$650 million of senior secured loans expected to be used to finance the acquisition of NewWave and the other transactions contemplated by the Merger Agreement (as defined in Note 19).

Table of Contents**8. INCOME TAXES**

The provision for income taxes consisted of the following:

(in thousands)

**Year Ended December 31, 2016**

U.S. Federal

State and Local

	<u>Current</u>	<u>Deferred</u>	<u>Total</u>
\$	55,759	(1,012)	54,747
	8,812	609	9,421
\$	<u>64,571</u>	<u>(403)</u>	<u>64,168</u>

**Year Ended December 31, 2015**

U.S. Federal

State and Local

\$	60,201	(12,163)	\$ 48,038
	7,468	881	8,349
\$	<u>67,669</u>	<u>(11,282)</u>	<u>\$ 56,387</u>

**Year Ended December 31, 2014**

U.S. Federal

State and Local

\$	73,636	4,143	\$ 77,779
	12,788	133	12,921
\$	<u>86,424</u>	<u>4,276</u>	<u>\$ 90,700</u>

The provision for income taxes exceeded the amount of income tax determined by applying the U.S. Federal statutory rate of 35% to income before taxes as a result of the following:

(in thousands)

U.S. Federal taxes at statutory rate

State and local taxes, net of U.S. Federal tax

Other, net

**Provision for Income Taxes**

	<u>Year Ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
\$	57,087	\$ 50,897	\$ 83,303
	6,124	5,427	8,399
	957	63	(1,002)
\$	<u>64,168</u>	<u>\$ 56,387</u>	<u>\$ 90,700</u>

Deferred income taxes consisted of the following:

(in thousands)

Other benefit obligations

Equity-based compensation

Accounts receivable

Other

**Deferred Tax Assets**

Property, plant and equipment

Goodwill and other intangible assets

**Deferred Tax Liabilities****Deferred Income Tax Liabilities**

	<u>As of December 31,</u>	
	<u>2016</u>	<u>2015</u>
\$	9,118	\$ 9,396
	5,041	1,868
	391	327
	555	839
	<u>15,105</u>	<u>12,430</u>
	125,134	122,789
	166,268	166,268
	<u>291,402</u>	<u>289,057</u>
\$	<u>276,297</u>	<u>\$ 276,627</u>

The Company has not established valuation allowances against any U.S. Federal or state deferred tax assets.

Before the spin-off, the Company was included in consolidated U.S. Federal and Arizona corporate income tax returns filed by GHC, and also filed in various other state and local governmental jurisdictions. The U.S. Federal tax return filing is considered the only major tax jurisdiction. The statute of limitations has expired on all GHC consolidated U.S. Federal corporate income tax returns filed through 2012, with the exception of an issue that does not involve the Company. The Internal Revenue Service ("IRS") is currently examining the 2013 GHC consolidated U.S. Corporation Income Tax Return.

The Company endeavors to comply with tax laws and regulations where it does business, but cannot guarantee that, if challenged, the Company's interpretation of all relevant tax laws and regulations will prevail and that all tax benefits recorded in the financial statements will ultimately be recognized in full. The Company has taken reasonable efforts to address uncertain tax positions and has determined that there are no material transactions and no material tax positions taken by the Company that would fail to meet the more-likely-than-not threshold for recognizing transactions or tax positions in the financial statements. Accordingly, the Company has

not recorded a reserve for uncertain tax positions in the financial statements, and the Company does not expect any significant tax increase or decrease to occur within the next 12 months with respect to any transactions or tax positions taken and reflected in the financial statements. In making these determinations, the Company presumes that taxing authorities pursuing examinations of the Company's compliance with tax law filing requirements will have full knowledge of all relevant information, and, if necessary, the Company will pursue resolution of disputed tax positions by appeals or litigation. The Company classifies interest and penalties, if applicable, associated with any uncertain tax positions as a component of Interest expense in its Consolidated Statements of Operations and Comprehensive Income.

Table of Contents**9. FAIR VALUE MEASUREMENTS**

The Company's deferred compensation liabilities were \$18.2 million and \$18.3 million at December 31, 2016 and 2015, respectively. These liabilities are included in Accounts payable and accrued liabilities and Accrued compensation and related benefits in the Consolidated Balance Sheets. These liabilities represent the market value of a participant's balance in a notional investment account that is comprised primarily of mutual funds, which is based on observable market prices. However, since the deferred compensation obligations are not exchanged in an active market, they are classified as Level 2 in the fair value hierarchy. Realized and unrealized gains (losses) on deferred compensation are included in operating income.

The carrying amounts and fair values of the Company's long-term debt, including current portion, money market and commercial paper investments as of December 31, 2016 were as follows (in thousands):

	December 31, 2016	
	Carrying Amount	Fair Value
<b>Assets:</b>		
Money market investments	\$ 47,527	\$ 47,527
Commercial paper	\$ 79,918	\$ 79,898
<b>Long-term debt, including current portion</b>		
Notes	\$ 450,000	\$ 463,500
Term Loan	\$ 95,000	\$ 95,000

Money market investments are included in cash and cash equivalents in the Consolidated Balance Sheets. Commercial paper investments with original maturities of 90 days or less are also included in cash and cash equivalents. These investments are primarily held in U.S. Treasury securities and registered money market funds. These investments were valued using a market approach based on the quoted market prices of the commercial paper (Level 2), or inputs that include quoted market prices for investments similar to the money market investments (Level 1). The fair value of the Notes was estimated based on market prices in active markets (Level 2). The fair value of the Term Loan was estimated based on discounting the remaining principal and interest payments using current market rates for similar debt (Level 2).

**10. TREASURY STOCK**

**Share Repurchase Program.** On July 1, 2015, the Company's board of directors (the "Board") authorized up to \$250 million of share repurchases (subject to a total cap of 600,000 shares of Company common stock). Purchases under the stock repurchase program may be made from time to time on the open market and in privately negotiated transactions. The size and timing of these purchases will be based on a number of factors, including price and business and market conditions. As of December 31, 2016, the Company repurchased 164,933 shares at an aggregate cost of \$72.7 million. During 2016, the Company repurchased 126,797 shares at an aggregate cost of \$56.4 million.

**Restricted Stock Tax Withholding.** Treasury stock is recorded at cost and is presented as a reduction of stockholders' equity in the Consolidated Financial Statements. Shares of Company common stock, with a fair market value equal to the applicable statutory minimum amount of the employee withholding taxes due, are withheld by the Company upon the vesting of restricted stock to pay the applicable statutory minimum amount of employee withholding taxes and are considered common stock repurchases. The Company then pays the applicable statutory minimum amount of withholding taxes in cash. The amount remitted in the year ended December 31, 2016 was \$2.2 million for which the Company withheld 3,616 shares of common stock. Treasury shares of 179,676 at December 31, 2016 includes the aforementioned shares withheld for withholding tax.

**11. EQUITY-BASED COMPENSATION**

Through June 30, 2015, certain of the Company's employees participated in an equity-based incentive compensation plan maintained by GHC for the benefit of certain officers, directors and employees. Equity-based awards issued to employees included non-qualified stock options and restricted stock awards. These compensation costs are recognized within selling, general and administrative expenses.

Table of Contents

On June 5, 2015, the Board adopted the Cable One, Inc. 2015 Omnibus Incentive Compensation Plan (the "2015 Plan"), which became effective July 1, 2015. The 2015 Plan is designed to promote the interests of the Company and its stockholders by providing the employees and directors of the Company with incentives and rewards to encourage them to continue in the service of the Company and with a proprietary interest in pursuing the long-term growth, profitability and financial success of the Company. Any of the directors, officers and employees of the Company and its affiliates are eligible to be granted one or more of the following types of awards under the 2015 Plan: (1) incentive stock options, (2) non-qualified stock options, (3) restricted stock awards, (4) stock appreciation rights ("SARs"), (5) restricted stock units ("RSUs"), (6) cash-based awards, (7) performance-based awards, (8) dividend equivalent rights and (9) other stock-based awards, including, without limitation, performance stock units and deferred stock units. The 2015 Plan includes the authority to grant awards that are intended to qualify as "qualified performance-based compensation" under Section 162(m) of the Internal Revenue Code of 1986, as amended. Unless the 2015 Plan is sooner terminated by the Board, no awards may be granted under the 2015 Plan after the tenth anniversary of its effective date.

The 2015 Plan provides that, subject to certain adjustments for certain corporate events, the maximum number of shares of Company common stock that may be issued under the 2015 Plan is equal to 600,000, and no more than 400,000 shares may be issued pursuant to incentive stock options.

**Restricted Stock Awards.** The Company has granted restricted shares of Company common stock subject to service-based and performance-based vesting conditions under the 2015 Plan to employees of the Company (the "Restricted Shares"). The Restricted Shares generally cliff-vest on the three-year anniversary of the grant date, except in the case of awards made to individuals (i) whose equity awards issued by GHC were forfeited in connection with the spin-off (the "Replacement Shares"), which Replacement Shares vested on December 12, 2016 (with certain exceptions as provided in the applicable award agreement), or (ii) who did not receive an equity award from GHC in 2015 in anticipation of the spin-off (the "Staking Shares"), which Staking Shares are scheduled to cliff-vest on January 2, 2018. For Restricted Shares granted in 2015, the performance goals, which have been met, related primarily to year over year growth in Adjusted EBITDA less capital expenditures. For performance-based Restricted Shares granted in 2016, the performance goals relate primarily to year over year growth in Adjusted EBITDA and to capital expenditures as a percentage of total revenues. The Restricted Shares are subject to the terms and conditions of the 2015 Plan and will otherwise be subject to the terms and conditions of the applicable award agreement.

The compensation arrangements for the Company's non-employee directors under the 2015 Plan provide that each non-employee director is entitled to an annual retainer of \$150,000, plus an additional annual retainer of \$15,000 for each non-employee director who serves as a committee chair or as lead independent director. Each such retainer will be provided in the form of RSUs. Such RSUs will generally be granted on the date of the Company's annual stockholders' meeting and will vest on the first anniversary of the grant date, subject to the director's continued service through such vesting date. Settlement of such RSUs will be in the form of one share of the Company's common stock and will follow vesting, unless the director has previously elected to defer such settlement until his or her separation from service from the Board. As of December 31, 2016, 2,206 RSUs were vested and deferred.

The Restricted Shares and RSUs are collectively referred to as "restricted stock" and a summary of the restricted stock is as follows:

	<u>Restricted Stock</u>	<u>Weighted Average Grant Date Fair Value Per Share</u>
Unvested as of December 31, 2014	-	\$ -
Granted	39,744	\$ 383.18
Unvested as of December 31, 2015	39,744	\$ 383.18
Granted	10,369	\$ 454.75
Forfeited	(1,343)	\$ 389.33
Vested	(10,345)	\$ 383.61
Unvested as of December 31, 2016	<u>38,425</u>	\$ 402.13
Vested and unissued as of December 31, 2016	<u>2,206</u>	\$ 414.62

Table of Contents

Compensation expense associated with unvested restricted stock is recognized on a straight-line basis over the vesting period. The expense recognized each period is dependent upon our estimate of the number of shares that will ultimately vest. Equity-based compensation expense for restricted stock was \$9.4 million and \$3.9 million for 2016 and 2015, respectively. At December 31, 2016, there was \$8.3 million of unrecognized compensation expense related to restricted stock, which is expected to be recognized over a weighted average period of 1.1 years.

**Stock Appreciation Rights.** The Company has granted SARs under the 2015 Plan to certain executives and other employees of the Company. The SARs are scheduled to vest in four equal ratable installments beginning on the first anniversary of the grant date (generally subject to the holder's continued employment with the Company through the applicable vesting date). The SARs are subject to the terms and conditions of the 2015 Plan and will otherwise be subject to the terms and conditions of the applicable award agreement.

A summary of SAR activity is as follows:

	Stock Appreciation Rights	Weighted Average Exercise Price	Weighted Average Fair Value	Aggregate Intrinsic Value (in millions)	Weighted Average Remaining Contractual Term (in years)
Outstanding as of December 31, 2014	-	\$ -	\$ -	\$ -	-
Granted	135,600	\$ 422.31	\$ 87.22	\$ -	-
Outstanding as of December 31, 2015	135,600	\$ 422.31	\$ 87.22	\$ 1.5	9.7
Granted	6,100	\$ 522.50	\$ 106.15	\$ -	9.5
Forfeited	(5,700)	\$ 422.31	\$ 87.22	\$ -	-
Outstanding as of December 31, 2016	136,000	\$ 426.80	\$ 88.07	\$ 26.5	8.7
Vested and exercisable as of December 31, 2016	32,475	\$ 422.31	\$ 87.22	\$ 6.5	8.7

The fair value of the SARs was measured based on the Black-Scholes model. The inputs used in the fair value measurement for 2016 were as follows:

	2016	2015
Expected volatility	21.63%	24.00%
Risk-free interest rate	1.39%	1.75%
Expected term (in years)	6.25	6.25
Expected dividend yield	1.16%	1.45%

Compensation expense associated with unvested SARs is recognized on a straight-line basis over the vesting period. The expense recognized each period is dependent upon our estimate of the number of SARs that will ultimately vest. Equity-based compensation expense for these SARs was \$2.9 million and \$1.0 million for 2016 and 2015, respectively. At December 31, 2016, there was \$8.1 million of unrecognized compensation expense related to the SARs, which is expected to be recognized over a weighted average period of 1.7 years.

The Black-Scholes model used to estimate the fair value of our SARs requires the input of highly subjective assumptions, including the fair value of the underlying common stock, the expected volatility of the price of our common stock, risk-free interest rates, the expected term of the SAR and the expected dividend yield of our common stock. These estimates involve inherent uncertainties and the application of management's judgment. If factors change and different assumptions are used, our equity-based compensation expense could be materially different in the future. These assumptions are estimated as follows:

- **Fair Value** — Our common stock is valued by reference to the publicly-traded price of our common stock.
- **Expected Volatility** — Prior to the spin-off, we did not have a history of market prices for our common stock and since the spin-off, we do not have what we consider a sufficiently active and readily traded market for our common stock to use historical market prices for our common stock to estimate volatility. Accordingly, we estimate the expected stock price volatility for our common stock by using leverage-adjusted average volatilities of industry peers based on daily price observations over a period equivalent to the expected term of the SAR grants. Industry peers consist of other public companies in the cable, satellite, and integrated telecommunication services industry similar in size, stage of life cycle and

financial leverage. We intend to continue to consistently apply this process using the same or similar public companies until a sufficient amount of historical information regarding the volatility of our own common stock share price becomes available.

- **Risk-Free Interest Rate** — The risk-free interest rate assumption is based on observed interest rates appropriate for the expected terms of our awards. The risk-free interest rate assumption is based on the yields of U.S. Treasury securities with maturities similar to the expected term of the SARs for each SAR group.

Table of Contents

- **Expected Term** — The expected term represents the period that our stock-based awards are expected to be outstanding. Prior to the spin-off, we did not have stock-based awards specific to Cable One and therefore did not have a history of the period that our stock-based awards are expected to be outstanding. Accordingly, the expected terms of the awards are based on a simplified method which defines the term as the average of the contractual term of the SARs and the weighted-average vesting period for all open tranches.
- **Expected Dividend Yield** — We expect to pay a dividend in the future and, as such, the weighted average expected dividend yield rate used in the valuation was 1.16%.

In addition to the assumptions used in the Black-Scholes model, the amount of SAR expense we recognize in our Consolidated Statements of Operations and Comprehensive Income includes an estimate of SAR forfeitures. We estimate our forfeiture rate based on an analysis of our actual forfeitures and will continue to evaluate the appropriateness of the forfeiture rate based on actual forfeiture experience, analysis of employee turnover and other factors. Changes in the estimated forfeiture rate can have a significant impact on our equity-based compensation expense as the cumulative effect of adjusting the rate is recognized in the period the forfeiture estimate is changed. If a revised forfeiture rate is higher than the previously estimated forfeiture rate, an adjustment is made that will result in a decrease to the equity-based compensation expense recognized in the Consolidated Financial Statements. If a revised forfeiture rate is lower than the previously estimated forfeiture rate, an adjustment is made that will result in an increase to the equity-based compensation expense recognized in our Consolidated Financial Statements.

**Compensation Expense.** Total equity-based compensation expense recognized was \$12.3 million, \$9.2 million and \$2.0 million for 2016, 2015 and 2014, respectively, and was included in Selling, general and administrative expenses in the Consolidated Statements of Operations and Comprehensive Income. The Company recorded a tax benefit of \$3.2 million related to the equity-based awards granted through December 31, 2016. As of December 31, 2016, the total deferred tax asset related to all outstanding equity-based awards was \$5.0 million. Prior to the spin-off, a portion of these charges related to costs allocated to the Company for GHC corporate employees not solely dedicated to the Company.

Also, in connection with the spin-off, GHC modified the terms of 10,830 restricted stock awards in the second quarter of 2015 affecting 21 Cable One employees. The modification resulted in the acceleration of the vesting period of 6,324 restricted stock awards and the forfeiture of 4,506 restricted stock awards. The Company recorded \$3.7 million of incremental stock compensation expense, net of forfeitures, related to such awards during the first half of 2015, which is included in Selling, general and administrative expenses in the Consolidated Statements of Operations and Comprehensive Income.

## 12. POSTEMPLOYMENT BENEFIT PLANS, PRE-SPIN

**Multiemployer Benefit Plans.** Through June 30, 2015, certain of the Company's employees participated in The Retirement Plan for Graham Holdings Company (the "GHC Retirement Plan") and GHC's Supplemental Executive Retirement Plan (collectively with the GHC Retirement Plan, the "GHC Plans"). The total cost of the GHC Plans was actuarially determined and the Company received an allocation of the service cost associated with the GHC Plans based upon actual benefits earned by the Company's employees. The amount of pension expense allocated to the Company related to these multiemployer plans was \$2.1 million and \$3.9 million in 2015 and 2014, respectively, and is reflected within Operating and Selling, general and administrative expenses in the Consolidated Statements of Operations and Comprehensive Income.

As of June 30, 2015, the GHC Retirement Plan was fully funded and is not in critical or endangered status as defined by the Pension Protection Act of 2006. The GHC Supplemental Executive Retirement Plan is unfunded.

**Multiemployer Savings Plans.** Also, through June 30, 2015, the Company's employees participated in defined contribution plans (primarily 401(k) plans) sponsored by GHC. The defined contribution plans allowed eligible employees to contribute a portion of their salary to the plans, and in some cases, a matching contribution to the funds was provided. The Company recorded expense associated with these GHC-sponsored defined contribution plans of approximately \$0.3 million and \$0.7 million in 2015 and 2014, respectively.

## 13. POSTEMPLOYMENT BENEFIT PLANS, POST-SPIN

As a condition of the spin-off, the Company assumed full financial and reporting responsibility for the postemployment benefit plans offered to eligible employees, other than the GHC Retirement Plan. The accumulated benefits of Company employees participating in GHC sponsored multiemployer benefit and/or savings plans other than the GHC Retirement Plan were transferred into corresponding Cable One sponsored plans. After the spin-off, GHC will continue to administer the GHC Retirement Plan, including making payments under the plan, with respect to current and former Company employees with vested rights thereunder.



Table of Contents

On June 5, 2015, the Board adopted the Cable One, Inc. Supplemental Executive Retirement Plan (the "SERP"), which became effective as of July 1, 2015. The SERP includes a defined benefit portion, or the "DB SERP," and a defined contribution portion, or the "DC SERP."

Upon the spin-off, under the SERP, a \$5.4 million long-term liability was transferred from GHC to the Company representing the accumulated DB SERP and DC SERP liabilities of \$4.1 million and \$1.3 million, respectively. As the DB SERP is unfunded, the Company makes contributions to the DB SERP based on actual benefits payments, which were not material for each of 2016 and 2015. Participant contributions into the DC SERP continued through December 31, 2015. No Company contributions were earned by DC SERP participants on or after July 1, 2015.

On June 5, 2015, the Board also adopted the Cable One 401(k) Savings Plan (the "401(k) Plan"). The 401(k) Plan allows for eligible employees to contribute a portion of their salary to the 401(k) Plan, and in some cases, a matching contribution to the 401(k) Plan is made by the Company. The Company recorded matching contributions to the 401(k) Plan of \$2.8 million and \$1.2 million for 2016 and 2015, respectively.

In addition to the advent of the post-spin postemployment plans described above, the Company has (prior to the spin-off) and may continue to enter into arrangements with certain current and former executives and officers of the Company who desire to defer all or a portion of their annual cash-based incentives under the Cable One, Inc. Deferred Compensation Plan. Upon execution of the agreements, the Company transfers the deferred incentive to a long-term liability. Market-based gains and losses are applied to the respective outstanding balances at each reporting period such that market-based period gains represent additional compensation expense to the Company and market-based losses represent a reduction of compensation expense. The Company recorded compensation expense of \$0.3 million for 2016 and income of \$1.1 million for 2015. The total deferred compensation balance as of December 31, 2016 and 2015 was \$18.2 million and \$18.3 million, respectively, which is included within Accounts payable and accrued liabilities and Accrued compensation and related benefits on the Consolidated Balance Sheets.

In 1999, the Company's then CEO was granted a special deferred compensation award in recognition of his efforts in growing the Company. Annual payouts under this arrangement will commence when he separates service with the Company. The base amounts began accruing interest on May 1, 2016 at an annual rate corresponding to the applicable rate for 12-month U.S. treasury bills (set at each anniversary and carried forward), credited and compounded on an annual basis. The award may be payable in installments upon mutual agreement of the Company and the former CEO, not to extend beyond a ten-year period, however, in the event of his death, all amounts due will be payable in a lump sum within 60 days. No amounts were paid to the former CEO in 2016 in respect of this arrangement. As of December 31, 2016, the Company had an accrued liability of \$2.0 million for this special deferred compensation, which is included in the \$18.2 million deferred compensation balance discussed above.

#### 14. DEFINED BENEFIT POSTRETIREMENT PLAN

The following table sets forth obligation, asset and funding information for the DB SERP:

(in thousands)	As of December 31,	
	2016	2015
<b>Change in Benefit Obligation</b>		
Benefit obligation at Beginning of Period <sup>(1)</sup>	\$ 5,124	\$ 4,115
Interest cost	209	105
Actuarial loss (gain)	(197)	910
Benefits paid	(11)	(6)
<b>Benefit Obligation at End of Year</b>	<b>\$ 5,125</b>	<b>\$ 5,124</b>

<sup>(1)</sup> The beginning of period for 2015 was July 1, 2015 when the Company assumed the DB SERP obligation from GHC.

Table of Contents

The accumulated benefit obligation for the DB SERP at December 31, 2016 and 2015 was \$5.1 million and \$5.1 million, respectively. The amounts recognized in the Consolidated Balance Sheets for defined benefit pension plan were as follows:

(in thousands)	As of December 31,	
	2016	2015
Current liability	\$ (336)	\$ (334)
Noncurrent liability	(4,789)	(4,790)
<b>Recognized Asset (Liability)</b>	<b>\$ (5,125)</b>	<b>\$ (5,124)</b>

Key assumptions utilized for determining the benefit obligation included the use of a discount rate of 3.95% and 4.22% for 2016 and 2015, respectively.

The Company recognized \$0.2 million and \$0.1 million in DB SERP expense for 2016 and 2015, respectively. As the plan is unfunded, the Company makes contributions to the DB SERP based on actual benefit payments. Company contributions were not material for the years ended December 31, 2016 and 2015.

At December 31, 2016, future estimated benefit payments, excluding charges for early retirement programs, were as follows:

(in thousands)	DB SERP
2017	\$ 342
2018	340
2019	337
2020	334
2021	331
2022 – 2026	1,602

During 2017, the Company expects to recognize the following amortization components of net periodic cost for the DB SERP:

(in thousands)	DB SERP
Actuarial loss recognition	\$ 8

## 15. NET INCOME PER SHARE

Basic net income per common share is computed by dividing the net income allocable to the common stockholders by the weighted average number of common shares outstanding during the period. Diluted income per share further includes any common shares available to be issued upon exercise of outstanding SARs if such inclusion would be dilutive.

The following table sets forth the computation of basic and diluted net income per common share (dollars in thousands, except share and per share amounts):

	Year Ended December 31,		
	2016	2015	2014
Numerator:			
Net income	\$ 98,939	\$ 89,033	\$ 147,309
Denominator:			
Weighted average common shares outstanding - Basic	5,743,568	5,853,283	5,843,313
Effect of dilutive equity awards <sup>(1)</sup>	27,392	6,806	-
Weighted average common shares outstanding - Diluted	5,770,960	5,860,089	5,843,313
Net income per share:			
Basic	\$ 17.23	\$ 15.21	\$ 25.21
Diluted	\$ 17.14	\$ 15.19	\$ 25.21

<sup>(1)</sup> SARs outstanding that were not included in the diluted net income per share calculation because the effect would have been anti-dilutive were 438; 89,909 and 0 SARs as of December 31, 2016, 2015 and 2014, respectively.



Table of Contents**16. RELATED PARTY TRANSACTIONS**

**Allocation of expenses.** Prior to the spin-off, the Consolidated Financial Statements included allocations of expenses from GHC for certain overhead functions, including, but not limited to, finance, human resources, legal, information technology, general insurance, risk management and other corporate functions. These expenses were allocated to the Company on the basis of direct usage when identifiable, with the remainder generally allocated on a proportional basis using revenue or headcount. The Company was allocated \$5.8 million and \$12.7 million in 2015 and 2014, respectively, of corporate overhead costs incurred by GHC. These cost allocations are included in selling, general and administrative expenses in the Consolidated Statements of Operations and Comprehensive Income.

These expense allocations were determined on the basis that both the Company and GHC considered to be a reasonable reflection of the utilization of services provided or the benefit received by the Company. The allocations may not, however, have reflected the expense the Company would have incurred as an independent company for the periods prior to the spin-off. Actual costs that may have been incurred if the Company had been a stand-alone company would depend on a number of factors, including the chosen organizational structure and certain strategic decisions.

**Additional GHC Investment (Deficit).** Prior to the spin-off, the net assets of the Company were represented by the cumulative investment in the Company by GHC that is shown as Additional GHC investment (deficit), which comprised share capital, settlements of intercompany balances and transactions between the Company and GHC, and net transfers of cash and cash equivalents. The settlement of intercompany balances and transactions between the Company and GHC that were not historically settled in cash were included in Additional GHC investment (deficit) and thus effectively deemed settled in cash for presentation purposes.

The components of net transfers to GHC were as follows (in thousands):

	<b>Year Ended December 31,</b>	
	<b>2015</b>	<b>2014</b>
Net change in current income tax accounts	\$ (39,083)	\$ 85,071
Allocation of overhead and other expenses from GHC	5,800	12,671
Net advances to GHC	(2,916)	(227,022)
<b>Total net transfers to GHC</b>	<b>\$ (36,199)</b>	<b>\$ (129,280)</b>

**17. COMMITMENTS AND CONTINGENCIES**

**Contractual Obligations.** The Company has obligations to make future payments for goods and services under certain contractual arrangements. These contractual obligations secure the future rights to various assets and services to be used in the normal course of the Company's operations. For example, the Company is contractually committed to make certain minimum lease payments for the use of property under operating lease agreements. In accordance with applicable accounting rules, the future rights and obligations pertaining to firm commitments, such as operating lease obligations and certain purchase obligations under contracts, are not reflected as assets or liabilities in the Consolidated Balance Sheets.

The Company's rent expense, which primarily includes facility rental expense, was \$8.1 million, \$8.4 million and \$1.8 million in 2016, 2015 and 2014, respectively. The Company has lease obligations under various operating leases including minimum lease obligations for real estate.

Table of Contents

The following table summarizes the Company's contractual obligations outstanding as of December 31, 2016 under various contractual obligations (including amounts associated with data processing services, high-speed data connectivity and fiber-related obligations) and the estimated timing and effect that such obligations are expected to have on the Company's liquidity and cash flows in future periods (in thousands):

Years ending December 31,	Programming purchase commitments (1)	Operating leases	Total debt, including capital lease	Other purchase obligations (2)	Total
2017	\$ 171,995	\$ 1,038	\$ 6,250	\$ 24,162	\$ 203,445
2018	150,830	728	8,767	15,731	176,056
2019	124,507	564	12,517	8,988	146,576
2020	83,621	452	67,517	3,990	155,580
2021	19,244	360	17	2,507	22,128
Thereafter	-	741	450,216	4,060	455,017
Total	\$ 550,197	\$ 3,883	\$ 545,284	\$ 59,438	\$ 1,158,802

(1) Includes commitments to purchase programming to be produced in future years.

(2) Includes purchase obligations related to capital projects and other legally binding commitments. Other purchase orders made in the ordinary course of business are excluded from the table above. Any amounts for which we are liable under purchase orders are reflected in our Consolidated Balance Sheets as accounts payable and accrued liabilities.

Programming and content purchases represent contracts that the Company has with cable television networks and broadcast stations to provide programming services to its subscribers. The amounts included above represent estimates of the future programming costs for these contract requirements and commitments based on subscriber numbers and tier placement as of December 31, 2016 applied to the per-subscriber rates contained in these contracts. Actual amounts due under such contracts may differ from the amounts above based on the actual subscriber numbers and tier placements.

The following items are not included as contractual obligations due to various factors discussed below. However, the Company incurs these costs as part of its operations:

- The Company rents utility poles used in its operations. Generally, pole rentals are cancellable on short notice, but the Company anticipates that such rentals will recur. Rent expense for pole attachments was approximately \$5.7 million, \$5.7 million and \$5.5 million in 2016, 2015 and 2014, respectively.
- The Company pays franchise fees under multi-year franchise agreements based on a percentage of revenues generated from video service per year. Franchise fees and other franchise-related costs included in the Consolidated Statements of Operations and Comprehensive Income were \$14.2 million, \$15.7 million and \$16.7 million in 2016, 2015 and 2014, respectively.
- The Company has cable franchise agreements containing provisions requiring the construction of cable plant and the provision of services to customers within the franchise areas. In connection with these obligations under existing franchise agreements, the Company obtains surety bonds or letters of credit guaranteeing performance to municipalities and public utilities and payment of insurance premiums. Such surety bonds and letters of credit as of December 31, 2016 and 2015 totaled \$5.1 million and \$4.6 million, respectively. Payments under these arrangements are required only in the event of nonperformance. The Company does not expect that these contingent commitments will result in any amounts being paid in the foreseeable future.

**Litigation and Legal Matters.** The Company is subject to complaints and administrative proceedings and is a defendant in various civil lawsuits that have arisen in the ordinary course of its businesses. Such matters include: contract disputes; actions alleging negligence; invasion of privacy; trademark, copyright and patent infringement; violations of applicable wage and hour laws; statutory or common law claims involving current and former employees; and other matters. Although the outcomes of the legal claims and proceedings against the Company cannot be predicted with certainty, based on currently available information, management believes that there are no existing claims or proceedings that are likely to have a material effect on the Company's business, financial condition, results of operations or cash flows. Also, based on currently available information, management is of the opinion that the exposure to future material losses from existing legal proceedings is not reasonably possible or that future material losses in excess of the amounts accrued are not reasonably possible.



Table of Contents

**Regulation in the Cable Industry.** The operation of a cable system is extensively regulated by the Federal Communications Commission (the "FCC"), some state governments and most local governments. The FCC has the authority to enforce its regulations through the imposition of substantial fines, the issuance of cease and desist orders and/or the imposition of other administrative sanctions, such as the revocation of FCC licenses needed to operate certain transmission facilities used in connection with cable operations. The Telecommunications Act of 1996 altered the regulatory structure governing the nation's communications providers. It removed barriers to competition in both the cable television market and the voice market. Among other things, it reduced the scope of cable rate regulation and encouraged additional competition in the video programming industry by allowing telephone companies to provide video programming in their own telephone service areas. Future legislative and regulatory changes could adversely affect the Company's operations.

**GHC Agreements.** On June 16, 2015, Cable One entered into several agreements with GHC that set forth the principal actions taken in connection with the spin-off and that govern the relationship of the parties following the spin-off, including a Separation and Distribution Agreement, a Tax Matters Agreement and an Employee Matters Agreement.

**18. SUMMARY OF QUARTERLY OPERATING RESULTS**

**For Each of the Four Quarters in the Year Ended  
December 31, 2016  
(Unaudited)**

**Statement of Operations Information**

(in thousands, except per share and share data)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenues	\$ 202,805	\$ 204,557	\$ 205,536	\$ 206,727
Operating costs and expenses	155,422	154,000	161,716	160,280
Income from operations	47,383	50,557	43,820	46,447
Net income	27,044	26,633	20,874	24,388
Net income per common share:				
Basic	\$ 4.67	\$ 4.64	\$ 3.65	\$ 4.27
Diluted	\$ 4.65	\$ 4.62	\$ 3.63	\$ 4.23
Weighted average common share outstanding:				
Basic	5,796,252	5,743,465	5,720,257	5,714,862
Diluted	5,810,639	5,766,312	5,755,161	5,760,834

**For Each of the Four Quarters in the Year Ended  
December 31, 2015  
(Unaudited)**

**Statement of Operations Information**

(in thousands, except per share and share data)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenues	\$ 202,909	\$ 202,698	\$ 198,215	\$ 203,444
Operating costs and expenses	166,976	166,909	159,219	152,420
Income from operations	35,933	35,789	38,996	51,024
Net income	22,109	21,434	19,412	26,078
Net income per common share:				
Basic	\$ 3.78	\$ 3.67	\$ 3.31	\$ 4.45
Diluted	\$ 3.78	\$ 3.67	\$ 3.30	\$ 4.44
Weighted average common share outstanding:				
Basic	5,843,313	5,843,313	5,871,928	5,854,253
Diluted	5,843,313	5,843,313	5,875,588	5,864,083

Table of Contents**19. SUBSEQUENT EVENTS****Acquisition of NewWave**

On January 18, 2017, the Company announced that the Company and Frequency Merger Sub, LLC, its wholly owned subsidiary, entered into an Agreement and Plan of Merger, dated as of January 17, 2017 (the "Merger Agreement"), with RBI Holding LLC ("NewWave"), RBI Blocker Corp., RBI Blocker Holdings LLC and GTCR-RBI, LLC, as equityholder representative, pursuant to which the Company has agreed to acquire all of the outstanding equity interests in NewWave. NewWave is owned by funds affiliated with GTCR LLC, a leading private equity firm based in Chicago. Under the terms of the Merger Agreement, the Company will pay a purchase price of \$735 million in cash, subject to customary post-closing adjustments. The closing of the transaction is subject to the receipt of certain regulatory approvals and other customary closing conditions. The Company currently anticipates that the transaction will be completed in the second quarter of 2017.

The Company expects to finance the transaction with \$650 million of senior secured loans and cash on hand. In connection with the entry into the Merger Agreement, the Company entered into a commitment letter on January 17, 2017, as amended and restated on February 13, 2017, with JPMorgan Chase Bank, N.A., Wells Fargo Bank, National Association, Wells Fargo Securities, LLC, RBC Capital Markets, Royal Bank of Canada, Toronto Dominion Bank, New York Branch, TD Securities (USA) LLC, SunTrust Bank, SunTrust Robinson Humphrey, Inc. and U.S. Bank National Association (the "Lenders"). Pursuant to the amended and restated commitment letter, and subject to the terms and conditions set forth therein, the Lenders have committed to provide the Company with \$300 million of incremental five-year term "A" loans and \$350 million of incremental seven-year term "B" loans to finance the transaction.

On February 13, 2017, the Company entered into an amendment to the Credit Agreement to permit, among other things, the incurrence of the \$650 million of senior secured loans expected to be used to finance the acquisition of NewWave and the other transactions contemplated by the Merger Agreement.

**Change in Accounting Estimate**

In the first quarter of 2017, the Company changed its accounting estimate related to the capitalization of certain internal labor and related costs associated with construction and customer installation activities. As a result of this change in estimate, the Company expects the amount of capitalized labor costs to increase as compared to prior periods, resulting in lower expenses and higher capital expenditures beginning in 2017.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2016
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 No. 001-7784



CENTURYLINK, INC.

(Exact name of registrant as specified in its charter)

Louisiana
(State or other jurisdiction of
incorporation or organization)

100 CenturyLink Drive, Monroe, Louisiana
(Address of principal executive offices)

72-0651161
(I.R.S. Employer
Identification No.)

71203
(Zip Code)

(318) 388-9000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Table with 2 columns: Title of Each Class, Name of Each Exchange on Which Registered. Row: Common Stock, par value \$1.00 per share, New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: Stock Options

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes [X] No [ ]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes [ ] No [X]

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 [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, 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). Yes [X] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

Indicate by check mark 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 [ ]
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [X]

On February 16, 2017, 546,575,404 shares of common stock were outstanding. The aggregate market value of the voting stock held by non-affiliates as of June 30, 2016 was \$15.7 billion.

**DOCUMENTS INCORPORATED BY REFERENCE:**

Portions of the Registrant's Proxy Statement to be furnished in connection with the 2017 annual meeting of shareholders are incorporated by reference in Part III of this annual report.

## TABLE OF CONTENTS

### PART I

<u>Item 1. Business</u>	<u>3</u>
<u>Item 1A. Risk Factors</u>	<u>19</u>
<u>Item 1B. Unresolved Staff Comments</u>	<u>42</u>
<u>Item 2. Properties</u>	<u>43</u>
<u>Item 3. Legal Proceedings</u>	<u>43</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>43</u>

### PART II

<u>Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>44</u>
<u>Item 6. Selected Financial Data</u>	<u>45</u>
<u>Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>48</u>
<u>Item 7A. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>76</u>
<u>Item 8. Consolidated Financial Statements and Supplementary Data</u>	<u>77</u>
<u>Consolidated Statements of Operations</u>	<u>79</u>
<u>Consolidated Statements of Comprehensive Income (Loss)</u>	<u>80</u>
<u>Consolidated Balance Sheets</u>	<u>81</u>
<u>Consolidated Statements of Cash Flows</u>	<u>82</u>
<u>Consolidated Statements of Stockholders' Equity</u>	<u>83</u>
<u>Notes to Consolidated Financial Statements</u>	<u>84</u>
<u>Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>133</u>
<u>Item 9A. Controls and Procedures</u>	<u>133</u>
<u>Item 9B. Other Information</u>	<u>134</u>

### PART III

<u>Item 10. Directors, Executive Officers and Corporate Governance</u>	<u>134</u>
<u>Item 11. Executive Compensation</u>	<u>134</u>
<u>Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>135</u>
<u>Item 13. Certain Relationships and Related Transactions and Director Independence</u>	<u>135</u>
<u>Item 14. Principal Accountant Fees and Services</u>	<u>135</u>

### PART IV

<u>Item 15. Exhibits and Financial Statement Schedules</u>	<u>136</u>
<u>Item 16. Summary Business and Financial Information</u>	<u>144</u>
<u>Signatures</u>	<u>145</u>

Unless the context requires otherwise, references in this annual report on Form 10-K, for all periods presented, to "CenturyLink," "we," "us" and "our" refer to CenturyLink, Inc. and its consolidated subsidiaries.

## PART I

### ITEM 1. BUSINESS

#### Overview

We are an integrated communications company engaged primarily in providing an array of services to our residential and business customers. Our communications services include local and long-distance voice, broadband, Multi-Protocol Label Switching ("MPLS"), private line (including special access), Ethernet, colocation, hosting (including cloud hosting and managed hosting), data integration, video, network, public access, Voice over Internet Protocol ("VoIP"), information technology and other ancillary services. We strive to maintain our customer relationships by, among other things, bundling our service offerings to provide our customers with a complete offering of integrated communications services.

Based on our approximately 11.1 million total access lines at December 31, 2016, we believe we are the third largest wireline telecommunications company in the United States. We operate 74% of our total access lines in portions of Colorado, Arizona, Washington, Minnesota, Florida, North Carolina, Oregon, Iowa, Utah, New Mexico, Missouri, and Idaho. We also provide local service in portions of Nevada, Wisconsin, Ohio, Virginia, Texas, Nebraska, Pennsylvania, Alabama, Montana, Indiana, Arkansas, Wyoming, Tennessee, New Jersey, South Dakota, North Dakota, Kansas, South Carolina, Louisiana, Michigan, Illinois, Georgia, Mississippi, Oklahoma, and California. In the portion of these 37 states where we have access lines, which we refer to as our local service area, we are the incumbent local telephone company.

At December 31, 2016, we served approximately 5.9 million broadband subscribers and 325 thousand Prism TV subscribers. We also operate 58 data centers throughout North America, Europe and Asia.

We were incorporated under the laws of the State of Louisiana in 1968. Our principal executive offices are located at 100 CenturyLink Drive, Monroe, Louisiana 71203 and our telephone number is (318) 388-9000.

For a discussion of certain risks applicable to our business, see "Risk Factors" in Item 1A of Part I of this annual report. The summary financial information in this section should be read in conjunction with, and is qualified by reference to, our consolidated financial statements and notes thereto in Item 8 and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 of Part II of this annual report.

#### *Pending Transactions*

##### **Pending Acquisition of Level 3**

On October 31, 2016, we entered into a definitive merger agreement under which we propose to acquire Level 3 Communications, Inc. ("Level 3") in a cash and stock transaction. Under the terms of the agreement, Level 3 shareholders will receive \$26.50 per share in cash and 1.4286 of CenturyLink shares for each share of Level 3 common stock they own at closing. CenturyLink shareholders are expected to own approximately 51% and Level 3 shareholders are expected to own approximately 49% of the combined company at closing. On December 31, 2016, Level 3 had outstanding \$10.9 billion of long-term debt.

Completion of the transaction is subject to the receipt of regulatory approvals, including the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act, as well as approvals from the Federal Communications Commission ("FCC") and certain state regulatory authorities. The transaction is also subject to the approval of CenturyLink and Level 3 shareholders at meetings scheduled to be held on March 16, 2017, as well as other customary closing conditions. Subject to these conditions, we anticipate closing this transaction by the end of the third quarter 2017. If the merger agreement is terminated under certain circumstances, we may be obligated to pay Level 3 a termination fee of \$472 million, or Level 3 may be obligated to pay CenturyLink a termination fee of \$738 million.

See "Risk Factors—Risks Relating to Our Pending Acquisition of Level 3" in Item 1A of Part I of this annual report, for additional information concerning our pending acquisition of Level 3. Additional information about Level 3 is included in documents filed by it with the Securities and Exchange Commission ("SEC").

The foregoing description of the pending Level 3 acquisition is not complete, and is qualified in its entirety by reference to the definitive joint proxy statement/prospectus filed with the SEC by us on February 13, 2017.

## Pending Sale of Colocation Business and Data Centers

On November 3, 2016, we entered into a definitive stock purchase agreement to sell our data centers and colocation business to a consortium led by BC Partners, Inc. and Medina Capital ("the Purchaser") in exchange for cash and a minority stake in the consortium's newly-formed global secure infrastructure company. During 2016, as a result of the pending sale, the assets to be sold to the Purchaser have been reclassified as assets held for sale in other current assets on our consolidated balance sheet. Additionally, the liabilities to be assumed by the Purchaser have been reclassified and presented as current liabilities associated with assets held for sale on our consolidated balance sheet. The sale is subject to regulatory approvals, including a review by the Committee of Foreign Investments in the United States, as well as other customary closing conditions. This transaction will result in the Purchaser acquiring 57 data centers. This business generated revenues of \$622 million, \$626 million and \$643 million (excluding revenue with affiliates) for the years ended December 31, 2016, 2015 and 2014, respectively (a small portion of which will be retained by us). Based on certain estimates and assumptions regarding the closing date and various tax matters, we currently project that the net cash proceeds from the divestiture will be approximately \$1.5 billion to \$1.7 billion. We plan to use a portion of these net cash proceeds to partly fund our acquisition of Level 3.

See Note 3—Pending Sale of Colocation Business and Data Centers to our consolidated financial statements in Item 8 of Part II of this annual report for additional information on this pending sale.

The foregoing description of the pending sale of our data centers and colocation business is not complete, and is qualified in its entirety by reference to our current report on Form 8-K filed with the SEC on November 7, 2016.

## Financial and Operational Highlights

The following table summarizes the results of our consolidated operations:

	Years Ended December 31,		
	2016 <sup>(1)(2)</sup>	2015 <sup>(1)</sup>	2014 <sup>(3)</sup>
	(Dollars in millions)		
Consolidated statements of operations summary results:			
Operating revenues	\$ 17,470	17,900	18,031
Operating expenses	15,139	15,295	15,621
Operating income	\$ 2,331	2,605	2,410
Net income	\$ 626	878	772

- (1) During 2016 and 2015, we recognized an incremental \$201 million and \$215 million, respectively, of revenue associated with the FCC's Connect America Fund Phase 2 support program as compared to the interstate USF program. For additional information, see Note 1—Basis of Presentation and Summary of Significant Accounting Policies to our consolidated financial statements in Item 8 of Part II of this annual report.
- (2) During 2016, we recognized \$189 million of severance expenses and other one-time termination benefits associated with our workforce reductions and \$52 million of expenses related to our pending acquisition of Level 3.
- (3) During 2014, we recognized a \$60 million tax benefit associated with a deduction for the tax basis for worthless stock in a wholly-owned foreign subsidiary and a \$63 million pension settlement charge.

The following table summarizes certain selected financial information from our consolidated balance sheets:

	As of December 31,	
	2016	2015
	(Dollars in millions)	
Consolidated balance sheets summary information:		
Total assets	\$ 47,017	47,604
Total long-term debt <sup>(1)</sup>	19,993	20,225
Total stockholders' equity	13,399	14,060

- (1) Total long-term debt is the sum of current maturities of long-term debt, capital lease obligations of \$305 million (associated with the pending sale of colocation business and data centers) included in current liabilities associated with assets held for sale and long-term debt on our consolidated balance sheets. For additional information on our total long-term debt, see Note 5—Long-Term Debt and Credit Facilities to our consolidated financial statements in Item 8 of Part II of this annual report. For information on our total obligations, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Future Contractual Obligations" in Item 7 of Part II of this annual report.

The following table summarizes certain of our operational metrics:

	As of December 31,		
	2016	2015	2014
	(in thousands except for data centers, which are actuals)		
Operational metrics:			
Total access lines <sup>(1)</sup>	11,090	11,748	12,394
Total broadband subscribers <sup>(1)</sup>	5,945	6,048	6,082
Total Prism TV subscribers	325	285	242
Total data centers <sup>(2)</sup>	58	59	58

(1) Access lines are lines reaching from the customers' premises to a connection with the public network and broadband subscribers are customers that purchase broadband connection service through their existing telephone lines, stand-alone telephone lines, or fiber-optic cables. Our methodology for counting our access lines and broadband subscribers includes only those lines that we use to provide services to external customers and excludes lines used solely by us and our affiliates. It also excludes unbundled loops and includes stand-alone broadband subscribers. We count lines when we install the service.

(2) We define a data center as any facility where we market, sell and deliver either colocation services, multi-tenant managed services, or both. Our data centers are located in North America, Europe and Asia.

Our methodology for counting access lines, broadband subscribers, Prism TV subscribers and data centers may not be comparable to those of other companies.

Substantially all of our long-lived assets are located in the United States and substantially all of our total consolidated operating revenues are from customers located in the United States. We estimate that approximately 1% of our consolidated revenues is derived from providing telecommunications, colocation and hosting services outside the United States.

## Operations

### Segments

We are organized into operating segments based on customer type, business and consumer. These operating segments are our two reportable segments in our consolidated financial statements:

- Business Segment.** Consists generally of providing strategic, legacy and data integration products and services to small, medium and enterprise business, wholesale and governmental customers, including other communication providers. Our strategic products and services offered to these customers include our MPLS, Ethernet, colocation, hosting (including cloud hosting and managed hosting), broadband, VoIP, information technology and other ancillary services. Our legacy services offered to these customers primarily include local and long-distance voice, including the sale of unbundled network elements ("UNEs"), private line (including special access), switched access and other ancillary services. Our data integration offerings include the sale of telecommunications equipment located on customers' premises and related products and professional services, all of which are described further below under the heading "Products and Services"; and
- Consumer Segment.** Consists generally of providing strategic and legacy products and services to residential customers. Our strategic products and services offered to these customers include our broadband, video (including our Prism TV services) and other ancillary services. Our legacy services offered to these customers include local and long-distance voice and other ancillary services.

The following table shows the composition of our operating revenues by segment under our current segment categorization for the years ended December 31, 2016, 2015 and 2014:

	Years Ended December 31,			Percent Change	
	2016	2015	2014	2016 vs 2015	2015 vs 2014
Percentage of revenues:					
Business segment	59%	59%	61%	—%	(2)%
Consumer segment	34%	34%	33%	—%	1 %
Other operating revenues	7%	7%	6%	—%	1 %
Total operating revenues	100%	100%	100%		

For additional information on our segment data, including information on certain centrally-managed assets and expenses not reflected in our segment results, see Note 14—Segment Information to our consolidated financial statements in Item 8 of Part II of this annual report and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 of Part II of this annual report.

In January 2017, we announced to our employees an organizational change designed to better align our customer-facing organizations into three business units: consumer; enterprise and IT and managed services. These organizations will be fully integrated with sales, marketing and service delivery support teams to enable faster decision-making, market responsiveness and deeper accountability. We implemented this organization change to create greater focus on the customer experience in each business unit and accelerate strategic revenue growth.

#### *Products and Services*

From time to time, we change the categorization of our products and services, and we may make similar changes in the future. During the second quarter of 2016, we determined that because of declines due to customer migration to other strategic products and services, certain of our business low-bandwidth data services, specifically our private line (including special access) services in our business segment, are more closely aligned with our legacy services than with our strategic services. As described in greater detail in Note 14—Segment Information, these operating revenues are now reflected as legacy services.

Our products and services include local and long-distance voice, broadband, MPLS, private line (including special access), Ethernet, colocation, hosting (including cloud hosting and managed hosting), data integration, video, network, public access, VoIP, information technology and other ancillary services.

We offer our customers the ability to bundle together several products and services. For example, we offer integrated and unlimited local and long-distance voice services. Our customers can also bundle two or more services such as broadband, video (including DIRECTV through our strategic partnership), voice and Verizon Wireless (through our strategic partnership) services. We believe our customers value the convenience and price discounts associated with receiving multiple services through a single company.

Most of our products and services are provided using our telecommunications network, which consists of voice and data switches, copper cables, fiber-optic cables and other equipment. Our network serves approximately 11.1 million access lines and forms a portion of the public switched telephone network, or PSTN. For more information on our network, see "Business—Network Architecture" below.

Described in greater detail below are our key products and services.

### Strategic Services

We primarily focus our marketing and sales efforts on our "strategic" services, which are those services for which demand generally remains strong and that we believe are most important to our future performance. Generally speaking, our strategic services enable our customers to access the Internet, connect to private networks and transmit data, and enhance the security, reliability and efficiency of our customers' communications. Our strategic services are comprised of the following:

- *Broadband.* Our broadband services allow customers to connect at high speeds to the Internet through their existing telephone lines or fiber-optic cables. Substantially all of our broadband subscribers are located within the local service area of our wireline telephone operations;
- *MPLS.* Multi-Protocol Label Switching is a standards-approved data networking technology that we provide to support real-time voice and video transmission services. This technology allows network operators flexibility to divert and route traffic around link failures, congestion and bottlenecks;
- *Ethernet.* Ethernet services include point-to-point and multi-point equipment configurations that facilitate data transmissions across metropolitan areas and wide area networks. Ethernet services are also used to provide transmission services to wireless service providers that use our fiber-optic cables connected to their towers;
- *Colocation.* Colocation services enable our customers to install their own IT equipment in our data centers;
- *Managed Hosting.* Managed hosting includes provision of centralized IT infrastructure and a variety of managed services including cloud and traditional computing, application management, back-up, storage, and other advanced services including planning, design, implementation and support services;
- *Video.* Our video services include our facilities-based video, marketed as CenturyLink Prism TV, which is a premium entertainment service that allows our customers to watch hundreds of television or cable channels and record up to four shows on one home digital video recorder. We also offer satellite digital television under an arrangement with DIRECTV that allows us to market, sell and bill for its services under its brand name;
- *VoIP.* Voice over Internet Protocol, or VoIP, is a real-time, two-way voice communication service (similar to our traditional voice services) that originates over a broadband connection and often terminates on the PSTN; and
- *Managed Services.* Managed services represents a blend of network, hosting, cloud, and IT services that typically require ongoing support from our staff. These services frequently involve equipment or networks owned, acquired or controlled by the customer and often include consulting or software development.

### Legacy Services

Our "legacy" services represent our traditional voice, data and network services, which include the following:

- *Local Voice Services.* We offer local calling services for our residential and business customers within the local service area of our wireline markets, generally for a fixed monthly charge. These services include a number of enhanced calling features and other services, such as call forwarding, caller identification, conference calling, voice mail, selective call ringing and call waiting, for which we generally charge an additional monthly fee. We also generate revenues from non-recurring services, such as inside wire installation, maintenance services, service activation and reactivation. For our wholesale customers, our local calling service offerings include primarily the resale of our voice services and the sale of UNEs, which allow our wholesale customers to use all or part of our network to provide voice and data services to their customers. Local calling services provided to our wholesale customers allow other telecommunications companies the ability to originate or terminate telecommunications services on our network;
- *Long-distance Voice Services.* We offer our residential and business customers domestic and international long-distance services and toll-free services. Our international long-distance services include voice calls that either terminate or originate with our customers in the United States;

- *Private Line.* A private line (including special access) is a direct circuit or channel specifically dedicated for the purpose of directly connecting two or more sites. Private line service offers a high-speed, secure solution for frequent transmission of large amounts of data between sites, including wireless backhaul transmissions;
- *Switched Access Services.* As part of our wholesale services, we provide various forms of switched access services to wireline and wireless service providers for the use of our facilities to originate and terminate their interstate and intrastate voice transmissions;

- *ISDN*. We offer integrated services digital network ("ISDN") services, which use regular telephone lines to support voice, video and data applications; and
- *WAN*. We offer wide area network ("WAN") services, which allow a local communications network to link to networks in remote locations.

### **Data Integration**

Data integration includes the sale of telecommunications equipment located on customers' premises and related products and professional services. These services include network management, installation and maintenance of data equipment and the building of proprietary fiber-optic broadband networks for our governmental and business customers.

### **Other Operating Revenues**

Other operating revenues consist primarily of Connect America Fund ("CAF") support payments, Universal Service Fund ("USF") support payments and USF surcharges. We receive federal support payments from both Phase 1 and Phase 2 of the CAF program, and support payments from both federal and state USF programs. These support payments are government subsidies designed to reimburse us for various costs related to certain telecommunications services, including the costs of deploying, maintaining and operating voice and broadband infrastructure in high-cost rural areas where we are not able to fully recover our costs from our customers. We also collect USF surcharges based on specific items we list on our customers' invoices to fund the Federal Communications Commission's ("FCC") universal service programs. We also generate other operating revenues from the leasing and subleasing of space in our office buildings, warehouses and other properties. Because we centrally manage the activities that generate these other operating revenues, these revenues are not included in our segment revenues.

### **Additional Information**

From time to time, we also make investments in other communications or technology companies.

For further information on regulatory, technological and competitive changes that could impact our revenues, see "Regulation" and "Competition" under this Item 1 below and "Risk Factors" under Item 1A below. For more information on the financial contributions of our various services, see "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 of Part II of this annual report.

### **Patents, Trade Names, Trademarks and Copyrights**

Either directly or through our subsidiaries, we have rights in various patents, trade names, trademarks, copyrights and other intellectual property necessary to conduct our business, such as our CenturyLink® and Prism® brand names. Our services often use the intellectual property of others, including licensed software. We also occasionally license our intellectual property to others as we deem appropriate.

We periodically receive offers from third parties to purchase or obtain licenses for patents and other intellectual property rights in exchange for royalties or other payments. We also periodically receive notices, or are named in lawsuits, alleging that our products or services infringe on patents or other intellectual property rights of third parties. In certain instances, these matters can potentially adversely impact our operations, operating results or financial position. For additional information, see "Risk Factors—Risks Affecting Our Business" in Item 1A of Part I of this annual report, and Note 16—Commitments and Contingencies to our consolidated financial statements in Item 8 of Part II of this annual report.

### **Sales and Marketing**

We maintain local offices in most of the larger population centers within our local service area. These offices provide sales and customer support services in the community. We also rely on our call center personnel and a variety of channel partners to promote sales of services that meet the needs of our customers. Our sales and marketing strategy is to enhance our sales by offering solutions tailored to the needs of our various customers and promoting our brands. Our offerings include both stand-alone services and bundled services designed to meet the needs of different customer segments.

We conduct most of our operations under the brand name "CenturyLink." Our satellite television service is offered on a co-branded basis under the "DIRECTV" name. Our switched digital television service offering is branded under the name "Prism TV." The wireless service that we offer under our agency agreement with Verizon Wireless is marketed under the "Verizon Wireless" brand name.

Our sales and marketing approach to our residential customers emphasizes customer-oriented sales, marketing and service with a local presence. Our marketing plans include marketing our products and services primarily through direct sales representatives, inbound call centers, local retail stores, telemarketing and third parties, including retailers, satellite television providers, door to door sales agents and digital marketing firms. We support our distribution with digital marketing, direct mail, bill inserts, newspaper and television advertising, website promotions, public relations activities and sponsorship of community events and sports venues.

Similarly, our sales and marketing approach to our business customers includes a commitment to provide comprehensive communications and IT solutions for business, wholesale and governmental customers of all sizes, ranging from small offices to select enterprise customers. We strive to offer our business customers stable, reliable, secure and trusted solutions. Our marketing plans include marketing our products and services primarily through digital advertising, direct sales representatives, inbound call centers, telemarketing and third parties, including telecommunications agents, system integrators, value-added resellers and other telecommunications firms. We support our distribution through digital advertising, events, television advertising, website promotions and public relations.

### Network Architecture

Most of our products and services are provided using our telecommunications network, which consists of voice switches, data switches and routers, high-speed transport equipment, fiber-optic and copper cables and other equipment. Our local exchange carrier networks also include central offices and remote site assets. A substantial portion of our equipment operates with licensed software. As of December 31, 2016, we maintained approximately 1 million miles of copper plant and approximately 265 thousand miles of domestic fiber-optic plant.

We continue to enhance and expand our network by deploying broadband-enabled technologies to provide additional capacity to our customers. Rapid and significant changes in technology are expected to continue in the telecommunications industry. Our future success will depend, in part, on our ability to anticipate and adapt to changes in customer demands and technology. In particular, we anticipate that continued increases in broadband usage by our customers will require us to make significant capital expenditures to increase network capacity or to implement network management practices to alleviate network capacity shortages. The FCC's definition of "broadband service" could create additional requirements for higher capital spending to address marketing and competitive issues. Any such additional expenditures could adversely impact our results of operations and financial condition.

Similarly, we continue to take steps to simplify and modernize our network. To attain our objectives, we plan to continue to undertake several complex projects that we expect will be costly and take several years to complete. The costs of these projects could increase materially if we conclude that we need to replace any or all of our legacy systems.

Like other large telecommunications companies, we are a constant target of cyber-attacks of varying degrees, which has caused us to spend increasingly more time and money to deal with increasingly sophisticated attacks. Some of the attacks result in security breaches, and we periodically notify our customers, our employees or the public of these breaches when necessary or appropriate. None of these resulting security breaches to date have materially adversely affected our business, results of operations or financial condition.

We rely on several other communications companies to provide our offerings. We lease a significant portion of our core fiber network from our competitors and other third parties. Many of these leases will lapse in future years. All of our satellite television and wireless voice services are provided by other carriers under agency agreements, and some of our other services are reliant upon reselling arrangements with other carriers. Our future ability to provide services on the terms of our current offerings will depend in part upon our ability to renew or replace these leases, agreements and arrangements on terms substantially similar to those currently in effect.

For additional information regarding our systems, network, cyber risks, capital expenditure requirements and reliance upon third parties, see "Risk Factors," generally, in Item 1A of Part I of this annual report, and, in particular, "Risk Factors—Risks Affecting Our Business" and "Risk Factors—Risks Affecting Our Liquidity and Capital Resources." For more information on our properties, see "Properties" in Item 2 of Part I of this annual report.

## Regulation

### Overview

As discussed further below, our operations are subject to significant local, state, federal and foreign laws and regulations.

We are subject to significant regulation by the FCC, which regulates interstate communications, and state utility commissions, which regulate intrastate communications. These agencies (i) issue rules to protect consumers and promote competition, (ii) set the rates that telecommunication companies charge each other for exchanging traffic, and (iii) have traditionally developed and administered support programs designed to subsidize the provision of services to high-cost rural areas. In most states, local voice service, switched and special access services and interconnection services are subject to price regulation, although the extent of regulation varies by type of service and geographic region. In addition, we are required to maintain licenses with the FCC and with state utility commissions. Laws and regulations in many states restrict the manner in which a licensed entity can interact with affiliates, transfer assets, issue debt and engage in other business activities. Many acquisitions and divestitures require approval by the FCC and some state commissions. These agencies typically have the authority to withhold their approval, or to request or impose substantial conditions upon the transacting parties in connection with granting their approvals.

The following description discusses some of the major industry regulations that affect our traditional telephone operations, but numerous other regulations not discussed below could also impact us. Some legislation and regulations are currently the subject of judicial, legislative and administrative proceedings which could substantially change the manner in which the telecommunications industry operates and the amount of revenues we receive for our services. Neither the outcome of these proceedings, nor their potential impact on us, can be predicted at this time. For additional information, see "Risk Factors" in Item 1A of Part I of this annual report.

The laws and regulations governing our affairs are quite complex and occasionally in conflict with each other. From time to time, we are fined for failing to meet applicable regulations or service requirements.

### Federal Regulation

#### General

We are required to comply with the Communications Act of 1934. Among other things, this law requires our incumbent local exchange carriers ("ILECs") to offer various of our legacy services at just and reasonable rates and on non-discriminatory terms. The Telecommunications Act of 1996 materially amended the Communications Act of 1934, primarily to promote competition.

The FCC regulates interstate services we provide, including the special access charges we bill for wholesale network transmission and the interstate access charges that we bill to long-distance companies and other communications companies in connection with the origination and termination of interstate phone calls. Additionally, the FCC regulates a number of aspects of our business related to privacy, homeland security and network infrastructure, including our access to and use of local telephone numbers and our provision of emergency 911 services. The FCC has responsibility for maintaining and administering support programs designed to expand nationwide access to communications services (which are described further below), as well as other programs supporting service to low-income households, schools and libraries, and rural health care providers. Changes in the composition of the five members of the FCC or its Chairman can have significant impacts on the regulation of our business.

In recent years, our operations and those of other telecommunications carriers have been further impacted by legislation and regulation imposing additional obligations on us, particularly with regards to providing voice and broadband service, bolstering homeland security, increasing disaster recovery requirements, minimizing environmental impacts and enhancing privacy. These laws include the Communications Assistance for Law Enforcement Act, and laws governing local telephone number portability and customer proprietary network information requirements. In addition, the FCC has heightened its focus on the reliability of emergency 911 services. The FCC has imposed fines on us and other companies for 911 outages and has adopted new compliance requirements for providing 911 service. We are incurring capital and operating expenses designed to comply with the FCC's new requirements and minimize future outages. All of these laws and regulations may cause us to incur additional costs and could impact our ability to compete effectively against companies not subject to the same regulations.

Over the past several years, the FCC has taken various actions and initiated certain proceedings designed to comprehensively evaluate the proper regulation of the provisions of data services to businesses. As part of its evaluation, the FCC has reviewed the rates,

terms and conditions under which these services are provided. The FCC's proceedings remain pending, and their ultimate impact on us is currently unknown.

In 2015, the FCC issued an order regulating the manner in which ILECs can discontinue or reduce certain copper-based services. This order requires ILECs to provide prior notice to certain customers of their proposed change in services, and in certain cases to provide replacement offerings on reasonably comparable terms and conditions. We expect that this order will limit our flexibility to react to changing conditions in the communications industry.

### **Intercarrier Compensation and Universal Service**

For decades, the FCC has regularly considered various intercarrier compensation reforms, generally with a goal to create a uniform mechanism to be used by the entire telecommunications industry for payments between carriers originating, terminating, or carrying telecommunications traffic. The FCC has also traditionally administered support programs designed to promote the deployment of voice and broadband services in high-cost rural areas of the country.

In October 2011, the FCC adopted the Connect America and Intercarrier Compensation Reform order ("the 2011 order"), intended to reform the existing regulatory regime to recognize ongoing shifts to new technologies, including VoIP, and to re-direct universal service funding to foster nationwide broadband coverage. The 2011 order provides for a multi-year transition as terminating intercarrier compensation charges are reduced, universal service funding is explicitly targeted to broadband deployment, and line charges paid by end user customers are increased. These changes have increased the pace of reductions in the amount of switched access revenues related to our wholesale services, while creating opportunities for increased federal USF support and retail revenue funding.

In late 2011, numerous parties filed a petition for reconsideration with the FCC seeking numerous revisions to the 2011 order. Future judicial challenges to the 2011 order are also possible, which could alter or delay the FCC's proposed changes. In addition, based on the outcome of the FCC proceedings, various state commissions may consider changes to their universal service funds or intrastate access rates. Rulemaking designed to implement the order is not complete, and several FCC proceedings relating to the 2011 order remain pending. For these and other reasons, we cannot predict the ultimate impact of these proceedings at this time.

As a result of the 2011 order, a new Universal Service program was created to deploy broadband to unserved and underserved rural areas utilizing the Connect America Fund or "CAF". The CAF substantially replaces interstate USF funding, that we previously utilized to support voice services in high-cost rural markets. There are two phases to the CAF program, CAF Phase 1, a one-time broadband grant program, and CAF Phase 2, which is a multi-year recurring subsidy program for more extensive broadband deployment in price-cap ILEC territories.

In 2015, we accepted CAF funding from the FCC of approximately \$500 million per year for six years to fund the deployment of voice and broadband capable infrastructure for approximately 1.2 million rural households and businesses in 33 states of the 37 states in which we are an ILEC under the CAF Phase 2 high-cost support program. The funding from the CAF Phase 2 support program in these 33 states has substantially replaced the funding from the interstate USF high-cost program that we previously utilized to support voice services in high-cost rural markets in these 33 states. In late 2015, we began receiving these support payments from the FCC under the new CAF Phase 2 support program, which included (i) monthly support payments at a higher rate than under the interstate USF support program and (ii) a substantial one-time transitional payment, designed to align the prior USF payments with the new CAF Phase 2 payments for the full year 2015. For additional information on the payments we have thus far received under this program, see "Management's Discussion and Analysis of Financial Conditions and Results of Operations" in Item 7 of Part II of this annual report.

As a result of accepting CAF Phase 2 support payments for 33 states, we will be obligated to make substantial capital expenditures to build infrastructure by certain specified milestone deadlines. Future funding is contingent upon our compliance with these infrastructure buildout commitments and certain other service requirements, including certain minimum upload and download transmission speed requirements. In addition, if we are not in compliance with FCC measures at the end of the six-year CAF Phase 2 period, we will have 12 months to attain full compliance. If we are not in full compliance after the additional 12 months, we would incur a penalty equal to 1.89 times the average amount of support per location received in the state over the six-year term, plus a potential penalty of 10% of the total CAF Phase 2 support over the six-year term for the state. For information on the risks associated with participating in this program, see "Risk Factors—Risks Relating to Legal and Regulatory Matters" in Item 1A of Part I of this annual report.

For additional information about the potential financial impact of the CAF Phase 2 program, see "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 of Part II of this annual report.

## **Broadband Regulation**

In February 2015, the FCC adopted new regulations that regulate Internet services as a public utility under Title II of the Communications Act of 1934. In 2016, that order was upheld by a court of appeals. We anticipate that these regulations and any related rules may be reviewed by Congress. In addition, the newly-constituted FCC may reconsider these regulations. At this time, we cannot estimate the impact this may have on our business.

In 2015, the FCC adopted a broadband standard of 25 megabits per second download speed and 3 megabits per second of upload speed. At this time, we are not aware of any regulatory mandates requiring us to deploy this target speed. The new target is simply a benchmark by which the FCC will evaluate broadband deployment progress in the future. However, the FCC could attempt to utilize this broadband speed target in future regulatory proceedings, and our failure to attain these speeds in certain markets could place us at a marketing disadvantage.

## **State Regulation**

In recent years, most states have reduced their regulation of ILECs. Nonetheless, state regulatory commissions generally continue to regulate local service rates, intrastate access charges, state universal service funds and in some cases service quality. We are generally regulated under various forms of alternative regulation that typically limit our ability to increase rates for stand-alone, basic local voice service, but relieve us from the requirement to meet certain earnings tests. In a number of states, we have gained pricing freedom for the majority of retail services other than stand-alone basic consumer voice service. In most of the states in which we operate, we have gained pricing flexibility for certain enhanced calling services, such as caller identification and for bundled services that also include local voice service.

Under state law, our telephone operating subsidiaries are typically governed by laws and regulations that (i) regulate the purchase and sale of ILECs, (ii) prescribe certain reporting requirements, (iii) require ILECs to provide service under publicly-filed tariffs setting forth the terms, conditions and prices of regulated services, (iv) limit ILECs' ability to borrow and pledge their assets, (v) regulate transactions between ILECs and their affiliates and (vi) impose various other service standards.

Unlike many of our competitors, as an ILEC we generally face "carrier of last resort" obligations which include an ongoing requirement to provide service to all prospective and current customers in our service area who request service and are willing to pay rates prescribed in our tariffs. In certain situations, this may constitute a competitive disadvantage to us if competitors can choose to focus on low-cost profitable customers and withhold service from high-cost unprofitable customers. In addition, strict adherence to carrier-of-last-resort requirements may force us to construct facilities with a low likelihood of attractive economic return.

We operate in states where traditional cost recovery mechanisms, including rate structures, are under evaluation or have been modified. As laws and regulations change, there can be no assurance that these mechanisms will continue to provide us with any cost recovery.

For several years, we have faced various carrier complaints, legislation or other investigations regarding our intrastate switched access rates in several of our states. The outcomes of these disputes cannot be determined at this time. If we are required to reduce our intrastate switched access rates as a result of any of these disputes or state initiatives, we will seek to recover displaced switched access revenues from state universal service funds or other services. However, the amount of such recovery, particularly from residential customers, is not assured.

## **Other Regulations**

We are subject to federal and state regulations of customer service standards related to Prism TV. The FCC adopted customer service standards that we must meet in all of our Prism TV markets. The FCC has largely delegated its enforcement powers to local franchise authorities, who have the ability to adopt more stringent standards. We are subject to penalties in many of our local franchise agreements if we fail to meet applicable customer service standards.

Certain of our telecommunications, colocation and hosting services conducted in foreign countries are or may become subject to various foreign laws. Some of the legal requirements governing our foreign operations are more restrictive than or conflict with those governing our domestic operations, which raises our compliance costs and regulatory risks.

Various foreign, federal and state laws govern our storage, maintenance and use of customer data, including a wide range of consumer protection, data protection, privacy, intellectual property and similar laws. The application, interpretation and enforcement of these laws are often uncertain, and may be interpreted and applied inconsistently from jurisdiction to jurisdiction. Various foreign, federal and state legislative or regulatory bodies have recently adopted increasingly restrictive laws or regulations governing the protection or retention of data, and others are contemplating similar actions.

For additional information about these matters, see "Risk Factors—Risks Affecting Our Business" and "Risk Factors—Risks Relating to Legal and Regulatory Matters" in item 1A of Part I of this annual report.

## Competition

### General

We compete in a rapidly evolving and highly competitive market, and we expect intense competition to continue. In addition to competition from larger national telecommunications providers, we are facing increasing competition from several other sources, including cable and satellite companies, wireless providers, technology companies, cloud companies, broadband providers, device providers, resellers, sales agents and facilities-based providers using their own networks as well as those leasing parts of our network. Technological advances and regulatory and legislative changes have increased opportunities for a wide range of alternative communications service providers, which in turn have increased competitive pressures on our business. These alternate providers often face fewer regulations and have lower cost structures than we do. In addition, the communications industry has, in recent years, experienced substantial consolidation, and some of our competitors in one or more lines of our business are generally larger, have stronger brand names, have more financial and business resources and have broader service offerings than we currently do.

Wireless telephone services are a significant source of competition with our legacy ILEC services. It is increasingly common for customers to completely forego use of traditional wireline phone service and instead rely solely on wireless service for voice services. We anticipate this trend will continue, particularly as our older customers are replaced over time with younger customers who are less accustomed to using traditional wireline voice services. Technological and regulatory developments in wireless services, Wi-Fi, and other wired and wireless technologies have contributed to the development of alternatives to traditional landline voice services. Moreover, the growing prevalence of electronic mail, text messaging, social networking and similar digital non-voice communications services continues to reduce the demand for traditional landline voice services. These factors have led to a long-term systemic decline in the number of our wireline voice service customers.

The Telecommunications Act of 1996, which obligates ILECs to permit competitors to interconnect their facilities to the ILEC's network and to take various other steps that are designed to promote competition, imposes several duties on an ILEC if it receives a specific request from another entity which seeks to connect with or provide services using the ILEC's network. In addition, each ILEC is obligated to (i) negotiate interconnection agreements in good faith, (ii) provide nondiscriminatory "unbundled" access to all aspects of the ILEC's network, (iii) offer resale of its telecommunications services at wholesale rates and (iv) permit competitors, on terms and conditions (including rates) that are just, reasonable and nondiscriminatory, to colocate their physical plant on the ILEC's property, or provide virtual colocation if physical colocation is not practicable. Current FCC rules require ILECs to lease a network element only in those situations where competing carriers genuinely would be impaired without access to such network elements, and where the unbundling would not interfere with the development of facilities-based competition.

As a result of these regulatory, consumer and technological developments, ILECs also face competition from competitive local exchange carriers, or CLECs, particularly in densely populated areas. CLECs provide competing services through reselling an ILEC's local services, through use of an ILEC's unbundled network elements or through their own facilities.

Technological developments have led to the development of new products and services that have reduced the demand for our traditional services, as noted above, or that compete with traditional ILEC services. Technological improvements have enabled cable television companies to provide traditional circuit-switched telephone service over their cable networks, and several national cable companies have aggressively marketed these services. Similarly, companies providing VoIP services provide voice communication services over the Internet which compete with our traditional telephone service and our own VoIP services. In addition, demand for our broadband services could be adversely affected by advanced wireless data transmission technologies being deployed by wireless providers and by certain technologies permitting cable companies and other competitors to deliver faster average broadband transmission speeds than ours.

Similar to us, many cable, technology or other communications companies that previously offered a limited range of services are now offering diversified bundles of services, either through their own networks, reselling arrangements or joint ventures. As such, a growing number of companies are competing to serve the communications needs of the same customer base. Such activities will continue to place downward pressure on the demand for and pricing of our services.

As both residential and business customers increasingly demand high-speed connections for entertainment, communications and productivity, we expect the demands on our network will continue to increase over the next several years. To succeed, we must

continue to invest in our networks to ensure that they can deliver competitive services that meet these increasing bandwidth and speed requirements. In addition, network reliability and security are increasingly important competitive factors in our business.

In addition to facing direct competition from those providers described above, ILECs increasingly face competition from alternate communication systems constructed by long distance carriers, large customers, municipalities or alternative access vendors. These systems are capable of originating or terminating calls without use of an ILEC's networks or switching services. Other potential sources of competition include non-carrier systems that are capable of bypassing ILECs' local networks, either partially or completely, through various means, including the provision of special access or independent switching services and the concentration of telecommunications traffic on a few of an ILEC's access lines. We anticipate that all these trends will continue and lead to decreased billable use of our networks.

Additional information about competitive pressures is located (i) under the heading "Risk Factors—Risks Affecting Our Business" in Item 1A of Part I of this annual report and (ii) in the discussion immediately below, which contains more specific information on how these trends in competition have impacted our segments.

## ***Business Segment***

### **Strategic Services**

In connection with providing strategic services to our business customers, which includes our small, medium and enterprise business, wholesale and governmental customers, we compete against other telecommunication providers, as well as other regional and national carriers, other data transport providers, cable companies, CLECs and other enterprises, some of whom are substantially larger than us. Competition is based on price, bandwidth, quality and speed of service, promotions and bundled offerings. In providing broadband services, we compete primarily with cable companies, wireless providers, technology companies and other broadband service providers. We face competition in Ethernet based services in the wholesale market from cable companies and fiber based providers.

Our competitors for providing integrated data, broadband, voice services and other IT services to our business customers range from mid-sized businesses to large enterprises. Due to the size and capacity of some of these companies, our competitors may be able to offer more inexpensive solutions to our customers. To compete, we focus on providing sophisticated, secure and performance-driven services to our business customers through our global infrastructure.

The number of companies providing business services has grown and increased competition for these services, particularly with respect to smaller business customers. Many of our competitors for strategic services are not subject to the same regulatory requirements as we are and therefore they are able to avoid significant regulatory costs and obligations.

Our competitors for cloud, hosting, colocation and other IT services include telecommunications companies, technology companies, cloud companies, colocation companies, hardware manufacturers and system integrators that support the in-house IT operations for a business or offer outsourcing solutions. Due to the size, capacity and strategically low pricing tactics of some of these companies, our competitors may be able to offer more inexpensive solutions to our customers. The increase in recent years in the number of companies providing these services has placed substantial downward pressure on pricing for a wide range of cloud, hosting, colocation and other IT services. We believe, however, that our hybrid IT services capabilities, which offer multiple products and services (including network services), could help differentiate our products and services from those offered by competitors with a narrower range of products and services. We have remained focused on expanding our hybrid cloud capabilities through internal product development and strategic acquisitions of select startup businesses.

### **Legacy Services**

We face intense competition with respect to our legacy services and continue to see customers migrating away from these services and into strategic services. In addition, our legacy services revenues have been, and we expect they will continue to be, adversely affected by product substitution, technological migration and price competition. For our wholesale customers, we will continue to be adversely affected by product substitution, technological migration, industry consolidation and mandated rate reductions. Competition for private line services is based on price, network reach and reliability, service, promotions and bundled offerings. We face significant competition for access services from CLECs, cable companies, resellers and wireless service providers as well as some of our own wholesale markets customers, many of which are deploying their own networks to provide customers with local services. By doing so, these competitors reduce revenue producing traffic on our network.

### **Data Integration**

In providing data integration to our business customers, we compete primarily with large integrators, equipment providers and national telecommunication providers. Competition is based on package offerings, and as such we focus on providing these customers individualized and customizable packages. Our strategy is to provide our data integration through packages that include other strategic and legacy services. As such, in providing data integration we often face many of the same competitive pressures as we face in providing strategic and legacy services, as discussed above.

We expect data integration revenues to continue to fluctuate from quarter to quarter as this offering tends to be more sensitive than others to changes in the economy and in spending trends of our governmental customers. We further expect the profit margins on our data integration offerings to continue to be lower than those of our strategic and legacy services.

### *Consumer Segment*

#### **Strategic Services**

With respect to providing our strategic services to residential customers, competition is based on price, bandwidth, quality and speed of service, promotions and bundled offerings. Wireless carriers' latest generation technologies are allowing them to more directly compete with our strategic services. The manner in which we compete for broadband customers in this segment is substantially similar to the manner in which we compete for business customers, as described in the above section. In reselling DIRECTV video services, we compete primarily with cable and other satellite companies as well as other sales agents and resellers. Our Prism TV residential video service faces substantial competition from a variety of competitors, including well-established cable companies, satellite companies and several national companies that deliver content over the Internet and on mobile devices. Many of our competitors for these strategic services are not subject to the same regulatory requirements as we are, and therefore are able to avoid significant regulatory costs and obligations.

Our strategy for maintaining and increasing our base of broadband customers is based on pricing, packaging of services and features and quality of service. In order to remain competitive, we believe continually increasing connection speeds is important. As a result, we continue to invest in our network, which allows for the delivery of higher speed broadband services. We also continue to expand our marketing and product bundling efforts by offering a variety of bundled products and services with various pricing discounts, as we compete in a maturing market in which a significant portion of consumers already have broadband services. We offer these bundled products and services through various sales and marketing opportunities as further described above under the heading "Sales and Marketing."

#### **Legacy Services**

Although our status as an ILEC continues to provide us advantages in providing local services in our local service area, as noted above, we increasingly face significant competition as an increasing number of consumers are willing to substitute cable, wireless and electronic communications for traditional voice telecommunications services. This has led to an increase in the number and type of competitors within our industry, price compression and a decrease in our market share. As a result of this product substitution, we face greater competition in providing local and long-distance voice services from wireless providers, resellers and sales agents (including ourselves), social media hosts and broadband service providers, including cable companies. We also continue to compete with traditional telecommunications providers, such as national carriers, smaller regional providers, CLECs and independent telephone companies.

Our strategy to manage access line loss is based primarily on our pricing, packaging of services and features and quality of service. While bundle price discounts have resulted in lower average revenues for our individual services, we believe service bundles continue to positively impact our customer retention.

#### **Acquisitions and Dispositions**

We regularly evaluate the possibility of acquiring additional assets or disposing of assets in exchange for cash, securities or other properties, and at any given time may be engaged in discussions or negotiations regarding additional acquisitions or dispositions. We generally do not announce our acquisitions or dispositions until we have entered into a preliminary or definitive agreement.

During 2016, we acquired all of the outstanding stock of three companies for total consideration of \$53 million, including future deferred or contingent cash payments of \$14 million, of which \$49 million has initially been attributed to goodwill. These acquisitions were consummated to expand the product offerings of our then business segment, and therefore, the goodwill was assigned to that segment. The majority of the goodwill is attributed primarily to expected future increases in revenue from the sale of new products. The majority of the goodwill from these acquisitions is expected to be deductible for tax purposes. See Note 4—Goodwill, Customer Relationships and Other Intangible Assets for additional information on these acquisitions.

## Environmental Compliance

From time to time we may incur environmental compliance and remediation expenses, mainly resulting from owning or operating prior industrial sites or operating vehicle fleets or power supplies for our communications equipment. Although we cannot assess with certainty the impact of any future compliance and remediation obligations or provide you with any assurances regarding the ultimate impact thereof, we do not currently believe that future environmental compliance and remediation expenditures will have a material adverse effect on our financial condition or results of operations. For additional information, see "Risk Factors—Risks Relating to Legal and Regulatory Matters—Risks posed by other regulation" in Item 1A of Part I of this annual report and Note 16—Commitments and Contingencies included in Item 8 of Part II of this annual report.

## Seasonality

Overall, our business is not materially impacted by seasonality. Our network-related operating expenses are, however, generally higher in the second and third quarters of the year. From time to time, weather related problems have resulted in increased costs to repair our network and respond to service calls in some of our markets. The amount and timing of these costs are subject to the weather patterns of any given year, but have generally been highest during the third quarter and have been related to damage from severe storms, including hurricanes, tropical storms and tornadoes in our markets along the Atlantic and Gulf of Mexico coastlines.

## Employees

At December 31, 2016, we had approximately 40,000 employees, of which approximately 15,000 are members of either the Communications Workers of America ("CWA") or the International Brotherhood of Electrical Workers ("IBEW"). See the discussion of risks relating to our labor relations in "Risk Factors—Risks Affecting Our Business" in Item 1A of Part I of this annual report and see Note 18—Labor Union Contracts to our consolidated financial statements in Item 8 of Part II of this annual report for additional information on the timing of certain contract expirations.

Over the last several years, we have reduced our workforce primarily due to (i) increased competitive pressures, (ii) the loss of access lines and related legacy revenues, (iii) cost reduction initiatives, (iv) process improvements through automation and (v) integration efforts from our acquisitions.

## Website Access and Important Investor Information

Our website is [www.centurylink.com](http://www.centurylink.com). We routinely post important investor information in the "Investor Relations" section of our website at [ir.centurylink.com](http://ir.centurylink.com). The information contained on, or that may be accessed through, our website is not part of this annual report. You may obtain free electronic copies of our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports in the "Investor Relations" section of our website ([ir.centurylink.com](http://ir.centurylink.com)) under the heading "SEC Filings." These reports are available on our website as soon as reasonably practicable after we electronically file them with the SEC. From time to time we also use our website to webcast our earnings calls and certain of our meetings with investors or other members of the investment community.

We have adopted a written code of conduct that serves as the code of ethics applicable to our directors, officers and employees, in accordance with applicable laws and rules promulgated by the SEC and the New York Stock Exchange. In the event that we make any changes (other than by a technical, administrative or non-substantive amendment) to, or provide any waivers from, the provisions of our code of conduct applicable to our directors or executive officers, we intend to disclose these events on our website or in a report on Form 8-K filed with the SEC. The code of conduct, as well as copies of our guidelines on significant governance issues and the charters of our key board committees, are also available in the "Corporate Governance" section of our website at [www.centurylink.com/Pages/AboutUs/Governance/](http://www.centurylink.com/Pages/AboutUs/Governance/) or in print to any shareholder who requests them by sending a written request to our Corporate Secretary at CenturyLink, Inc., 100 CenturyLink Drive, Monroe, Louisiana, 71203.

Investors may also read and copy any materials filed with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. For information on the operation of the Public Reference Room, you are encouraged to call the SEC at 1-800-SEC-0330. For all of our electronic filings, the SEC maintains a website at [www.sec.gov](http://www.sec.gov) that contains reports, proxy statements and other information regarding issuers that file electronically with the SEC.

In connection with filing this annual report, our chief executive officer and chief financial officer made the certifications regarding our financial disclosures required under the Sarbanes-Oxley Act of 2002, and its related regulations. In addition, during

2016, our chief executive officer certified to the New York Stock Exchange that he was unaware of any violations by us of the New York Stock Exchange's corporate governance listing standards.

We typically disclose material non-public information by disseminating press releases, making public filings with the SEC, or disclosing information during publicly accessible meetings or conference calls. Nonetheless, from time to time we have used, and intend to continue to use, our website and social media accounts to augment our disclosures.

### Special Note Regarding Forward-Looking Statements and Related Matters

This annual report and other documents filed by us under the federal securities law include, and future oral or written statements or press releases by us and our management may include, forward-looking statements about our business, financial condition, operating results and prospects. These statements constitute "forward-looking" statements as defined by, and are subject to the "safe harbor" protections under, the federal securities laws. These statements include, among others:

- forecasts of our anticipated future results of operations or financial position;
- statements concerning the impact of our transactions, investments, product development and other initiatives, including our pending acquisitions and dispositions and our participation in government programs;
- statements about our liquidity, tax position, tax rates, asset values, contingent liabilities, growth opportunities and growth rates, acquisition and divestiture opportunities, business prospects, regulatory and competitive outlook, investment and expenditure plans, business strategies, dividend and stock repurchase plans, capital allocation plans, financing alternatives and sources, and pricing plans; and
- other similar statements of our expectations, beliefs, future plans and strategies, anticipated developments and other matters that are not historical facts, many of which are highlighted by words such as "may," "would," "could," "should," "plan," "believes," "expects," "anticipates," "estimates," "projects," "intends," "likely," "seeks," "hopes," or variations or similar expressions.

These forward-looking statements are based upon our judgment and assumptions as of the date such statements are made concerning future developments and events, many of which are beyond our control. These forward-looking statements, and the assumptions upon which they are based, (i) are not guarantees of future results, (ii) are inherently speculative and (iii) are subject to a number of risks and uncertainties. Actual events and results may differ materially from those anticipated, estimated, projected or implied by us in those statements if one or more of these risks or uncertainties materialize, or if our underlying assumptions prove incorrect. Factors that could affect actual results include but are not limited to:

- the effects of competition from a wide variety of competitive providers, including decreased demand for our legacy offerings and increased pricing pressures;
- the effects of new, emerging or competing technologies, including those that could make our products less desirable or obsolete;
- the effects of ongoing changes in the regulation of the communications industry, including the outcome of regulatory or judicial proceedings relating to intercarrier compensation, interconnection obligations, access charges, universal service, broadband deployment, data protection and net neutrality;
- our ability to (i) successfully complete our pending acquisition of Level 3, including the timely receipt of all requisite financing and all shareholder and regulatory approvals free of any detrimental conditions, and (ii) timely realize the anticipated benefits of the transaction, including our ability after the closing to attain anticipated cost savings, to use Level 3's net operating loss carryforwards in the amounts projected, to retain key personnel and to avoid unanticipated integration disruptions.
- our ability to effectively adjust to changes in the communications industry, and changes in the composition of our markets and product mix;
- possible changes in the demand for our products and services, including our ability to effectively respond to increased demand for high-speed broadband service;
- our ability to successfully maintain the quality and profitability of our existing product and service offerings, to provision

them successfully to our customers and to introduce new offerings on a timely and cost-effective basis;

- the adverse impact on our business and network from possible equipment failures, service outages, security breaches or similar events impacting our network;
- our ability to generate cash flows sufficient to fund our financial commitments and objectives, including our capital expenditures, operating costs, periodic share repurchases, dividends, pension contributions and other benefits payments, and debt repayments;

- changes in our operating plans, corporate strategies, dividend payment plans or other capital allocation plans, whether based upon changes in our cash flows, cash requirements, financial performance, financial position, market conditions or otherwise;
- our ability to effectively retain and hire key personnel and to successfully negotiate collective bargaining agreements on reasonable terms without work stoppages;
- increases in the costs of our pension, health, post-employment or other benefits, including those caused by changes in markets, interest rates, mortality rates, demographics or regulations;
- adverse changes in our access to credit markets on favorable terms, whether caused by changes in our financial position, lower debt credit ratings, unstable markets or otherwise;
- our ability to maintain favorable relations with our key business partners, suppliers, vendors, landlords and financial institutions;
- our ability to effectively manage our network buildout project and our other expansion opportunities;
- our ability to collect our receivables from financially troubled customers;
- any adverse developments in legal or regulatory proceedings involving us;
- changes in tax, communications, pension, healthcare or other laws or regulations, in governmental support programs, or in general government funding levels;
- the effects of changes in accounting policies or practices, including potential future impairment charges;
- the effects of adverse weather or other natural or man-made disasters;
- the effects of more general factors such as changes in interest rates, in operating costs, in general market, labor, economic or geo-political conditions, or in public policy; and
- other risks referenced in "Risk Factors" in Item 1A or elsewhere in this annual report or other of our filings with the SEC.

Additional factors or risks that we currently deem immaterial, that are not presently known to us or that arise in the future could also cause our actual results to differ materially from our expected results. Given these uncertainties, investors are cautioned not to unduly rely upon our forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements for any reason, whether as a result of new information, future events or developments, changed circumstances, or otherwise. Furthermore, any information about our intentions contained in any of our forward-looking statements reflects our intentions as of the date of such forward-looking statement, and is based upon, among other things, existing regulatory, technological, industry, competitive, economic and market conditions, and our assumptions as of such date. We may change our intentions, strategies or plans (including our dividend or other capital allocation plans) at any time and without notice, based upon any changes in such factors, in our assumptions or otherwise.

Investors should also be aware that while we do, at various times, answer questions raised by securities analysts, it is against our policy to disclose to them selectively any material non-public information or other confidential information. Accordingly, investors should not assume that we agree with any statement or report issued by an analyst with respect to our past or projected performance. To the extent that reports issued by securities analysts contain any projections, forecasts or opinions, such reports are not our responsibility.

Unless otherwise indicated, information contained in this annual report and other documents filed by us under the federal securities laws concerning our views and expectations regarding the communications industry are based on estimates made by us using data from industry sources, and on assumptions made by us based on our management's knowledge and experience in the markets in which we operate and the communications industry generally. You should be aware that we have not independently verified data from industry or other third-party sources and cannot guarantee its accuracy or completeness.



## ITEM IA. RISK FACTORS

The following discussion identifies the most significant risks or uncertainties that could (i) materially and adversely affect our business, financial condition, results of operations, liquidity or prospects or (ii) cause our actual results to differ materially from our anticipated results or other expectations. The following information should be read in conjunction with the other portions of this annual report, including "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 of Part II and our consolidated financial statements and related notes in Item 8 of Part II. Please note that the following discussion is not intended to comprehensively list all risks or uncertainties faced by us. Our operations or actual results could also be similarly impacted by additional risks and uncertainties that are not currently known to us, that we currently deem to be immaterial, that arise in the future or that are not specific to us, such as general economic conditions.

### Risks Affecting Our Business

*We may not be able to compete successfully against current or future competitors.*

Each of our offerings to our residential and business customers face increasingly intense competition from a variety of sources under evolving market conditions. We expect these trends will continue. In addition to competition from larger national telecommunications providers, we are facing increasing competition from several other sources, including cable and satellite companies, wireless providers, technology companies, cloud companies, broadband providers, device providers, resellers, sales agents and facilities-based providers using their own networks as well as those leasing parts of our network. In particular, (i) intense competition from wireless and other communications providers has led to a long-term systemic decline in the number of our wireline voice customers, (ii) strong competition from cable companies and others has impacted the growth of our broadband operations and (iii) aggressive competition from a wide range of technology companies and other market entrants has limited the prospects for our cloud computing operations. For more detailed information, see "Business—Competition" in Item I of Part I of this annual report.

Some of our current and potential competitors (i) offer products or services that are substitutes for our legacy wireline voice services, including wireless voice and non-voice communication services, (ii) offer a more comprehensive range of communications products and services, (iii) offer products or services with features that we cannot readily match in some or all of our markets, (iv) offer shorter installation intervals, allowing customers to begin receiving services sooner after ordering, (v) have greater marketing, engineering, research, development, technical, financial and other resources, (vi) have larger or more diverse networks with greater transmission capacity, (vii) conduct operations or raise capital at a lower cost than us, (viii) are subject to less regulation, which we believe enables such competitors to operate more flexibly than us with respect to certain offerings, (ix) offer services nationally or internationally to a larger geographic area or larger base of customers, (x) have substantially stronger brand names, which may provide them with greater pricing power than ours, or (xi) have larger operations than ours, which may enable them to compete more successfully in recruiting top talent, entering into operational or strategic partnerships or acquiring companies. Consequently, these competitors may be better equipped to provide more attractive offerings, to charge lower prices for their products and services, to develop and expand their communications and network infrastructure more quickly, to adapt more swiftly to changes in technologies or customer requirements, to devote greater resources to the marketing and sale of their products and services, to provide more comprehensive customer service, to provide greater resources to research and development initiatives and to take advantage of business or other opportunities more readily. In the past, several of our competitors and their operations have grown through acquisitions and aggressive product development. The continued growth of our competitors could further enhance their competitive positions.

Competition could adversely impact us in several ways, including (i) the loss of customers and market share, (ii) the possibility of customers terminating or reducing their usage of our services or shifting to less profitable services, (iii) reduced traffic on our networks, (iv) our need to expend substantial time or money on new capital improvement projects, (v) our need to lower prices or increase marketing expenses to remain competitive and (vi) our inability to diversify by successfully offering new products or services.

We are continually taking steps to respond to these competitive pressures, but these efforts may not be successful. Our operating results and financial condition would be adversely affected if these initiatives are unsuccessful or insufficient. If this occurred, our ability to pay our debt and other obligations and to re-invest in the business would also be adversely affected.

***Rapid technological changes could significantly impact our competitive and financial position.***

The communications industry has been and continues to be impacted by significant technological changes, which in general are enhancing wireless services and enabling a broader array of companies to compete with us. Many of these technological changes are (i) enabling customers to reduce or bypass use of our networks, (ii) displacing or reducing demand for our services, or (iii) enabling the development of competitive products or services. For years, improvements in wireless and Internet-based voice communications technologies have reduced demand for our legacy voice services, and these trends continue. More recently, continuous improvements in wireless data technologies have enabled wireless carriers to offer competing products, and we expect this trend to continue as technological advances enable these carriers to carry greater amounts of data faster and with less latency. Technological advancements have also permitted cable companies and other of our competitors to deliver faster average broadband transmission speeds than ours. Rapid changes in technology have also placed competitive pressures on our video, cloud and hosting businesses, and enabled new competitors to enter our markets. To enhance the competitiveness of certain of our services, we will likely be required to spend additional capital to install more fiber optic cable or to augment the capabilities of our copper-based services.

We may not be able to accurately predict or respond to changes in technology or industry standards, or to the introduction of newly-offered services. Any of these developments could make some or all of our offerings less desirable or even obsolete, which would place downward pressure on our market share and revenues. These developments could also require us to (i) expend capital or other resources in excess of currently contemplated levels, (ii) forego the development or provision of products or services that others can provide more efficiently, or (iii) make other changes to our operating plans, corporate strategies or capital allocation plans, any of which could be contrary to the expectations of our security holders or could adversely impact our operations. Our inability to effectively respond to technological changes could adversely affect our operating results and financial condition, as well as our ability to service debt and fund other commitments or initiatives.

Even if we succeed in adapting to changes in technology or industry standards by developing new products or services, there is no assurance that the new products or services would have a positive impact on our profit margins or financial performance.

In addition to introducing new technologies and offerings, we may need, from time to time, to phase out outdated and unprofitable technologies and services. If we are unable to do so on a cost-effective basis, we could experience reduced profits.

For additional information on the risks of increased expenditures, see "Risk Factors—Risks Affecting our Liquidity and Capital Resources—Our business requires us to incur substantial capital and operating expenses, which reduces our available free cash flow."

***Our legacy services continue to experience declining revenues, and our efforts to offset these declines may not be successful.***

Primarily as a result of the competitive and technological changes discussed above, we have experienced a prolonged systemic decline in our local voice, long-distance voice, network access, private line and other legacy revenues. Consequently, we have experienced lower consolidated revenues in each of our last several years.

We have taken a variety of steps to counter these declines in our legacy services revenues, including:

- an increased focus on selling a broader range of higher-growth strategic services, which are described in detail elsewhere in this annual report;
- an increased focus on serving a broader range of business, governmental and wholesale customers;
- greater use of service bundles; and
- acquisitions to increase our scale, enhance our business segment and strengthen our product offerings.

However, for the reasons described elsewhere in this annual report, most of our strategic services generate lower profit margins than our legacy services, and some can be expected to experience slowing growth as increasing numbers of our existing or potential customers subscribe to our newer strategic product and service offerings. Moreover, we cannot assure you that the revenues generated from our new offerings will offset revenue losses associated with our legacy services. In addition, our reliance on third parties to provide certain of these strategic services could constrain our flexibility, as described further below.

***Our failure to develop new products and services could adversely impact our competitive position.***

In order to compete effectively and respond to the changing communication needs of our customers, we continuously develop, test and introduce new products and services. Our ability to successfully introduce new product or service offerings on a timely and cost-effective basis could be constrained by a range of factors, including network limitations, support system limitations, limited capital, an inability to attract key personnel with the necessary skills, intellectual property constraints, testing delays, technological limits or an inability to act as quickly or efficiently as other competitors. In addition, new product or service offerings may not be widely accepted by our customers. Our business could be materially adversely affected if we are unable to timely and successfully develop and introduce new products or services.

***Our failure to continuously develop effective service support systems could adversely impact our competitive position.***

For many of our services, we can effectively compete only if we can quickly and efficiently (i) quote and accept customer orders, (ii) provision and initiate ordered services, (iii) provide customers with adequate means to manage their services and (iv) accurately bill for our services. Development of systems designed to support these tasks is a significant undertaking that continuously requires our personnel and third-party vendors to adjust to changes in our offerings and customers' preferences, to eliminate inconsistencies between the practices of our legacy operations and newly-acquired operations, to eliminate older support systems that are costly or obsolete, to develop uniform practices and procedures, and to automate them as much as possible. Our failure to continuously develop service support systems that are satisfactory to our current and potential customers could adversely impact our competitive position.

***We may not be able to successfully adjust to changes in our industry, our markets and our product mix.***

Ongoing changes in the communications industry have fundamentally changed consumers' communications expectations and requirements. In response to these changes, we have substantially altered our product and service offerings through acquisitions and internal product development. Many of these changes have placed a higher premium on sales, marketing and product development functions, and necessitated ongoing changes in our processes and operating protocols, as well as periodic reorganizations of our sales and leadership teams. In addition, we now offer a more complex range of products and services, operate larger and more complex networks and serve a much larger and more diverse set of customers. Consequently, we now face greater challenges in effectively managing and administering our operations and allocating capital and other resources to our various offerings. For all these reasons, we cannot assure you that our efforts to adjust to these changes will be timely or successful.

***Our revenues and cash flows may not be adequate to fund all of our current objectives.***

As noted in the risk factor disclosures appearing above and below, changes in competition, technology, regulation and demand for our legacy services continue to place downward pressure on our consolidated revenues and cash flows. During each of 2016, 2015, 2014 and 2013, we experienced declines in revenues and net cash provided by operating activities as compared to prior periods. Our cash flows will be further impacted by other changes discussed herein, including anticipated increases in our cash tax payments prior to the pending Level 3 acquisition and additional post-retirement health care payments as a result of the depletion in 2016 of substantially all of the post-retirement benefit plan trust assets.

We rely upon our consolidated revenues and cash flows to fund our commitments and business objectives, including without limitation, funding our capital expenditures, operating costs, debt repayments, dividends, periodic share repurchases, periodic pension contributions and other benefits payments. We cannot assure you that our future cash flows will be sufficient to fund all of our cash requirements in the manner currently contemplated. Our inability to fund certain of these payments could have an adverse impact on our business, operations or competitive position or on the value of our securities.

*We could be harmed by security breaches, damages or other significant disruptions or failures of our networks, information technology infrastructure or related systems, or of those we operate for certain of our customers.*

We are materially reliant upon our networks, information technology infrastructure and related technology systems (including our billing and provisioning systems) to provide products and services to our customers and to manage our operations and affairs. We face the risk, as does any company, of a security breach or significant disruption of our information technology infrastructure and related systems. As a communications company that transmits large amounts of information over communications networks, we face an added risk that a security breach or other significant disruption of our public networks or information technology infrastructure and related systems that we develop, install, operate and maintain for certain of our business customers (which includes our wholesale and governmental customers) could lead to material interruptions or curtailments of service. Moreover, in connection with processing and storing sensitive and confidential customer data, we face a heightened risk that a security breach or disruption could result in unauthorized access to our customers' proprietary information on our public networks or internal systems or the systems that we operate and maintain for certain of our customers.

We strive to maintain the security and integrity of information and systems under our control, and maintain contingency plans in the event of security breaches or other system disruptions. Nonetheless, we cannot assure you that our security efforts and measures will prevent unauthorized access to our systems, loss or destruction of data (including confidential customer information), account takeovers, unavailability of service, computer viruses, malware, distributed denial-of-service attacks, or other forms of cyber-attacks or similar events. These threats may derive from human error, hardware or software vulnerabilities, fraud, malice or sabotage on the part of employees, third parties or foreign nations, or could result from aging equipment or accidental technological failure. These threats may also arise from failure or breaches of systems owned, operated or controlled by other unaffiliated operators to the extent we rely on such other systems to deliver services to our customers.

Similar to other large telecommunications companies, we are a constant target of cyber-attacks of varying degrees. Although some of these attacks have resulted in security breaches, to date, none of these breaches have resulted in a material adverse effect on our operating results or financial condition. You should be aware, however, that defenses against cyber-attacks currently available to U.S. companies are unlikely to prevent intrusions by a highly-determined, highly-sophisticated hacker. Consequently, you should assume that we will be unable to implement security barriers or other preventative measures that repel all future cyber-attacks. Any such future security breaches or disruptions could materially adversely affect our business, results of operations or financial condition, especially in light of the growing frequency, scope and well-documented sophistication of cyber-attacks and intrusions.

Although we maintain insurance coverage that may, subject to policy terms and conditions (including self-insured deductibles, coverage restrictions and monetary coverage caps), cover certain aspects of our cyber risks, such insurance coverage may be unavailable or insufficient to cover our losses.

Additional risks to our network, infrastructure and related systems include:

- power losses or physical damage, whether caused by fire, flood, adverse weather conditions, terrorism, sabotage, vandalism or otherwise;
- capacity or system configuration limitations, including those resulting from changes in our customer's usage patterns, the introduction of new technologies or products, or incompatibilities between our newer and older systems;
- theft or failure of our equipment;
- software or hardware obsolescence, defects or malfunctions;
- deficiencies in our processes or controls;
- our inability to hire and retain personnel with the requisite skills to adequately maintain our systems;
- programming, processing and other human error; and
- service failures of our third-party vendors and other disruptions that are beyond our control.

Due to these factors, from time to time in the ordinary course of our business we experience disruptions in our service, and could experience more significant disruptions in the future.

Disruptions, security breaches and other significant failures of the above-described networks and systems could:

- disrupt the proper functioning of these networks and systems, which could in turn disrupt (i) our operational or administrative functions or (ii) the operations of certain of our customers who rely upon us to provide services critical to their operations;
- result in the unauthorized access to, and destruction, loss, theft, misappropriation or release of proprietary, confidential, sensitive, classified or otherwise valuable information of ours, our customers or our customers' end users, including trade secrets, which others could use for competitive, disruptive, destructive or otherwise harmful purposes and outcomes;
- require significant management attention or financial resources to remedy the resulting damages or to change our systems, including expenses to repair systems, add new personnel or develop additional protective systems;
- require us to notify customers, regulatory agencies or the public of data breaches;
- require us to provide credits for future service under certain service level commitments we have provided contractually to our customers or to offer expensive incentives to retain customers;
- subject us to claims for damages, fines, penalties, termination or other remedies under our customer contracts or service standards set by state regulatory commissions, which in certain cases could exceed our insurance coverage; or
- result in a loss of business, damage our reputation among our customers and the public generally, subject us to additional regulatory scrutiny or expose us to prolonged litigation.

*We could experience difficulties in expanding and updating our technical infrastructure.*

Our ability to expand and update our systems and information technology infrastructure in response to our growth and changing business needs is important to our ability to maintain and develop attractive product and service offerings. As discussed further under "Business—Network Architecture" in Item 1 of Part I of this annual report, we are currently undertaking several complex, costly and time-consuming projects to simplify and modernize our network, which combines our legacy network and the networks of companies we have acquired in the past. Unanticipated delays in the completion of these projects may lead to increased project costs or operational inefficiencies. In addition, there may be issues related to our expanded or updated infrastructure that are not identified by our testing processes, and which may only become evident after we have started to fully utilize the redesigned systems. Our failure to modernize and upgrade our technology infrastructure could have adverse consequences, including the delayed implementation of new service offerings, decreased competitiveness of existing service offerings, network instabilities, increased operating or acquisition integration costs, service or billing interruptions, and the diversion of development resources.

Any or all of the foregoing developments could have a negative impact on our business, results of operations, financial condition and cash flows.

*Negative publicity may adversely impact us.*

Outages or other service failures of networks operated by us or other operators could cause substantial adverse publicity affecting us specifically or our industry generally. In either case, media coverage and public statements that insinuate improper actions by us or other operators, regardless of their factual accuracy or truthfulness, may result in negative publicity, litigation, governmental investigations or additional regulations. Addressing negative publicity and any resulting litigation or investigations may distract management, increase costs and divert resources. Negative publicity may have an adverse impact on our reputation and the morale of our employees, which could adversely affect our business, results of operations, financial condition and cash flows.

*Market prices for many of our services have decreased in the past, and any similar price decreases in the future will adversely affect our revenues and margins.*

Over the past several years, a range of competitive and technological factors, including robust network construction and intense competition, have lowered market prices for many of our products and services. If these market conditions persist, we may need to continue to reduce prices to retain customers and revenue. If future price reductions are necessary, we will suffer unless we are able to offset these reductions by reducing our operating expenses or increasing our sales volumes.



***Our future growth potential will depend in part on the continued development and expansion of the Internet.***

Our future growth potential will depend in part upon the continued development and expansion of the Internet as a communication medium and marketplace for the distribution of data, video and other products by businesses, consumers, and governments. The use of the Internet for these purposes may not grow and expand at the rate anticipated by us or others, or may be restricted by factors outside of our control, including (i) actions by other carriers or governmental authorities that restrict us from delivering traffic over other parties' networks, (ii) changes in regulations, (iii) technological stagnation or (iv) changes in consumers' preferences or data usage.

***If we fail to hire and retain qualified executives, managers and employees, our operating results could be harmed.***

Our future success depends on our ability to identify, hire, train and retain executives, managers and employees with technological, engineering, product development, operational, provisioning, marketing, sales, administrative, managerial and other key skills. There is a shortage of qualified personnel in several of these fields. We compete with several other companies for this limited pool of potential employees. As our industry increasingly becomes more competitive, it could become especially difficult to attract and retain top personnel with skills in high demand. Our workforce reduction initiatives over the past couple of years have further increased the challenges of attracting and retaining talented individuals. In addition, subject to limited exceptions, none of our executives or domestic employees have long-term employment agreements. For all these reasons, there is no assurance that our efforts to recruit and retain qualified personnel will be successful.

***Increases in broadband usage may cause network capacity limitations, resulting in service disruptions, reduced capacity or slower transmission speeds for our customers.***

Video streaming services, gaming and peer-to-peer file sharing applications use significantly more bandwidth than other Internet activity such as web browsing and email. As use of these newer services continues to grow, our broadband customers will likely use much more bandwidth than in the past. If this occurs, we could be required to make significant capital expenditures to increase network capacity in order to avoid service disruptions, service degradation or slower transmission speeds for our customers. Alternatively, we could choose to implement network management practices to reduce the network capacity available to bandwidth-intensive activities during certain times in market areas experiencing congestion, which could negatively affect our ability to retain and attract customers in affected markets. While we believe demand for these services may drive broadband customers to pay for faster broadband speeds, competitive or regulatory constraints may preclude us from recovering the costs of the necessary network investments. This could result in an adverse impact to our operating margins, results of operations, financial condition and cash flows.

***We have been accused of infringing the intellectual property rights of others and will likely face similar accusations in the future, which could subject us to costly and time-consuming litigation or require us to seek third-party licenses.***

Like other communications companies, we have increasingly in recent years received a number of notices from third parties or have been named in lawsuits filed by third parties claiming we have infringed or are infringing upon their intellectual property rights. We are currently responding to several of these notices and claims and expect this industry-wide trend will continue. Responding to these claims may require us to expend significant time and money defending our use of the applicable technology, and divert management's time and resources away from other business. In certain instances, we may be required to enter into licensing agreements requiring royalty payments. In the case of litigation, we could be required to pay damages or cease using the applicable technology. If we are required to take one or more of these actions, our profit margins may decline or our operations could be impaired. In addition, in responding to these claims, we may be required to stop selling or redesign one or more of our products or services, which could significantly and adversely affect our business, results of operations, financial condition and cash flows.

Similarly, from time to time, we may need to obtain the right to use certain patents or other intellectual property from third parties to be able to offer new products and services. If we cannot license or otherwise obtain rights to use any required technology from a third party on reasonable terms, our ability to offer new products and services may be prohibited, restricted, made more costly or delayed.

***We may not be successful in protecting and enforcing our intellectual property rights.***

We rely on various patents, copyrights, trade names, trademarks, service marks, trade secrets and other similar intellectual property rights, as well as confidentiality procedures and contractual restrictions, to establish and protect our proprietary rights. The steps we have taken, however, may not prevent unauthorized use or the reverse engineering of our technology. Others may independently develop technologies that are substantially equivalent, superior to, or otherwise competitive to the technologies we employ in our services or that infringe on our intellectual property. We may be unable to prevent competitors from acquiring proprietary rights that are similar to or infringe upon our proprietary rights, or to prevent our current or former employees from using or disclosing to others our proprietary information. Enforcement of our intellectual property rights may depend on initiating legal actions against parties who infringe or misappropriate our proprietary information, but these actions may not be successful, even when our rights have been infringed. If we are unsuccessful in protecting or enforcing our intellectual property rights, our business, competitive position, results of operations and financial condition could be adversely affected.

***Our operations, financial performance and liquidity are materially reliant on various third parties.***

**Reliance on other communications providers.** To offer voice or data services in certain of our markets, we must either lease network capacity from, or interconnect our network with the infrastructure of, other communications carriers who typically compete against us in those markets. Our reliance on these lease or interconnection arrangements limits our control over the quality of our services and exposes us to the risk that our ability to market our services could be adversely impacted by changes in the plans or properties of the carriers upon which we are reliant. In addition, we are exposed to the risk that the other carriers may be unwilling to continue or renew these arrangements in the future on terms favorable to us, or at all. This risk is heightened when the other carrier is a competitor of ours and may benefit from terminating the agreement. If we lose these arrangements and cannot timely replace them, our ability to provide services to our customers and conduct our business could be materially adversely affected.

Conversely, certain of our operations carry a significant amount of voice or data traffic for other communications providers. Their reliance on our services exposes us to the risk that they may transfer all or a portion of this traffic from our network to networks built, owned or leased by them, thereby reducing our revenues. For additional information, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Segment Results" included in Item 7 of Part II of this annual report.

We also rely on reseller and sales agency arrangements with other communications companies to provide some of the services that we offer to our customers, including video services and wireless products and services. As a reseller or sales agent, we do not control the availability, retail price, design, function, quality, reliability, customer service or branding of these products and services, nor do we directly control all of the marketing and promotion of these products and services. Similar to the risks described above regarding our reliance upon other carriers, we could be adversely affected if these communication companies fail to maintain competitive products or services, or fail to continue to make them available to us on attractive terms, or at all.

Our operations and financial performance could be adversely affected if our relationships with any of these other communications companies are disrupted or terminated for any other reason, including if such other companies:

- become bankrupt or experience substantial financial difficulties;
- suffer work stoppages or other labor strife;
- challenge our right to receive payments or services under applicable regulations or the terms of our existing contractual arrangements; or
- are otherwise unable or unwilling to make payments or provide services to us.

**Reliance on other key suppliers and vendors.** We depend on a limited number of suppliers and vendors for equipment and services relating to our network infrastructure. Our local exchange carrier networks consist of central office and remote sites, all with advanced digital switches. If any of these suppliers experience interruptions or other problems delivering or servicing these network components on a timely basis, our operations could suffer significantly. To the extent that proprietary technology of a supplier is an integral component of our network, we may have limited flexibility to purchase key network components from alternative suppliers and may be adversely affected if third parties assert patent infringement claims against our suppliers or us. We also rely on a limited number of (i) software vendors to support our business management systems, (ii) content suppliers to provide programming to our video operations, and (iii) contractors to assist us in connection with our network construction and maintenance activities. In the event it becomes necessary to seek alternative suppliers and vendors, we may be unable to obtain satisfactory replacement supplies, services, utilities or programming on economically attractive terms, on a timely basis, or at all, which could increase costs or cause disruptions in our services.



**Reliance on utility providers and landlords.** Pending the sale of our colocation business, we operate a substantial number of data center facilities, which are susceptible to electrical power shortages or outages. Our energy costs can fluctuate significantly or increase for a variety of reasons, including changes in legislation and regulation. Several pending proposals designed to reduce greenhouse emissions could substantially increase our energy costs, which we may not be able to pass on to our customers. Due to the increasing sophistication of equipment and our products, our demand or our customers' demand for power may exceed the power capacity in older data centers, which may limit our ability to fully utilize these data centers.

Pending the sale of our colocation business, we lease most of our data centers. Although the majority of these leases provide us with the opportunity to renew the lease, many of these renewal options provide that rent for the renewal period will be equal to the fair market rental rate at the time of renewal. Any resulting increases in our rent costs could have a negative impact on our financial results. We cannot assure you that our data centers in the future will have access to sufficient space or power on attractive terms, or at all.

**Reliance on governmental payments.** We receive a material amount of revenue or government subsidies under various government programs, which are further described under the heading "Risk Factors—Risks Relating to Legal and Regulatory Matters." We also provide products or services to various federal, state and local agencies. Our failure to comply with complex governmental regulations and laws applicable to these programs, or the terms of our governmental contracts, could result in us being suspended or barred from future governmental programs or contracts for a significant period of time. Moreover, certain governmental agencies frequently reserve the right to terminate their contracts for convenience. If our governmental contracts are terminated for any reason, or if we are suspended or barred from governmental programs or contracts, our results of operations and financial condition could be materially adversely affected.

**Reliance on financial institutions.** We rely on a number of financial institutions to provide us with short-term liquidity under our credit facility. If one or more of these lenders default on their funding commitments, our access to revolving credit could be adversely affected.

*Rising costs, changes in consumer behaviors and other industry changes may adversely impact our video business.*

The costs of purchasing video programming have risen significantly in recent years and continue to rise. Moreover, an increasing number of consumers are receiving access to video content through video streaming or other services pursuant to new technologies for a nominal or no fee, which will likely reduce demand for more traditional video products, such as the satellite TV services that we resell and our Prism TV services.

New technologies are also affecting consumer behavior in ways that are changing how content is delivered and viewed. Increased access to various media through wireless devices has the potential to reduce the viewing of our content through traditional distribution outlets. These new technologies have increased the number of entertainment choices available to consumers and intensified the challenges posed by audience fragmentation. Some of these newer technologies also give consumers greater flexibility to watch programming on a time-delayed or on-demand basis. All of these changes, coupled with changing consumer preferences and other related developments, could reduce demand for our video products and services.

*If we fail to extend or renegotiate our collective bargaining agreements with our labor unions as they expire from time to time, or if our unionized employees were to engage in a strike or other work stoppage, our business and operating results could be materially harmed.*

As of December 31, 2016, approximately 38% of our employees were members of various bargaining units represented by the Communications Workers of America or the International Brotherhood of Electrical Workers. From time to time, our labor agreements with unions expire. Approximately 11,000, or 28%, of our employees are subject to collective bargaining agreements that are scheduled to expire October 7, 2017. Although we typically are able to negotiate new bargaining agreements, we cannot predict the outcome of our future negotiations of these agreements. We may be unable to reach new agreements, and union employees may engage in strikes, work slowdowns or other labor actions, which could materially disrupt our ability to provide services and result in increased cost to us. In addition, new labor agreements may impose significant new costs on us, which could impair our financial condition or results of operations in the future. To the extent they contain benefit provisions, these agreements may also limit our flexibility to change benefits in response to industry or competitive changes. In particular, post-employment benefits provided under these agreements could cause us to incur costs not faced by many of our competitors, which could ultimately hinder our competitive position.

*Portions of our property, plant and equipment are located on property owned by third parties.*

We rely on rights-of-way, colocation agreements and other authorizations granted by governmental bodies, railway companies, carriers and other third parties to locate our cable, conduit and other network equipment on or under their respective properties. A significant number of these authorizations are scheduled to lapse over the next five to ten years, unless we are able to extend or renew them. Our operations could be adversely affected if any of these authorizations terminate or lapse, or if the landowner requests price increases.

Over the past few years, certain utilities, cooperatives and municipalities in certain of the states in which we operate have requested significant rate increases for attaching our plant to their facilities. To the extent that these entities are successful in increasing the amount we pay for these attachments, our future operating costs will increase.

*Our business customers may seek to shift risk to us.*

We furnish to and receive from our business customers indemnities relating to damages caused or sustained by us in connection with certain of our operations. Our customers' changing views on risk allocation could cause us to accept greater risk to win new business or could result in us losing business if we are not prepared to take such risks. To the extent that we accept such additional risk, and seek to insure against it, our insurance premiums could rise.

*Our international operations expose us to various regulatory, currency, tax, legal and other risks.*

Our international operations are subject to U.S. and other laws and regulations regarding operations in foreign jurisdictions in which we provide services. These numerous and sometimes conflicting laws and regulations include anti-corruption laws, anti-competition laws, trade restrictions, tax laws, immigration laws, privacy laws and accounting requirements. Many of these laws are complex and change frequently. Regulations that require the awarding of contracts to local contractors or the employment of local citizens may adversely affect our flexibility or competitiveness in these jurisdictions. Local laws and regulations, and their interpretation and enforcement, differ significantly among those jurisdictions. There is a risk that these laws or regulations may materially restrict our ability to deliver services in various foreign jurisdictions or could be breached through inadvertence or mistake, fraudulent or negligent behavior of our employees or agents, failure to comply with certain formal documentation or technical requirements, or otherwise. Violations of these laws and regulations could result in fines and penalties, criminal sanctions against us or our personnel, or prohibitions on the conduct of our business or our ability to operate in one or more countries, any of which could have a material adverse effect on our business, reputation, results of operations, financial condition or prospects.

Many foreign laws and regulations relating to communications services are more restrictive than U.S. laws and regulations, particularly those relating to privacy rights and data retention. For example, all 28 member states of the European Union have adopted new European data protection laws that we believe could impact our operations in Europe and could potentially expose us to an increased risk of litigation or significant regulatory fines. Moreover, national regulatory frameworks that are consistent with the policies and requirements of the World Trade Organization have only recently been, or are still being, enacted in many countries. Accordingly, many countries are still in the early stages of providing for and adapting to a liberalized telecommunications market. As a result, in these markets we may encounter more protracted and difficult procedures to obtain licenses necessary to provide the full set of products and services we seek to offer.

In addition to these international regulatory risks, some of the other risks inherent in conducting business internationally include:

- tax, licensing, political or other business restrictions or requirements;
- uncertainty concerning import and export restrictions, including the risk of fines or penalties assessed for violations;
- longer payment cycles and problems collecting accounts receivable;
- domestic and foreign regulation of overseas operations, including regulation under the Foreign Corrupt Practices Act, or FCPA, as well as other anti-corruption laws;
- economic, social and political instability, with the attendant risks of terrorism, kidnapping, extortion, civic unrest and potential seizure or nationalization of assets;
- currency and exchange controls, repatriation restrictions and fluctuations in currency exchange rates;
- challenges in securing and maintaining the necessary physical and telecommunications infrastructure;

- the inability in certain jurisdictions to enforce contract rights either due to underdeveloped legal systems or government actions that result in a deprivation of contract rights;

- the inability in certain jurisdictions to adequately protect intellectual property rights;
- laws, policies or practices that restrict with whom we can contract or otherwise limit the scope of operations that can legally or practicably be conducted within any particular country;
- potential submission of disputes to the jurisdiction of a foreign court or arbitration panel;
- reliance on third parties, including those with which we have limited experience;
- limitations in the availability, amount or terms of insurance coverage;
- the imposition of unanticipated or increased taxes, increased communications or privacy regulations or other forms of public or governmental regulation that increase our operating expenses; and
- challenges in staffing and managing foreign operations.

Many of these risks are beyond our control, and we cannot predict the nature or the likelihood of the occurrence or corresponding effect of any such events, each of which could have an adverse effect on our financial condition and results of operations.

We do business and may in the future do additional business in certain countries or regions in which corruption is a serious problem. Moreover, in order to effectively compete in certain foreign jurisdictions, it is frequently necessary or required to establish joint ventures, strategic alliances or marketing arrangements with local operators, partners or agents. In certain instances, these local operators, partners or agents may have interests that are not always aligned with ours. Reliance on local operators, partners or agents could expose us to the risk of being unable to control the scope or quality of our overseas services or products, or being held liable under the FCPA or other anti-corruption laws for actions taken by our strategic or local partners or agents even though these partners or agents may not themselves be subject to the FCPA or other applicable anti-corruption laws. Any determination that we have violated the FCPA or other anti-corruption laws could have a material adverse effect on our business, results of operations, reputation or prospects.

*We may not be able in the future to acquire new businesses on attractive terms.*

Historically, much of our growth has been attributable to acquisitions. Our future ability to grow through additional acquisitions could be limited by several factors, including our leverage, debt covenants and inability to identify attractively-priced target companies. Moreover, we generally must devote significant management attention and resources to evaluate acquisition opportunities, which could preclude us from evaluating acquisition opportunities during periods when management is committed to other opportunities, tasks or activities. Accordingly, we cannot assure you that we will be able to attain future growth through acquisitions. See "Risks Relating to Our Pending Acquisition of Level 3" for a discussion of certain specific risks raised by our pending acquisition of Level 3 and see the next risk factor immediately below for a discussion of certain general risks raised by acquisitions.

*Any additional future acquisitions by us would subject us to additional business, operating and financial risks, the impact of which cannot presently be evaluated, and could adversely impact our capital structure or financial position.*

In an effort to implement our business strategies, we may from time to time in the future pursue other acquisition or expansion opportunities, including strategic investments. These transactions could involve acquisitions of entire businesses or investments in start-up or established companies, and could take several forms, including mergers, joint ventures, investments in new lines of business, or the purchase of equity interests or assets. These types of transactions may present significant risks and uncertainties, including the difficulty of identifying appropriate companies to acquire or invest in on acceptable terms, distraction of management from current operations, insufficient revenue acquired to offset liabilities assumed, unexpected expenses, inadequate return of capital, regulatory or compliance issues, potential infringements, potential violations of covenants in our debt instruments and other unidentified issues not discovered in due diligence. To the extent we acquire part or all of a business that is financially unstable or is otherwise subject to a high level of risk, we may be affected by currently unascertainable risks of that business. Accordingly, there is no current basis for you to evaluate the possible merits or risks of the particular business or assets that we may acquire. Moreover, we cannot guarantee that any such transaction will ultimately result in the realization of the benefits of the transaction originally anticipated by us or that any such transaction will not have a material adverse impact on our financial condition or results of operations. In particular, we can provide no assurances that we will be able to successfully integrate the technology systems, billing systems, accounting processes, sales force, cost structure, product development and service delivery processes, standards, controls, policies, strategies and culture of the acquired company with ours. In addition, the financing of any future acquisition completed by us could adversely impact our capital structure as any such financing would likely include the issuance of additional securities or the borrowing of additional funds.



Except as required by law or applicable securities exchange listing standards, we do not expect to ask our shareholders to vote on any proposed acquisition. Moreover, we generally do not announce our acquisitions until we have entered into a preliminary or definitive agreement.

*Unfavorable general economic conditions could negatively impact our operating results and financial condition.*

Unfavorable general economic conditions, including unstable economic and credit markets, could negatively affect our business. Worldwide economic growth has been sluggish since 2008, and many experts believe that a confluence of global factors may result in a prolonged period of economic stagnation, slow growth or economic uncertainty. While it is difficult to predict the ultimate impact of these general economic conditions, they could adversely affect demand for some of our products and services and could cause customers to shift to lower priced products and services or to delay or forego purchases of our products and services. These conditions impact, in particular, our ability to sell discretionary products or services to business customers that are under pressure to reduce costs or to governmental customers that have suffered substantial budget cuts in recent years. Any one or more of these circumstances could continue to depress our revenues. Also, our customers may encounter financial hardships or may not be able to obtain adequate access to credit, which could negatively impact their ability to make timely payments to us. In addition, as discussed further below, unstable economic and credit markets may preclude us from refinancing maturing debt at terms that are as favorable as those from which we previously benefited, at terms that are acceptable to us, or at all. For these reasons, among others, if current economic conditions persist or decline, our operating results, financial condition, and liquidity could be adversely affected.

For additional information about our business and operations, see "Business" in Item 1 of Part I of this annual report.

**Risks Relating to Our Pending Acquisition of Level 3**

*The completion of the Level 3 acquisition is subject to several conditions, including the receipt of consents and approvals from government entities, which may impose conditions that could have an adverse effect on the combined company or could cause the proposed transaction to be abandoned.*

The completion of the Level 3 acquisition is subject to a number of conditions, including, among others, the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act and the receipt of approvals from the FCC and certain other governmental entities. In deciding whether to grant some of these approvals, the relevant governmental entity will make a determination of whether, among other things, the transaction is in the public interest. We cannot provide any assurance that the necessary approvals will be obtained.

In addition, regulatory entities may impose certain requirements or obligations as conditions for their approval or in connection with their review. The merger agreement may require CenturyLink or Level 3 to accept conditions from these regulators that could adversely affect the combined company without either of CenturyLink or Level 3 having the right to refuse to close the acquisition on the basis of those regulatory conditions. While we are not required to accept conditions that would or would reasonably be likely to have a material adverse effect on the combined company (assuming for these purposes that the combined company is the size of CenturyLink), this assessment will be made at or prior to the closing and we cannot provide any assurance that any required conditions will not have a material adverse effect on the combined company following the proposed acquisition. In addition, we cannot provide any assurance that these conditions will not result in the abandonment of the acquisition.

It could take longer to receive the requisite governmental consents and approvals than currently anticipated. Any delay in completing the acquisition, whether caused by regulatory delays or otherwise, could cause us, Level 3, as well as the combined company, to incur extra transaction expenses or to delay or fail to realize fully the benefits that we currently expect to receive if the acquisition is successfully completed within the expected time frame.

***Failure to complete the acquisition could negatively affect our stock price and our future business and financial results.***

If the Level 3 acquisition is not completed, our ongoing businesses may be adversely affected and we will be subject to several risks, including the following:

- the possibility that we could be required to pay Level 3 a substantial termination fee and, in some cases, certain expenses of Level 3 if the acquisition is terminated under certain qualifying circumstances;
- the incurrence of costs and expenses relating to the proposed acquisition, such as financing, legal, accounting, financial advisor, filing, printing and mailing fees and expenses, including the potential expense reimbursement obligations described above;
- the possibility of a change in the trading price of our common stock to the extent current trading prices reflect a market assumption that the acquisition will be completed;
- the possibility that we could suffer potential negative reactions from our employees, customers or vendors; and
- the possibility that we could suffer adverse consequences associated with our management's focus on the acquisition instead of on pursuing other opportunities that could have been beneficial to us, without realizing any of the benefits contemplated by the acquisition.

In addition, if the acquisition is not completed, we could be subject to litigation related to any failure to complete the acquisition or to perform our obligations under the merger agreement.

If the acquisition is not completed, we cannot assure you that these risks will not materialize and will not materially affect our business financial results and stock price.

***Our merger agreement with Level 3 contains provisions that could discourage a potential competing acquirer of us or could result in any competing proposal being at a lower price than it might otherwise be.***

Our merger agreement with Level 3 contains "no-shop" provisions that, subject to limited exceptions, restrict our ability to solicit, encourage, facilitate or discuss competing third-party proposals to acquire all or a significant part of CenturyLink. In some circumstances on termination of the merger agreement, we may be required to pay a termination fee or expenses to Level 3. These provisions could discourage a potential competing acquirer that might have an interest in acquiring all or a significant part of us from considering or proposing that acquisition, even if it were prepared to pay an attractive purchase price, or might result in a potential competing acquirer proposing to pay a lower price than it might otherwise have proposed to pay because of the added expense of the termination fee or expenses that may become payable in certain circumstances. If the merger agreement is terminated and we attempt to seek another business acquisition, we may not be able to negotiate a transaction with another party on terms comparable or better than the terms of the Level 3 acquisition.

***The pendency of the Level 3 acquisition could adversely affect the business and operations of CenturyLink or Level 3.***

In connection with the pending Level 3 acquisition, some of the customers or vendors of CenturyLink or Level 3 may delay or defer decisions or reduce their level of business with either or both of the companies, any of which could negatively affect the revenues, earnings, cash flows and expenses of CenturyLink or Level 3, regardless of whether the acquisition is completed. Similarly, current and prospective employees of CenturyLink and Level 3 may experience uncertainty about their future roles with the combined company following the acquisition, which may materially adversely affect the ability of each of CenturyLink or Level 3 to attract and retain key management, sales, marketing, operational and technical personnel during the pendency of the acquisition. In addition, due to operating covenants in the merger agreement, each of CenturyLink and Level 3 may be unable, during the pendency of the acquisition, to pursue strategic transactions, undertake significant capital projects, undertake certain significant financing transactions and otherwise pursue other actions that are not in the ordinary course of business, even if such actions would prove beneficial. Any of these effects could have an adverse effect on the ability to generate revenue at anticipated levels prior to the completion of the acquisition. Moreover, the pursuit of the acquisition and the preparation for the integration of the companies may place a significant burden on the management and personnel of both companies. The diversion of management's attention away from operating the companies in the ordinary course could adversely affect CenturyLink's and Level 3's financial results.

***Current CenturyLink shareholders may have a reduced ownership and voting interest in the combined company after the Level 3 acquisition.***

CenturyLink expects to issue or reserve for issuance approximately 538 million shares of CenturyLink common stock to Level 3 stockholders in connection with the acquisition (including shares of CenturyLink common stock to be issued in connection with outstanding Level 3 equity awards). Upon completion of the Level 3 acquisition, each CenturyLink shareholder will remain a shareholder of CenturyLink with a percentage ownership of the combined company that may be smaller than the shareholder's percentage of CenturyLink prior to the transaction, depending upon such shareholder's current ownership of Level 3 shares. As a result of these potentially reduced ownership percentages, CenturyLink shareholders may have less voting power in the combined company than they now have with respect to CenturyLink.

***We expect to incur substantial expenses related to the Level 3 acquisition.***

We expect to incur substantial expenses in connection with completing the acquisition and integrating our business, operations, networks, systems, technologies, policies and procedures with those of Level 3. There are a large number of systems that will likely be integrated, including management information, purchasing, accounting and finance, sales, payroll and benefits, fixed asset, lease administration and regulatory compliance systems. While we have assumed that a certain level of transaction and integration expenses would be incurred, there are a number of factors beyond our control that could affect the total amount or the timing of our integration expenses. Many of the expenses that will be incurred, by their nature, are difficult to estimate accurately at the present time. Due to these factors, the transaction and integration expenses associated with the acquisition are likely in the near term to exceed the savings that we expect to achieve from the elimination of duplicative expenses and the realization of economies of scale and cost savings related to the integration of the businesses following the completion of the acquisition. As a result of these expenses, we expect to take charges against our earnings before and after the completion of the acquisition. The charges taken after the acquisition are expected to be significant, although the aggregate amount and timing of such charges are uncertain at present.

***Following the Level 3 acquisition, the combined company may be unable to integrate successfully our business and Level 3's business and realize the anticipated benefits of the acquisition.***

The proposed transaction involves the combination of two companies which currently operate as independent public companies. The combined company will be required to devote significant management attention and resources to integrating the business practices and operations of CenturyLink and Level 3. Potential difficulties the combined company may encounter in the integration process include the following:

- the inability to successfully combine our business and Level 3's business in a manner that permits the combined company to achieve the cost savings and operating synergies anticipated to result from the acquisition, which would result in the anticipated benefits of the acquisition not being realized in the time frame currently anticipated or at all;
- lost sales and customers as a result of certain customers of either of the two companies deciding to terminate or reduce their business with the combined company;
- the complexities associated with managing the combined businesses out of several different locations and integrating personnel from the two companies, while at the same time attempting to (i) provide consistent, high quality products and services under a unified culture and (ii) focus on other on-going transactions, including the pending divestiture of our data centers and colocation business and related transactions;
- the additional complexities of combining two companies with different histories, regulatory restrictions, operating structures and markets;
- the failure to retain key employees of either of the two companies;
- potential unknown liabilities and unforeseen increased expenses, delays or regulatory conditions associated with the acquisition; and
- performance shortfalls at one or both of the two companies as a result of the diversion of management's attention caused by completing the acquisition and integrating the companies' operations.

For all these reasons, you should be aware that it is possible that the integration process could result in the distraction of the combined company's management, the disruption of the combined company's ongoing business or inconsistencies in the combined company's products, services, standards, controls, procedures and policies, any of which could adversely affect the ability of the combined company to maintain relationships with customers, vendors and employees or to achieve the anticipated benefits of the acquisition, or could otherwise adversely affect the business and financial results of the combined company.



***Following the Level 3 acquisition, we may be unable to retain key employees.***

The success of the combined company after the acquisition will depend in part upon its ability to retain key Level 3 and CenturyLink employees. Key employees may depart either before or after the acquisition because of issues relating to the uncertainty and difficulty of integration or a desire not to remain with the combined company following the acquisition. Accordingly, no assurance can be given that we, Level 3 and, following the acquisition, the combined company will be able to retain key employees to the same extent as in the past.

***In connection with the Level 3 acquisition, we will incur and assume a substantial amount of indebtedness and the agreements that will govern the indebtedness to be incurred or assumed by us are expected to contain various covenants and other provisions that impose restrictions on our ability to operate.***

As a result of incurring the debt financing for the Level 3 acquisition and assuming Level 3's existing consolidated indebtedness in connection with the acquisition, we will become more leveraged. This could have material adverse consequences for us, including those listed below under the heading "Risks Affecting Our Liquidity and Capital Resources—Our high debt levels expose us to a broad range of risks."

The agreements that will govern the indebtedness to be incurred or assumed by us in connection with the acquisition are expected to contain certain affiliate guarantees and pledges of stock of certain affiliates and various affirmative and negative covenants that may, subject to certain significant exceptions, restrict the ability of us and certain of our subsidiaries to, among other things, pledge property, incur additional indebtedness, enter into sale and lease-back transactions, make loans, advances or other investments, make non-ordinary course asset sales, declare or pay dividends or make other distributions with respect to equity interest, merge or consolidate with any other person or sell or convey certain assets to any one person, among various other things. In particular, certain covenants contained in Level 3's indebtedness to be assumed by us may restrict our ability to distribute cash from Level 3 to other of our affiliated entities, or enter into other transactions among our wholly owned subsidiaries. In addition, some of the agreements that govern the debt financing are expected to contain financial covenants that will require us to maintain certain financial ratios. The ability of us and our subsidiaries to comply with these provisions may be affected by events beyond our and their control. Failure to comply with these covenants could result in an event of default, which, if not cured or waived, could accelerate our debt repayment obligations. Certain of our debt instruments have cross-default or cross-acceleration provisions. When present, these provisions could have a wider impact on liquidity than might otherwise arise from a default or acceleration of a single debt instrument. For additional information, see "Risks Affecting Our Liquidity and Capital Resources."

***Following the Level 3 acquisition, we plan to conduct rebranding initiatives that are likely to involve substantial costs and may not be favorably received by customers.***

Prior to the Level 3 acquisition, CenturyLink and Level 3 will each continue to market their respective products and services using the "CenturyLink" and "Level 3" brand names and logos. Following the acquisition, "CenturyLink" will be the brand name of the combined company. As a result, we expect to incur substantial costs in rebranding the combined company's products and services in those markets that previously used the "Level 3" name, and may incur write-offs associated with the discontinued use of Level 3's brand names. We cannot assure you that customers will be receptive to our proposed rebranding efforts. The failure of any of these initiatives could adversely affect our ability to attract and retain customers after the acquisition, resulting in reduced revenues.

***Consummation of the Level 3 acquisition will increase our exposure to the risk of operating internationally.***

CenturyLink and, to a greater extent, Level 3 conduct international operations, which expose each of them to the risks described under the heading "Risks Affecting Our Business—Our international operations expose us to various regulatory, currency, tax, legal and other risks." Consummation of the Level 3 acquisition will generally increase our exposure to these risks. In particular, our acquisition of Level 3 will increase our exposure to currency exchange rate risks and currency transfer restrictions. Moreover, the acquisition of Level 3's Latin American operations will expose CenturyLink to the economic and political risks of operating in those markets.

***Level 3 has only recently generated net income, and has generated substantial net losses in the past.***

As indicated in Level 3's consolidated financial statements included in its reports filed with the SEC, Level 3 has only generated net income for its three most recently completed full fiscal years, and generated substantial losses prior to then.



***Counterparties to certain significant agreements with Level 3 may exercise contractual rights to terminate such agreements following the Level 3 acquisition.***

Level 3 is a party to certain agreements that give the counterparty a right under certain conditions to terminate the agreement following a "change in control" of Level 3. Under most such agreements, the Level 3 acquisition will constitute a change in control and therefore the counterparty may terminate the agreement upon the closing of the acquisition, subject to the terms and conditions specified in such agreements. Level 3 has agreements subject to such termination provisions with significant customers, major suppliers and providers of services where Level 3 has acted as reseller or sales agent. In addition, certain Level 3 customer contracts, including those with state or federal government agencies, allow the customer to terminate the contract at any time for convenience, which would allow the customer to terminate its contract before, at or after the closing of the acquisition. Any such counterparty may request modifications of their respective agreements as a condition to foregoing exercise of their termination rights. There is no assurance that such agreements will not be terminated, that any such terminations will not result in a material adverse effect, or that any modifications of such agreements to avoid termination will not result in a material adverse effect.

***We may be unable to obtain security clearances necessary to perform certain Level 3 government contracts.***

Certain Level 3 legal entities and officers have security clearances required for Level 3's performance of customer contracts with various government entities. Following the acquisition, it may be necessary for us to obtain comparable security clearances. If we or our officers are unable to qualify for such security clearances, we may not be able to continue to perform such contracts.

***We cannot assure you whether, when or in what amounts we will be able to use Level 3's net operating loss carryforwards following the Level 3 acquisition.***

As of December 31, 2016, Level 3 had approximately \$9.0 billion of net operating loss carryforwards, ("NOLs"), which for U.S. federal income tax purposes can be used to offset future taxable income, subject to certain limitations under Section 382 of the Code and related Treasury regulations. Our ability to use these NOLs following the Level 3 acquisition would likely be further limited by Section 382 if Level 3 is deemed to undergo an ownership change as a result of the acquisition or CenturyLink is deemed to undergo an ownership change following the acquisition, either of which could restrict use of a material portion of the NOLs. Determining the limitations under Section 382 is technical and highly complex. Although the parties, based on their review to date, currently believe that Level 3 will undergo an ownership change as a result of the acquisition, neither company has definitively completed the analysis necessary to confirm this. Moreover, issuances or sales of our stock following the acquisition (including certain transactions outside of our control) could result in an ownership change of CenturyLink under Section 382, which may further limit its use of the NOLs. For these and other reasons, we cannot assure you that we will be able to use the NOLs after the acquisition in the amounts we project.

***Our pending acquisition of Level 3 raises other risks.***

Our pending acquisition of Level 3 and, upon completion thereof, our ownership of Level 3 raise additional risks not described above. For additional information, see (i) the definitive joint proxy statement/prospectus filed with the SEC by us on February 13, 2017 and (ii) Level 3's most recently filed annual report on Form 10-K, as updated by its subsequent quarterly reports on Form 10-Q.

## **Risks Relating to Legal and Regulatory Matters**

***We operate in a highly regulated industry and are therefore exposed to restrictions on our operations and a variety of claims relating to such regulation.***

**General.** We are subject to significant regulation by, among others, (i) the Federal Communications Commission ("FCC"), which regulates interstate communications, (ii) state utility commissions, which regulate intrastate communications, and (iii) various foreign governments and international bodies, which regulate our international operations. Generally, we must obtain and maintain certificates of authority or licenses from these bodies in most territories where we offer regulated services. We cannot assure you that we will be successful in obtaining or retaining all licenses necessary to carry out our business plan, and, even if we are, the prescribed service standards and conditions imposed on us in connection with obtaining or acquiring control of these licenses may impose on us substantial costs and limitations. We are also subject to numerous requirements and interpretations under various international, federal, state and local laws, rules and regulations, which are quite detailed and occasionally in conflict with each other. Accordingly, we cannot ensure that we are always considered to be in compliance with all these requirements at any single point in time. The agencies responsible for the enforcement of these laws, rules and regulations may initiate inquiries or actions based on customer complaints or on their own initiative. Even if we are ultimately found to have complied with applicable regulations, such actions or inquiries could create adverse publicity that negatively impacts our business.



Regulation of the telecommunications industry continues to change, and the regulatory environment varies substantially from jurisdiction to jurisdiction. A substantial portion of our local voice services revenue remains subject to FCC and state utility commission pricing regulation, which periodically exposes us to pricing or earnings disputes and could expose us to unanticipated price declines. In addition, from time to time carriers or other third parties refuse to pay for certain of our services, challenge our rights to receive certain service payments, file complaints requesting rate reductions or take other similar actions that have the potential to reduce our revenues. Our future revenues, costs, and capital investment could be adversely affected by material changes to or decisions regarding the applicability of government requirements, including, but not limited to, changes in rules governing intercarrier compensation, state and federal USF support, competition policies, pricing limitations or operational restrictions. There can be no assurance that future regulatory, judicial or legislative activities will not have a material adverse effect on our operations, or that regulators or third parties will not raise material issues with regard to our compliance or noncompliance with applicable regulations.

Changes in the composition and leadership of the FCC, state commissions and other agencies that regulate our business could have significant impacts on our revenues, expenses, competitive position and prospects. Changes in the composition and leadership of these agencies are often difficult to predict, and make future planning more difficult.

**Risks associated with recent changes in regulation.** Changes in regulation can have a material impact on our business, revenues or financial performance. Recent changes in federal regulations have substantially impacted our operations. In October 2011, the FCC adopted an order providing for a multi-year transition to a regulatory structure that reduces intercarrier compensation charges, redeploys universal service funding to newer technologies, and increases certain end-user charges. These changes, coupled with our participation in the new FCC support programs, has significantly impacted various aspects of our operations, financial results and capital expenditures, including the amount of revenues we collect from our wholesale customers and our receipt of federal support payments. We expect these impacts will continue in the future. For more information, see "Business—Regulation" in Item 1 of Part I of this annual report, and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 of Part II of this annual report.

In addition, during the last few years Congress or the FCC has initiated various other changes, including various broadband and Internet regulation initiatives including "network neutrality" regulations (as discussed further below) and actions that will restrict our ability to discontinue or reduce certain services, even if unprofitable. In 2016, the FCC initiated rulemaking regarding the regulation of business data services. This rulemaking, which remains pending, could adversely affect our operations or financial results. Many of the FCC's regulations adopted in recent years remain subject to judicial review and additional rulemakings, thus increasing the difficulty of determining the ultimate impact of these changes on us and our competitors.

Certain states have recently taken steps that could reduce the amount of their universal service support payments to incumbent local exchange companies. If these trends continue, we would suffer a reduction in our revenues from state support programs.

**Risks of higher costs.** Regulations continue to create significant operating and capital costs for us. Challenges to our tariffs by regulators or third parties or delays in obtaining certifications and regulatory approvals could cause us to incur substantial legal and administrative expenses, and, if successful, such challenges could adversely affect the rates that we are able to charge our customers.

Our business also may be impacted by legislation and regulation imposing new or greater obligations related to regulations or laws related to regulating broadband services, storing records, bolstering homeland security or cyber security, increasing disaster recovery requirements, minimizing environmental impacts, enhancing privacy, restricting data collection, protecting intellectual property rights of third parties, or addressing other issues that impact our business, including (i) the Communications Assistance for Law Enforcement Act, which requires communications carriers to ensure that their equipment, facilities, and services are able to facilitate authorized electronic surveillance, (ii) the USA Freedom Act, which requires communication companies to store records of communications of their customers, and (iii) laws that have significantly enhanced our responsibilities relating to data security in certain jurisdictions. We expect our compliance costs to increase if future laws or regulations continue to increase our obligations.

**Increased risks of fines.** We have recently paid certain regulatory fines associated with network or service outages, particularly with respect to outages impacting the availability of emergency - 911 services. Over the past couple of years, we believe that regulators have assessed substantially higher fines than in the past for these types of incidents, and it is possible this trend will continue.

**Risks of reduced flexibility.** As a diversified full service incumbent local exchange carrier in many of our key operating markets, we have traditionally been subject to significant regulation that does not apply to many of our competitors. This regulation in many instances restricts our ability to change rates, to compete and to respond rapidly to changing industry conditions. In particular, cable television companies in recent years have been able to exploit differences in regulatory oversight, which we believe has helped them to develop service offerings competitive with ours. As our business becomes increasingly competitive, regulatory disparities between us and our competitors could increasingly impede our ability to compete.

**Risks posed by other regulations.** All of our operations are also subject to a variety of environmental, safety, health and other governmental regulations. We monitor our compliance with federal, state and local regulations governing the management, discharge and disposal of hazardous and environmentally sensitive materials. Although we believe that we are in compliance with these regulations in all material respects, our management, discharge or disposal of hazardous and environmentally sensitive materials might expose us to claims or actions that could potentially have a material adverse effect on our business, financial condition and operating results. For a discussion of regulatory risks associated with our international operations, see "Risk Factors—Risks Affecting Our Business—Our international operations expose us to various regulatory, currency, tax, legal and other risks."

***Our participation in the FCC's Connect America Fund ("CAF") Phase 2 support program poses certain risks.***

Our participation in the FCC's CAF Phase 2 support program subjects us to certain financial risks. If we fail to attain certain specified infrastructure buildout requirements, the FCC could withhold future CAF support payments until these shortcomings are rectified. In addition, if we are not in compliance with FCC measures by the end of the CAF Phase 2 program, we would incur substantial penalties. To comply with the FCC's buildout requirements, we believe we will need to dedicate a substantial portion of our future capital expenditure budget to the construction of new infrastructure. The CAF-related expenditures could reduce the amount of funds we are willing or able to allocate to other initiatives or projects.

***Regulation of the Internet could limit our ability to operate our broadband business profitably and to manage our broadband facilities efficiently.***

In order to continue to provide quality broadband service at attractive prices, we believe we need the continued flexibility to respond to changing consumer demands, to manage bandwidth usage efficiently for the benefit of all customers and to invest in our networks. In 2015, the FCC adopted new regulations that regulate broadband services as a public utility under Title II of the Communications Act. The ultimate impact of the new regulations will depend on several factors, including the manner in which the new regulations are implemented and enforced and whether those regulations are altered by the newly-constituted FCC or Congress. Although it is premature for us to determine the ultimate impact of the new regulations upon our operations, we currently anticipate that implementation of the proposed rules could hamper our ability to operate our data networks efficiently, restrict our ability to implement network management practices necessary to ensure quality service, increase the cost of network extensions and upgrades, and otherwise negatively impact our current operations. Our service offerings could become subject to additional laws and regulations as they are adopted or applied to the Internet. As the significance of the Internet expands, federal, state, local or foreign governments may adopt new laws or regulations, or apply existing laws and regulations to the Internet. We cannot predict the outcome of any such changes.

***We may be liable for the material that content providers distribute over our network.***

Although we believe our liability for third party information stored on or transmitted through our networks is limited, the liability of private network operators is impacted both by changing technology and evolving legal principles that remain unsettled in many jurisdictions. As a private network provider, we could be exposed to legal claims relating to third party content stored or transmitted on our networks. Such claims could involve, among others, allegations of defamation, invasion of privacy, copyright infringement, or aiding and abetting restricted activities such as online gambling or pornography. If we decide to implement additional measures to reduce our exposure to these risks, or if we are required to defend ourselves against these kinds of claims, our operations and financial results could be negatively affected.

***Any adverse outcome in any of our pending key legal proceedings could have a material adverse impact on our financial condition and operating results, on the trading price of our securities and on our ability to access the capital markets.***

There are several material proceedings pending against us, as described in Note 16—Commitments and Contingencies to our consolidated financial statements included in Item 8 of Part II of this annual report. Results of these legal proceedings cannot be predicted with certainty. Irrespective of its merits, litigation may be both lengthy and disruptive to our operations and could cause significant expenditure and diversion of management attention. Any of the proceedings described in Note 16, as well as current

litigation not described therein or future litigation, could have a material adverse effect on our financial position or operating results. We can give you no assurances as to the impact of these matters on our operating results or financial condition.

*We are subject to franchising requirements that could impede our expansion opportunities or result in potential fines or penalties.*

We may be required to obtain from municipal authorities operating franchises to install or expand certain facilities related to our fiber transport operations, our competitive local exchange carrier operations, and our facilities-based video services. Some of these franchises may require us to pay franchise fees. Many of our franchise agreements have compliance obligations and failure to comply may result in fines or penalties. In some cases, certain franchise requirements could delay us in expanding our operations or increase the costs of providing these services.

*We are exposed to risks arising out of recent legislation affecting U.S. public companies.*

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act and the Dodd-Frank Wall Street Reform and Consumer Protection Act, and related regulations implemented thereunder, have increased our legal and financial compliance costs and made some activities more time consuming. Any failure to successfully or timely complete annual assessments of our internal controls required by Section 404 of the Sarbanes-Oxley Act could subject us to sanctions or investigation by regulatory authorities. Any such action could adversely affect our financial results or our reputation with investors, lenders or others.

*Changes in any of the above-described laws or regulations may limit our ability to plan, and could subject us to further costs or constraints.*

From time to time, the laws or regulations governing us or our customers, or the government's policy of enforcing those laws or regulations, have changed frequently and materially. The variability of these laws could hamper the ability of us and our customers to plan for the future or establish long-term strategies. Moreover, future changes in these laws or regulations could further increase our operating or compliance costs, or further restrict our operational flexibility, any of which could have a material adverse effect on our results of operations, competitive position, financial condition or prospects.

For a more thorough discussion of the regulatory issues that may affect our business, see "Business—Regulation" in Item 1 of Part I of this annual report.

### **Risks Affecting Our Liquidity and Capital Resources**

*Our high debt levels expose us to a broad range of risks.*

We continue to carry significant debt. As of December 31, 2016, the aggregate principal amount of our consolidated long-term debt, excluding unamortized discounts, net, unamortized debt issuance costs and capital lease and other obligations, was \$19.879 billion. As of the date of this annual report, \$2.715 billion aggregate principal amount of this long-term debt is scheduled to mature prior to December 31, 2019. While we currently believe we will have the financial resources to meet or refinance our obligations when they come due, we cannot fully anticipate our future performance or financial condition, the future condition of the credit markets or the economy generally.

Our significant levels of debt can adversely affect us in several other respects, including:

- limiting our ability to obtain additional financing for working capital, capital expenditures, acquisitions, refinancings or other general corporate purposes, particularly if, as discussed further in the risk factor disclosure below, (i) the ratings assigned to our debt securities by nationally recognized credit rating organizations are revised downward or (ii) we seek capital during periods of turbulent or unsettled market conditions;
- requiring us to dedicate a substantial portion of our cash flow from operations to the payment of interest and principal on our debt, thereby reducing the funds available to us for other purposes, including acquisitions, capital expenditures, strategic initiatives, dividends, stock repurchases, marketing and other potential growth initiatives;
- hindering our ability to capitalize on business opportunities and to plan for or react to changing market, industry, competitive or economic conditions;
- increasing our future borrowing costs;
- increasing the risk that third parties will be unwilling or unable to engage in hedging or other financial or commercial arrangements with us;

- making us more vulnerable to economic or industry downturns, including interest rate increases;
- placing us at a competitive disadvantage compared to less leveraged competitors;

- increasing the risk that we will need to sell securities or assets, possibly on unfavorable terms, or take other unfavorable actions to meet payment obligations; or
- increasing the risk that we may not meet the financial covenants contained in our debt agreements or timely make all required debt payments, either of which could result in the acceleration of some or all of our outstanding indebtedness.

The effects of each of these factors could be intensified if we increase our borrowings.

Any failure to make required debt payments could, among other things, adversely affect our ability to conduct operations or raise capital.

*Our debt agreements and the debt agreements of our subsidiaries allow us to incur significantly more debt, which could exacerbate the other risks described in this annual report.*

The terms of our debt instruments and the debt instruments of our subsidiaries permit us to incur additional indebtedness. Additional debt may be necessary for many reasons, including those discussed above. Incremental borrowings that impose additional financial risks could exacerbate the other risks described in this annual report.

*We expect to periodically require financing, and we cannot assure you that we will be able to obtain such financing on terms that are acceptable to us, or at all.*

We have a significant amount of indebtedness that we intend to refinance over the next several years, principally through the issuance of debt securities of CenturyLink, Inc., Qwest Corporation or both. Our ability to arrange additional financing will depend on, among other factors, our financial position, performance, and credit ratings, as well as prevailing market conditions and other factors beyond our control. Global financial markets continue to be volatile. Prevailing market conditions could be adversely affected by (i) general market conditions, such as disruptions in domestic or overseas sovereign or corporate debt markets, geo-political instabilities, contractions or limited growth in the economy or other similar adverse economic developments in the U.S. or abroad and (ii) specific conditions in the communications industry. Volatility in the global markets could limit our access to the credit markets, leading to higher borrowing costs or, in some cases, the inability to obtain financing on terms that are as favorable as those from which we previously benefited, on terms that are acceptable to us, or at all. Any such failure to obtain additional financing could jeopardize our ability to repay, refinance or reduce our debt obligations.

We may also need to obtain additional financing under a variety of other circumstances, including if:

- revenues and cash provided by operations decline;
- economic conditions weaken, competitive pressures increase or regulatory requirements change;
- we engage in additional acquisitions or undertake substantial capital projects or other initiatives that increase our cash requirements;
- we are required to contribute a material amount of cash to our pension plans;
- we are required to begin to pay other post-retirement benefits earlier than anticipated;
- our payments of federal income taxes increase faster or in greater amounts than currently anticipated; or
- we become subject to significant judgments or settlements, including in connection with one or more of the matters discussed in Note 16—Commitments and Contingencies to our consolidated financial statements included in Item 8 of Part II of this annual report.

For all the reasons mentioned above, we can give no assurance that additional financing for any of these purposes will be available on terms that are acceptable to us, or at all.

In addition, our ability to borrow funds in the future will depend in part on the satisfaction of the covenants in our credit facilities and other debt instruments. If we are unable to satisfy the covenants contained in those instruments, or are unable to generate cash sufficient to make required debt payments, the parties to whom we are indebted could accelerate the maturity of some or all of our outstanding indebtedness. Certain of our debt instruments have cross-default or cross-acceleration provisions. When present, these provisions could have a wider impact on liquidity than might otherwise arise from a default or acceleration of a single debt instrument.



As noted above, if we are unable to make required debt payments or refinance our debt, we would likely have to consider other options, such as selling assets, issuing additional securities, reducing or terminating our dividend payments, cutting costs or otherwise reducing our cash requirements, or negotiating with our lenders to restructure our applicable debt. Our current and future debt instruments may restrict, or market or business conditions may limit, our ability to do some of these things on favorable terms, or at all.

*Any downgrade in the credit ratings of us or our affiliates could limit our ability to obtain future financing, increase our borrowing costs and adversely affect the market price of our existing debt securities or otherwise impair our business, financial condition and results of operations.*

Nationally recognized credit rating organizations have issued credit ratings relating to CenturyLink, Inc.'s long-term debt and the long-term debt of several of its subsidiaries. Most of these ratings are below "investment grade", which results in higher borrowing costs than "investment grade" debt as well as reduced marketability of our debt securities. There can be no assurance that any rating assigned to any of these debt securities will remain in effect for any given period of time or that any such ratings will not be lowered, suspended or withdrawn entirely by a rating agency if, in that rating agency's judgment, circumstances so warrant.

A downgrade of any of these credit ratings could:

- adversely affect the market price of some or all of our outstanding debt or equity securities;
- limit our access to the capital markets or otherwise adversely affect the availability of other new financing on favorable terms, if at all;
- trigger the application of restrictive covenants in certain of our debt agreements or result in new or more restrictive covenants in agreements governing the terms of any future indebtedness that we may incur;
- increase our cost of borrowing; and
- impair our business, financial condition and results of operations.

*Under certain circumstances upon a change of control, we will be obligated to offer to repurchase certain of our outstanding debt securities, which could have certain adverse ramifications.*

If the credit ratings relating to certain of our currently outstanding long-term debt securities are downgraded in the manner specified thereunder in connection with a "change of control" of CenturyLink, Inc., then we will be required to offer to repurchase such debt securities. If, due to lack of cash, legal or contractual impediments, or otherwise, we fail to offer to repurchase such debt securities, such failure could constitute an event of default under such debt securities, which could in turn constitute a default under other of our agreements relating to our indebtedness outstanding at that time. Moreover, the existence of these repurchase covenants may in certain circumstances render it more difficult or discourage a sale or takeover of us, or the removal of our incumbent directors.

*Our business requires us to incur substantial capital and operating expenses, which reduce our available free cash flow.*

Our business is capital intensive, and we anticipate that our capital requirements will continue to be significant in the coming years.

We expect to invest additional capital to expand and enhance our network infrastructure as a result of several factors, including:

- our regulatory commitments, including infrastructure construction requirements arising out of our participation in the FCC's CAF Phase 2 program, which are discussed further herein;
- increased demands by customers to transmit larger amounts of data at faster speeds;
- changes in customers' service requirements;
- technological advances of our competitors; or
- the development and launch of new services.

We may be unable to expand or adapt our network infrastructure to respond to these developments in a timely manner, at a commercially reasonable cost or on terms producing satisfactory returns on our investment.

In addition to investing in expanded networks, new products or new technologies, we must from time to time invest capital to (i) replace some of our aging equipment that supports many of our legacy services that are experiencing revenue declines or (ii) convert older systems to simplify and modernize our network. While we believe that our currently planned level of capital expenditures will meet both our maintenance and core growth requirements, this may not be the case if demands on our network continue to accelerate or other circumstances underlying our expectations change. Increased spending could, among other things, adversely affect our operating margins, cash flows, results of operations and financial position.

Similarly, we continue to anticipate incurring substantial operating expenses to support our incumbent services and growth initiatives. We may be unable to sufficiently manage or reduce these costs, even if revenues in some of our lines of business are decreasing. If so, our operating margins will be adversely impacted.

*Our senior notes are unsecured and will be effectively subordinated to any secured indebtedness.*

Our currently outstanding senior notes are unsecured and are effectively subordinated to any of our existing or future secured indebtedness, to the extent of the value of the assets securing such indebtedness, including, upon consummation of the Level 3 acquisition, any newly-incurred acquisition financing secured by subsidiary guarantees or pledges of stock of selected subsidiaries. In the event of a bankruptcy or similar proceeding, the stock that serve as collateral for any secured indebtedness would generally be available to satisfy our obligations under such secured indebtedness, and would not be expected to be available to satisfy other claims.

*As a holding company, we rely on payments from our operating companies to meet our obligations.*

As a holding company, substantially all of our income and operating cash flow is dependent upon the earnings of our subsidiaries and their distribution of those earnings to us in the form of dividends, loans or other payments. As a result, we rely upon our subsidiaries to generate the funds necessary to meet our obligations, including the payment of amounts owed under our long-term debt. Our subsidiaries are separate and distinct legal entities and have no obligation to pay any amounts owed by us or, subject to limited exceptions for tax-sharing or cash management purposes, to make any funds available to us to repay our obligations, whether by dividends, loans or other payments. State law applicable to each of our subsidiaries restricts the amount of dividends that they may pay. Restrictions that have been or may be imposed by state regulators (either in connection with obtaining necessary approvals for our acquisitions or in connection with our regulated operations), and restrictions imposed by credit instruments or other agreements applicable to certain of our subsidiaries may limit the amount of funds that our subsidiaries are permitted to transfer to us, including the amount of dividends that may be paid to us. Moreover, our rights to receive assets of any subsidiary upon its liquidation or reorganization will be effectively subordinated to the claims of creditors of that subsidiary, including trade creditors. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources" included elsewhere in this annual report for further discussion of these matters.

*We cannot assure you that we will continue paying dividends at the current rates, or at all.*

For the reasons noted below, we cannot assure you that we will continue periodic dividends on our capital stock at the current rates, or at all.

As noted in the immediately preceding risk factor, because we are a holding company with no material assets other than the stock of our subsidiaries, our ability to pay dividends will depend on the earnings and cash flow of our subsidiaries and their ability to furnish funds to us in the form of dividends, loans or other payments.

Any quarterly dividends on our common stock and our outstanding shares of preferred stock will be paid from funds legally available for such purpose when, as and if declared by our Board of Directors. Decisions on whether, when and in which amounts to continue making any future dividend distributions will remain at all times entirely at the discretion of our Board of Directors, which reserves the right to change or terminate our dividend practices at any time and for any reason without prior notice, including without limitation any of the following:

- our supply of cash or other liquid assets is anticipated to remain under pressure due to declining cash flows from operating activities, increased payments of post-retirement benefits and our projected payment of higher cash taxes prior to the pending Level 3 acquisition and might be further negatively impacted by any of the potential adverse events or developments described in this annual report, including (i) changes in competition, regulation, federal and state support, technology, taxes, capital markets, operating costs or litigation costs, or (ii) the impact of any liquidity shortfalls caused by the below-described restrictions on the ability of our subsidiaries to lawfully transfer cash to us;



- our cash requirements or plans might change for a wide variety of reasons, including changes in our capital allocation plans (including a desire to retain or accumulate cash), capital spending plans, stock purchase plans, acquisition strategies, strategic initiatives, debt payment plans (including a desire to maintain or improve credit ratings on our debt securities), pension funding payments, or financial position;
- our ability to service and refinance our current and future indebtedness and our ability to borrow or raise additional capital to satisfy our capital needs;
- the amount of dividends that we may distribute to our shareholders is subject to restrictions under Louisiana law and restrictions imposed by our existing or future credit facilities, debt securities, outstanding preferred stock securities, leases and other agreements, including restricted payment and leverage covenants; and
- the amount of cash that our subsidiaries may make available to us, whether by dividends, loans or other payments, may be subject to the legal, regulatory and contractual restrictions described in the immediately preceding risk factor.

Based on its evaluation of these and other relevant factors, our Board of Directors may, in its sole discretion, decide not to declare a dividend on our common stock or our outstanding shares of preferred stock for any period for any reason without prior notice, regardless of whether we have funds legally available for such purposes. Holders of our equity securities should be aware that they have no contractual or other legal right to receive dividends.

Similarly, holders of our common stock should be aware that repurchases of our common stock under any repurchase plan then in effect are completely discretionary, and may be suspended or discontinued at any time for any reason regardless of our financial position.

*Our current dividend practices could limit our ability to deploy cash for other beneficial purposes.*

The current practice of our Board of Directors to pay common share dividends reflects a current intention to distribute to our shareholders a substantial portion of our cash flow. As a result, we may not retain a sufficient amount of cash to apply to other transactions that could be beneficial to our shareholders or debtholders, including stock buybacks, debt prepayments or capital expenditures that strengthen our business. In addition, our ability to pursue any material expansion of our business through acquisitions or increased capital spending may depend more than it otherwise would on our ability to obtain third party financing.

*We cannot assure you whether, when or in what amounts we will be able to use our net operating loss carryforwards, or when they will be depleted.*

At December 31, 2016, we had state NOL carryforwards of approximately \$11.9 billion. A significant portion of the state NOL carryforwards are generated in states where separate company income tax returns are filed and our subsidiaries that generated the losses may not have the ability to generate income in sufficient amounts to realize these losses. In addition, certain of these state NOL carryforwards will be limited by state laws related to ownership changes. As a result, we expect to utilize only a small portion of the state NOL carryforwards, and consequently have determined that as of December 31, 2016, these state NOL carryforwards, net of federal benefit, had a net tax benefit (after valuation allowance) of \$131 million.

*Increases in costs for pension and healthcare benefits for our active and retired employees may reduce our profitability and increase our funding commitments.*

With approximately 36,000 active employees, approximately 72,000 active and retired employees and surviving spouses eligible for post-retirement benefits, approximately 68,000 pension retirees and approximately 14,000 former employees with vested pension benefits participating in our benefit plans as of December 31, 2016, the costs of pension and healthcare benefits for our active and retired employees have a significant impact on our profitability. Our costs of maintaining our pension and healthcare plans, and the future funding requirements for these plans, are affected by several factors, most of which are outside our control, including:

- decreases in investment returns on funds held by our pension and other benefit plan trusts;
- changes in prevailing interest rates and discount rates or other factors used to calculate the funding status of our pension and other post-retirement plans;
- increases in healthcare costs generally or claims submitted under our healthcare plans specifically;
- increasing longevity of our employees and retirees;
- the impact of the continuing implementation, modification or potential repeal of current federal healthcare legislation and

regulations promulgated thereunder;

- increases in the number of retirees who elect to receive lump sum benefit payments;
- increases in insurance premiums we are required to pay to the Pension Benefit Guaranty Corporation, an independent agency of the United States government that must cover its own underfunded status by collecting premiums from an ever shrinking population of pension plans that are qualified under the U.S. tax code;
- changes in plan benefits; and
- changes in funding laws or regulations.

Increased costs under these plans could reduce our profitability and increase our funding commitments to our pension plans. Any future material cash contributions could have a negative impact on our liquidity by reducing our cash flows available for other purposes. Similarly, depletion of assets placed in trust by us to fund these benefits, such as those discussed elsewhere herein, will similarly reduce our liquidity by reducing our cash flows available for other purposes.

As of December 31, 2016, our pension plans and our other post-retirement benefit plans were substantially underfunded from an accounting standpoint. See Note 9—Employee Benefits to our consolidated financial statements included in Item 8 of this annual report. For more information on our obligations under our defined benefit pension plans and other post-retirement benefit plans, please see “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Pension and Post-retirement Benefit Obligations” included in Item 7 of this annual report.

For additional information concerning our liquidity and capital resources, see Item 7 of this annual report. For a discussion of certain currency and liquidity risks associated with our international operations, see “Risk Factors—Risks Affecting Our Business—Our international operations expose us to various regulatory, currency, tax, legal and other risks.”

#### **Other Risks**

*We face risks from natural disasters, which can disrupt our operations and cause us to incur substantial additional capital and operating costs.*

A substantial number of our facilities are located in Florida, Alabama, Louisiana, Texas, North Carolina, South Carolina and other coastal states, which subjects them to the risks associated with severe tropical storms, hurricanes and tornadoes, including downed telephone lines, flooded facilities, power outages, fuel shortages, damaged or destroyed property and equipment, and work interruptions. Although we maintain property and casualty insurance on our property (excluding our above ground outside plant) and may, under certain circumstances, be able to seek recovery of some additional costs through increased rates, only a portion of our additional costs directly related to such natural disasters have historically been recoverable. We cannot predict whether we will continue to be able to obtain insurance for catastrophic hazard-related damages or, if obtainable and carried, whether this insurance will be adequate to cover our losses. In addition, we expect any insurance of this nature to be subject to substantial deductibles, retentions and coverage exclusions, and the premiums to be based on our loss experience. For all these reasons, any future hazard-related costs and work interruptions could adversely affect our operations and our financial condition.

*If conditions or assumptions differ from the judgments, assumptions or estimates used in our critical accounting policies, our consolidated financial statements and related disclosures could be materially affected.*

The preparation of financial statements and related disclosures in conformity with U.S. generally accepted accounting principles requires management to make judgments, assumptions and estimates that affect the amounts reported in our consolidated financial statements and accompanying notes. Our critical accounting policies, which are described in “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates” in Item 7 of Part II of this annual report, describe those significant accounting policies and methods used in the preparation of our consolidated financial statements that are considered “critical” because they require judgments, assumptions and estimates that materially impact our consolidated financial statements and related disclosures. As a result, if future events or assumptions differ significantly from the judgments, assumptions and estimates in our critical accounting policies, these events or assumptions could have a material impact on our consolidated financial statements and related disclosures.

While frequently presented with numeric specificity, the guidance and other forward-looking statements that we disseminate from time to time is based on numerous variables and assumptions (including, but not limited to, those related to industry performance and competition and general business, economic, market and financial conditions and additional matters specific to our business, as applicable) that are inherently subjective and uncertain and are largely beyond our control. As a result, actual results may differ

materially from our guidance or other forward-looking statements. For additional information, see "Special Note Regarding Forward-Looking Statements and Related Matters" in Item 1 of Part I of this annual report.

***Lapses in disclosure controls and procedures or internal control over financial reporting could materially and adversely affect our operations, profitability or reputation.***

There can be no assurance that our disclosure controls and procedures will be effective in the future or that we will not experience a material weakness or significant deficiency in internal control over financial reporting. Any such lapses or deficiencies may materially and adversely affect our business, operating results or financial condition, restrict our ability to access the capital markets, require us to expend significant resources to correct the lapses or deficiencies, expose us to regulatory or legal proceedings, including litigation brought by private individuals, subject us to fines, penalties or judgments, harm our reputation, or otherwise cause a decline in investor confidence and our stock price.

***If our goodwill or other intangible assets become impaired, we may be required to record a significant charge to earnings and reduce our stockholders' equity.***

As of December 31, 2016, approximately 51% of our total consolidated assets reflected on the consolidated balance sheet included in this annual report consisted of goodwill (excluding goodwill assigned to the colocation business and included in assets held for sale), customer relationships and other intangible assets. Under U.S. generally accepted accounting principles, most of these intangible assets must be tested for impairment on an annual basis or more frequently whenever events or circumstances indicate that their carrying value may not be recoverable. From time to time (most recently for the third quarter of 2013), we have recorded large non-cash charges to earnings in connection with required reductions of the value of our intangible assets. If our intangible assets are determined to be impaired in the future, we may be required to record additional significant, non-cash charges to earnings during the period in which the impairment is determined to have occurred. Any such charges could, in turn, have a material adverse effect on our results of operation, financial condition or ability to comply with financial covenants in our debt instruments.

***Tax audits or changes in tax laws could adversely affect us.***

Like all large businesses, we are subject to frequent and regular audits by the Internal Revenue Service as well as state and local tax authorities. These audits could subject us to tax liabilities if adverse positions are taken by these tax authorities.

We believe that we have adequately provided for tax contingencies. However, our tax audits and examinations may result in tax liabilities that differ materially from those that we have recognized in our consolidated financial statements. Because the ultimate outcomes of all of these matters are uncertain, we can give no assurance as to whether an adverse result from one or more of them will have a material effect on our financial results.

Legislators and regulators at all levels of government may from time to time change existing tax laws or regulations or enact new laws or regulations that could negatively impact our operating results or financial condition.

***Our agreements and organizational documents and applicable law could limit another party's ability to acquire us.***

A number of provisions in our agreements and organizational documents and various provisions of applicable law may delay, defer or prevent a future takeover of CenturyLink unless the takeover is approved by our Board of Directors. These provisions could deprive our shareholders of any related takeover premium. For additional information, please see our Registration Statement on Form 8-A/A filed with the SEC on March 2, 2015.

#### **ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

Our property, plant and equipment consists principally of telephone lines, cable, central office equipment, land and buildings related to our operations. Our gross property, plant and equipment consisted of the following components:

	As of December 31,	
	2016	2015
Land	2%	2%
Fiber, conduit and other outside plant <sup>(1)</sup>	43%	42%
Central office and other network electronics <sup>(2)</sup>	35%	36%
Support assets <sup>(3)</sup>	17%	18%
Construction in progress <sup>(4)</sup>	3%	2%
Gross property, plant and equipment	100%	100%

- (1) Fiber, conduit and other outside plant consists of fiber and metallic cable, conduit, poles and other supporting structures.
- (2) Central office and other network electronics consists of circuit and packet switches, routers, transmission electronics and electronics providing service to customers.
- (3) Support assets consist of buildings, data centers, computers and other administrative and support equipment.
- (4) Construction in progress includes inventory held for construction and property of the aforementioned categories that has not been placed in service as it is still under construction.

We own substantially all of our telecommunications equipment required for our business. However, we lease from third parties certain facilities, plant, equipment and software under various capital and operating lease arrangements when the leasing arrangements are more favorable to us than purchasing the assets. We also own and lease administrative offices in major metropolitan locations both in the United States and internationally. Substantially all of our network electronics equipment is located in buildings or on land that we own or lease within our local service area. Outside of our local service area, our assets are generally located on real property pursuant to an agreement with the property owner or another person with rights to the property. It is possible that we may lose our rights under one or more of these agreements, due to their termination or expiration or in connection with legal challenges to our rights under such agreements.

Our net property, plant and equipment was approximately \$17.0 billion and \$18.1 billion at December 31, 2016 and 2015, respectively. Some of our property, plant and equipment is pledged to secure the long-term debt of subsidiaries. For additional information, see Note 7—Property, Plant and Equipment to our consolidated financial statements in Item 8 of Part II of this annual report.

**ITEM 3. LEGAL PROCEEDINGS**

The information contained under the subheadings "Pending Matters" and "Other Proceedings and Disputes" in Note 16—Commitments and Contingencies to our consolidated financial statements included in Item 8 of Part II of this annual report is incorporated herein by reference.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is listed on the New York Stock Exchange ("NYSE") and the Berlin Stock Exchange and is traded under the symbol CTL and CYT, respectively. The following table sets forth the high and low reported sales prices on the NYSE along with the quarterly dividends, for each of the quarters indicated.

	Sales Price		Cash Dividend per Common Share
	High	Low	
<b>2016</b>			
First quarter	\$ 32.49	21.94	0.540
Second quarter	32.94	26.35	0.540
Third quarter	31.56	26.51	0.540
Fourth quarter	33.45	22.86	0.540
<b>2015</b>			
First quarter	\$ 40.59	34.04	0.540
Second quarter	37.00	29.28	0.540
Third quarter	31.13	24.29	0.540
Fourth quarter	29.37	24.11	0.540

Dividends on common stock during 2016 and 2015 were paid each quarter. On February 21, 2017, our Board of Directors declared a common stock dividend of \$0.54 per share.

As described in greater detail in "Risk Factors" in Item 1A of Part I of this annual report, the declaration and payment of dividends is at the discretion of our Board of Directors, and will depend upon our financial results, cash requirements, future prospects and other factors deemed relevant by our Board of Directors.

At February 16, 2017, there were approximately 122,000 stockholders of record, although there were significantly more beneficial holders of our common stock. At February 16, 2017, the closing stock price of our common stock was \$24.28.

#### Issuer Purchases of Equity Securities

The following table contains information about shares of our previously-issued common stock that we withheld from employees upon vesting of their stock-based awards during the fourth quarter of 2016 to satisfy the related minimum tax withholding obligations:

Period	Total Number of Shares Withheld for Taxes	Average Price Paid Per Share
October 2016	5,123	\$ 27.48
November 2016	24,858	26.94
December 2016	834	23.93
Total	30,815	

**ITEM 6. SELECTED FINANCIAL DATA**

The following tables of selected consolidated financial data should be read in conjunction with, and are qualified by reference to, our consolidated financial statements and notes thereto in Item 8 of Part II and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 of Part II of this annual report.

The tables of selected financial data shown below are derived from our audited consolidated financial statements. These historical results are not necessarily indicative of results that you can expect for any future period.

Selected financial information from our consolidated statements of operations is as follows:

	Years Ended December 31, <sup>(1)</sup>				
	2016 <sup>(2)(3)</sup>	2015 <sup>(2)</sup>	2014 <sup>(4)</sup>	2013 <sup>(5)</sup>	2012
	(Dollars in millions, except per share amounts and shares in thousands)				
Operating revenues	\$ 17,470	17,900	18,031	18,095	18,376
Operating expenses	15,139	15,295	15,621	16,642	15,663
Operating income	\$ 2,331	2,605	2,410	1,453	2,713
Income before income tax expense	1,020	1,316	1,110	224	1,250
Net income (loss)	626	878	772	(239)	777
Basic earnings (loss) per common share	1.16	1.58	1.36	(0.40)	1.25
Diluted earnings (loss) per common share	1.16	1.58	1.36	(0.40)	1.25
Dividends declared per common share	2.16	2.16	2.16	2.16	2.90
Weighted average basic common shares outstanding	539,549	554,278	568,435	600,892	620,205
Weighted average diluted common shares outstanding	540,679	555,093	569,739	600,892	622,285

- (1) See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Results of Operations" in Item 7 of Part II of this annual report for a discussion of unusual items affecting the results for the years ended December 31, 2016, 2015 and 2014.
- (2) During 2016 and 2015, we recognized an incremental \$201 million and \$215 million, respectively, of revenue associated with the Federal Communications Commission ("FCC") Connect America Fund Phase 2 support program as compared to the interstate USF program. For additional information, see Note 1—Basis of Presentation and Summary of Significant Accounting Policies to our consolidated financial statements in Item 8 of Part II of this annual report.
- (3) During 2016, we recognized \$189 million of severance expenses and other one-time termination benefits associated with our workforce reductions and \$52 million of expenses related to our pending acquisition of Level 3.
- (4) During 2014, we recognized a \$60 million tax benefit associated with a deduction for the tax basis for worthless stock in a wholly-owned foreign subsidiary and a \$63 million pension settlement charge.
- (5) During 2013, we recorded a non-cash, non-tax-deductible goodwill impairment charge of \$1.092 billion for goodwill attributed to one of our previous operating segments and a litigation settlement charge of \$235 million.

Selected financial information from our consolidated balance sheets is as follows:

	As of December 31,				
	2016	2015	2014	2013	2012
	(Dollars in millions)				
Net property, plant and equipment <sup>(1)</sup>	\$ 17,039	18,069	18,433	18,646	18,909
Goodwill <sup>(1)(2)</sup>	19,650	20,742	20,755	20,674	21,627
Total assets <sup>(3)</sup>	47,017	47,604	49,103	50,471	52,901
Total long-term debt <sup>(3)(4)</sup>	19,993	20,225	20,503	20,809	20,481
Total stockholders' equity <sup>(2)</sup>	13,399	14,060	15,023	17,191	19,289

- (1) During 2016, as a result of the pending sale of our colocation business and data centers, we reclassified \$1.071 billion in net property, plant and equipment and \$1.141 billion of goodwill to assets held for sale which is included in other current assets on our consolidated balance sheet. See Note 3—Pending Sale of Colocation Business and Data Centers to our consolidated financial statements in Item 8 of Part II of this annual report, for additional information.
- (2) During 2013, we recorded a non-cash, non-tax-deductible goodwill impairment charge of \$1.092 billion for goodwill attributed to one of our previous operating segments.
- (3) In 2015, we adopted both ASU 2015-03 "Simplifying the Presentation of Debt Issuance Costs" and ASU 2015-17 "Balance Sheet Classification of Deferred Taxes" by retrospectively applying the requirements of the ASUs to our previously issued consolidated financial statements. The adoption of both ASU 2015-03 and ASU 2015-17 reduced total assets by \$1.044 billion, \$1.316 billion and \$1.039 billion in each year for the three years ended December 31, 2014, respectively, and ASU 2015-03 reduced total long-term debt by \$168 million, \$157 million and \$124 million in each year for the three years ended December 31, 2014, respectively.
- (4) Total long-term debt is the sum of current maturities of long-term debt, capital lease obligations of \$305 million (associated with the pending sale of colocation business and data centers) included in current liabilities associated with assets held for sale and long-term debt on our consolidated balance sheets. For additional information on our total long-term debt, see Note 5—Long-Term Debt and Credit Facilities to our consolidated financial statements in Item 8 of Part II of this annual report. For total contractual obligations, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Future Contractual Obligations" in Item 7 of Part II of this annual report.

Selected financial information from our consolidated statements of cash flows is as follows:

	Years Ended December 31,				
	2016	2015	2014	2013	2012
	(Dollars in millions)				
Net cash provided by operating activities \$	4,608	5,152	5,188	5,559	6,065
Net cash used in investing activities	(2,994)	(2,853)	(3,077)	(3,148)	(2,690)
Net cash used in financing activities	(1,518)	(2,301)	(2,151)	(2,454)	(3,295)
Payments for property, plant and equipment and capitalized software	(2,981)	(2,872)	(3,047)	(3,048)	(2,919)

The following table presents certain of our selected operational metrics:

	As of December 31,				
	2016	2015	2014	2013	2012
	(in thousands except for data centers, which are actuals)				
<b>Operational metrics:</b>					
Total access lines <sup>(1)</sup>	11,090	11,748	12,394	13,002	13,751
Total broadband subscribers <sup>(1)</sup>	5,945	6,048	6,082	5,991	5,851
Prism TV subscribers	325	285	242	175	106
Total data centers <sup>(2)</sup>	58	59	58	55	54

(1) Access lines are lines reaching from the customers' premises to a connection with the public network and broadband subscribers are customers that purchase broadband connection service through their existing telephone lines, stand-alone telephone lines, or fiber-optic cables. Our methodology for counting our access lines and broadband subscribers includes only those lines that we use to provide services to external customers and excludes lines used solely by us and our affiliates. It also excludes unbundled loops and includes stand-alone broadband subscribers. We count lines when we install the service.

(2) We define a data center as any facility where we market, sell and deliver either colocation services, multi-tenant managed services, or both. Our data centers are located in North America, Europe and Asia.

## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*All references to "Notes" in this Item 7 of Part II refer to the Notes to Consolidated Financial Statements included in Item 8 of Part II of this annual report. Certain statements in this annual report constitute forward-looking statements. See "Special Note Regarding Forward-Looking Statements and Related Matters" in Item 1 of Part I of this annual report for factors relating to these statements and "Risk Factors" in Item 1A of Part I of this annual report for a discussion of certain risk factors applicable to our business, financial condition, results of operations, liquidity or prospects.*

### Overview

We are an integrated communications company engaged primarily in providing an array of services to our residential and business customers. Our communications services include local and long-distance voice, broadband, Multi-Protocol Label Switching ("MPLS"), private line (including special access), Ethernet, colocation, hosting (including cloud hosting and managed hosting), data integration, video, network, public access, Voice over Internet Protocol ("VoIP"), information technology and other ancillary services. We strive to maintain our customer relationships by, among other things, bundling our service offerings to provide our customers with a complete offering of integrated communications services.

At December 31, 2016, we operated approximately 11.1 million access lines in 37 states and served approximately 5.9 million broadband subscribers and 325 thousand Prism TV subscribers. We also operated 58 data centers throughout North America, Europe and Asia. Our methodology for counting access lines, broadband subscribers and data centers, which is described further in the operational metrics table below under "Results of Operations", and our methodology for counting Prism TV subscribers may not be comparable to those of other companies.

### Pending Acquisition of Level 3

On October 31, 2016, we entered into a definitive merger agreement under which we propose to acquire Level 3 Communications, Inc. ("Level 3") in a cash and stock transaction. Under the terms of the agreement, Level 3 shareholders will receive \$26.50 per share in cash and 1.4286 of CenturyLink shares for each share of Level 3 common stock they own at closing. CenturyLink shareholders are expected to own approximately 51% and Level 3 shareholders are expected to own approximately 49% of the combined company at closing. On December 31, 2016, Level 3 had outstanding \$10.9 billion of long-term debt.

Completion of the transaction is subject to the receipt of regulatory approvals, including the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act, as well as approvals from the Federal Communications Commission (the "FCC") and certain state regulatory authorities. The transaction is also subject to the approval of CenturyLink and Level 3 shareholders at meetings scheduled to be held on March 16, 2017, as well as other customary closing conditions. Subject to these conditions, we anticipate closing this transaction by the end of the third quarter 2017. If the merger agreement is terminated under certain circumstances, we may be obligated to pay Level 3 a termination fee of \$472 million, or Level 3 may be obligated to pay CenturyLink a termination fee of \$738 million.

As of December 31, 2016, we had recognized \$52 million of expenses associated with our activities related to the pending Level 3 acquisition. We have not recognized certain other expenses that are contingent on completion of the acquisition. These expenses include financial advisory fees and compensation expense comprised of retention bonuses, severance and stock-based compensation for stock-based awards that will vest in connection with the acquisition. Most of these contingent expenses will be recognized in our consolidated financial statements in the period in which the acquisition occurs, with the remainder recognized thereafter. The final amount of compensation expense to be recognized is partially dependent upon personnel decisions that will be made as part of integration planning. These amounts may be material.

Upon completion of the acquisition, Level 3's assets and liabilities will be revalued and recorded at fair value. The assignment of fair value will require a significant amount of judgment. The use of fair value measures will affect the comparability of our post-acquisition financial information and may make it more difficult to predict earnings in future periods. For example, Level 3 has certain deferred costs and deferred revenues on its balance sheet associated with capacity leases. Based on the accounting guidance for business combinations, these existing deferred costs and deferred revenues are expected to be assigned little or no value in the purchase price allocation process and will thus be eliminated.

For unaudited pro forma condensed combined financial information relating to the acquisition, see the definitive joint proxy statement/prospectus filed with the SEC by us on February 13, 2017. This pro forma financial information is based upon preliminary

purchase price allocations and various assumptions and estimates, all of which we urge you to carefully consider in connection with your review of such information.

### Pending Sale of Colocation Business and Data Centers

On November 3, 2016, we entered into a definitive stock purchase agreement to sell our data centers and colocation business to a consortium led by BC Partners, Inc. and Medina Capital ("the Purchaser") in exchange for cash and a minority stake in the consortium's newly-formed global secure infrastructure company. During 2016, as a result of the pending sale, the assets to be sold to the Purchaser have been reclassified as assets held for sale in other current assets on our consolidated balance sheet. Additionally, the liabilities to be assumed by the Purchaser have been reclassified and presented as current liabilities associated with assets held for sale on our consolidated balance sheet. As part of the transaction, the Purchaser will assume our capital lease obligations, which amounted to \$305 million as of December 31, 2016, related to the properties that we will sell. The sale is subject to regulatory approvals, including a review by the Committee of Foreign Investments in the United States, as well as other customary closing conditions.

Upon being completed, this transaction will result in the Purchaser acquiring 57 data centers. This business generated revenues of \$622 million, \$626 million and \$643 million (excluding revenue with affiliates) for the years ended December 31, 2016, 2015 and 2014, respectively (a small portion of which will be retained by us). Based on certain estimates and assumptions regarding the closing date and various tax matters, we currently project that the net cash proceeds from the divestiture will be approximately \$1.5 billion to \$1.7 billion. We plan to use a portion of these net cash proceeds to partly fund our acquisition of Level 3.

The following tables present additional metrics related to our data centers:

	As of December 31,		Increase / (Decrease)	% Change
	2016	2015		
Hosting data center metrics:				
Number of data centers <sup>(1)</sup>	58	59	(1)	(2)%
Sellable square feet, million sq ft	1.54	1.58	(0.04)	(3)%
Billed square feet, million sq ft	1.04	0.99	0.05	5 %
Utilization	67%	63%	4%	6 %
<hr/>				
	As of December 31,		Increase / (Decrease)	% Change
	2015	2014		
Hosting data center metrics:				
Number of data centers <sup>(1)</sup>	59	58	1	2%
Sellable square feet, million sq ft	1.58	1.46	0.12	8%
Billed square feet, million sq ft	0.99	0.92	0.07	8%
Utilization	63%	63%	—%	—%

(1) We define a data center as any facility where we market, sell and deliver either colocation services, multi-tenant managed services, or both. Our data centers are located in North America, Europe and Asia.

See Note 3—Pending Sale of Colocation Business and Data Centers to our consolidated financial statements in Item 8 of Part II of this annual report for additional information on the pending sale.

We are organized into operating segments based on customer type, business and consumer. These operating segments are our two reportable segments in our consolidated financial statements:

- **Business Segment.** Consists generally of providing strategic, legacy and data integration products and services to small, medium and enterprise business, wholesale and governmental customers, including other communication providers. Our strategic products and services offered to these customers include our MPLS, Ethernet, colocation, hosting (including cloud hosting and managed hosting), broadband, VoIP, information technology and other ancillary services. Our legacy services offered to these customers primarily include local and long-distance voice, including the sale of unbundled network elements ("UNEs"), private line (including special access), switched access and other ancillary services. Our data integration offerings include the sale of telecommunications equipment located on customers' premises and related products and professional services, all of which are described further below under the heading "Operating Revenues"; and



- *Consumer Segment.* Consists generally of providing strategic and legacy products and services to residential customers. Our strategic products and services offered to these customers include our broadband, video (including our Prism TV services) and other ancillary services. Our legacy services offered to these customers include local and long-distance voice and other ancillary services.

## Results of Operations

The following table summarizes the results of our consolidated operations for the years ended December 31, 2016, 2015 and 2014:

	Years Ended December 31,		
	2016 <sup>(1)(2)</sup>	2015 <sup>(1)</sup>	2014 <sup>(3)</sup>
	(Dollars in millions except per share amounts)		
Operating revenues	\$ 17,470	17,900	18,031
Operating expenses	15,139	15,295	15,621
Operating income	2,331	2,605	2,410
Other expense, net	1,311	1,289	1,300
Income tax expense	394	438	338
Net income	\$ 626	878	772
Basic earnings per common share	\$ 1.16	1.58	1.36
Diluted earnings per common share	\$ 1.16	1.58	1.36

(1) During 2016 and 2015, we recognized an incremental \$201 million and \$215 million, respectively, of revenue associated with the FCC's Connect America Fund Phase 2 support program as compared to the interstate USF program. For additional information, see Note 1—Basis of Presentation and Summary of Significant Accounting Policies to our consolidated financial statements in Item 8 of Part II of this annual report.

(2) During 2016, we recognized \$189 million of severance expenses and other one-time termination benefits associated with our workforce reductions and \$52 million of expenses related to our pending acquisition of Level 3

(3) During 2014, we recognized a \$60 million tax benefit associated with a deduction for the tax basis for worthless stock in a wholly-owned foreign subsidiary and a \$63 million pension settlement charge.

The following table summarizes our access lines, broadband subscribers, Prism TV subscribers, data centers and number of employees:

	As of December 31,		
	2016	2015	2014
	(in thousands except for data centers, which are actuals)		
Operational metrics:			
Total access lines <sup>(1)</sup>	11,090	11,748	12,394
Total broadband subscribers <sup>(1)</sup>	5,945	6,048	6,082
Total Prism TV subscribers	325	285	242
Total data centers <sup>(2)</sup>	58	59	58
Total employees	40	43	45

(1) Access lines are lines reaching from the customers' premises to a connection with the public network and broadband subscribers are customers that purchase broadband connection service through their existing telephone lines, stand-alone telephone lines, or fiber-optic cables. Our methodology for counting our access lines and broadband subscribers includes only those lines that we use to provide services to external customers and excludes lines used solely by us and our affiliates. It also excludes unbundled loops and includes stand-alone broadband subscribers. We count lines when we install the service.

(2) We define a data center as any facility where we market, sell and deliver either colocation services, multi-tenant managed services, or both. Our data centers

are located in North America, Europe and Asia.

During the last decade, we have experienced revenue declines primarily due to declines in access lines, private line customers, switched access rates and minutes of use. To mitigate these revenue declines, we remain focused on efforts to, among other things:

- promote long-term relationships with our customers through bundling of integrated services;
- provide a wide array of diverse services, including enhanced or additional services that may become available in the future due to, among other things, advances in technology or improvements in our infrastructure;
- provide our broadband and premium services to a higher percentage of our customers;
- pursue acquisitions of additional assets if available at attractive prices;
- increase prices on our products and services if and when practicable;
- increase the capacity, speed and usage of our networks; and
- market our products and services to new customers.

### Operating Revenues

From time to time, we change the categorization of our products and services, and we may make similar changes in the future. During the second quarter of 2016, we determined that because of declines due to customer migration to other strategic products and services, certain of our business low-bandwidth data services, specifically our private line (including special access) services in our business segment, are more closely aligned with our legacy services than with our strategic services. As described in greater detail in Note 14—Segment Information in our Notes, these operating revenues are now reflected as legacy services.

We currently categorize our products, services and revenues among the following four categories:

- *Strategic services*, which include primarily broadband, MPLS, Ethernet, colocation, hosting (including cloud hosting and managed hosting), video (including our facilities-based video services, which we offer in 16 markets), VoIP, information technology and other ancillary services;
- *Legacy services*, which include primarily local and long-distance voice services, including the sale of UNEs, private line (including special access), Integrated Services Digital Network ("ISDN") (which use regular telephone lines to support voice, video and data applications), switched access and other ancillary services;
- *Data integration*, which includes the sale of telecommunications equipment located on customers' premises and related products and professional services, such as network management, installation and maintenance of data equipment and the building of proprietary fiber-optic broadband networks for our governmental and business customers; and
- *Other operating revenues*, which consists primarily of Connect America Fund ("CAF") support payments, Universal Service Fund ("USF") support payments and USF surcharges. We receive federal support payments from both Phase 1 and Phase 2 of the CAF program, and support payments from both federal and state USF programs. These support payments are government subsidies designed to reimburse us for various costs related to certain telecommunications services, including the costs of deploying, maintaining and operating voice and broadband infrastructure in high-cost rural areas where we are not able to fully recover our costs from our customers. We also collect USF surcharges based on specific items we list on our customers' invoices to fund the FCC's universal service programs. We also generate other operating revenues from the leasing and subleasing of space in our office buildings, warehouses and other properties. Because we centrally manage the activities that generate these other operating revenues, these revenues are not included in our segment revenues.

The following tables summarize our consolidated operating revenues recorded under our four revenue categories:

	Years Ended December 31,		Increase / (Decrease)	% Change
	2016	2015		
	(Dollars in millions)			
Strategic services	\$ 8,050	7,753	297	4 %
Legacy services	7,672	8,338	(666)	(8)%
Data integration	533	577	(44)	(8)%
Other	1,215	1,232	(17)	(1)%
Total operating revenues	\$ 17,470	17,900	(430)	(2)%

	Years Ended December 31,		Increase / (Decrease)	% Change
	2015	2014		
	(Dollars in millions)			
Strategic services	\$ 7,753	7,303	450	6 %
Legacy services	8,338	9,033	(695)	(8)%
Data integration	577	692	(115)	(17)%
Other	1,232	1,003	229	23 %
Total operating revenues	\$ 17,900	18,031	(131)	(1)%

Our total operating revenues decreased by \$430 million, or 2%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015 and decreased by \$131 million, or 1%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The decline in operating revenues for both periods was primarily due to lower legacy services revenues, which decreased by \$666 million, or 8%, and \$695 million, or 8%, for the respective periods.

The decline in legacy services revenues for both periods reflects the continuing loss of access lines, loss of long-distance revenues primarily due to the displacement of traditional wireline telephone services by other competitive products and services, including data and wireless communication services, and reductions in the volume of our private line (including special access) services. At December 31, 2016, we had approximately 11.1 million access lines, or approximately 5.6% less than the number of access lines we operated at December 31, 2015. At December 31, 2015, we had approximately 11.7 million access lines, or approximately 5.2% less than the number of access lines we operated at December 31, 2014. We estimate that the rate of our access lines losses will be between 4% and 6% over the full year of 2017.

For 2016, the growth in our strategic services revenues was primarily due to increased demand for our Ethernet, MPLS, facilities-based video and VoIP services and from rate increases on various services, which were partially offset by declines in our hosting services and losses of broadband customers. For 2015, the growth in our strategic services revenues was primarily due to increased demand for our Ethernet, MPLS, facilities-based video and IT Services and from rate increases on various services, which were partially offset by declines in our colocation and hosting services.

Data integration revenues, which are typically more volatile than our other sources of revenues, decreased by \$44 million, or 8%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. The decline in data integration revenues was primarily due to declines in governmental and business sales and professional and maintenance services. Data integration revenues decreased by \$115 million, or 17%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The decline in data integration revenues was primarily due to declines in governmental sales and professional services, which were partially offset by an increase in maintenance services.

Other operating revenues decreased by \$17 million, or 1%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. The decrease in other operating revenues was primarily due to lower high-cost support revenues. These declines were partially offset by higher USF surcharge revenues related to increased universal service fund contribution factors. Other operating revenues increased by \$229 million, or 23%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The increase in other operating revenues was primarily due to additional revenue recorded under the CAF Phase 2 support program. For additional information about the CAF Phase 2 support program, see the discussion below in "Liquidity and Capital Resources—Connect America Fund."

We are aggressively marketing our strategic services in an effort to partially offset the continuing declines in our legacy services.

Further analysis of our segment operating revenues and trends impacting our performance are provided below in "Segment Results."

### Operating Expenses

Our current definitions of operating expenses are as follows:

- *Cost of services and products (exclusive of depreciation and amortization)* are expenses incurred in providing products and services to our customers. These expenses include: employee-related expenses directly attributable to operating and maintaining our network (such as salaries, wages, benefits and professional fees); facilities expenses (which include third-party telecommunications expenses we incur for using other carriers' networks to provide services to our customers); rents and utilities expenses; equipment sales expenses (such as data integration and modem expenses); payments to universal service funds (which are federal and state funds that are established to promote the availability of telecommunications services to all consumers at reasonable and affordable rates, among other things, and to which we are often required to contribute); certain litigation expenses associated with our operations; and other expenses directly related to our operations; and
- *Selling, general and administrative expenses* are corporate overhead and other operating expenses. These expenses include: employee-related expenses (such as salaries, wages, internal commissions, benefits and professional fees) directly attributable to selling products or services and employee-related expenses for administrative functions; marketing and advertising; property and other operating taxes and fees; external commissions; litigation expenses associated with general matters; bad debt expense; and other selling, general and administrative expenses.

These expense classifications may not be comparable to those of other companies.

The following tables summarize our operating expenses:

	Years Ended December 31,		Increase / (Decrease)	% Change
	2016	2015		
	(Dollars in millions)			
Cost of services and products (exclusive of depreciation and amortization)	\$ 7,774	7,778	(4)	— %
Selling, general and administrative	3,449	3,328	121	4 %
Depreciation and amortization	3,916	4,189	(273)	(7)%
Total operating expenses	<u>\$ 15,139</u>	<u>15,295</u>	<u>(156)</u>	<u>(1)%</u>

	Years Ended December 31,		Increase / (Decrease)	% Change
	2015	2014		
	(Dollars in millions)			
Cost of services and products (exclusive of depreciation and amortization)	\$ 7,778	7,846	(68)	(1)%
Selling, general and administrative	3,328	3,347	(19)	(1)%
Depreciation and amortization	4,189	4,428	(239)	(5)%
Total operating expenses	<u>\$ 15,295</u>	<u>15,621</u>	<u>(326)</u>	<u>(2)%</u>

#### Cost of Services and Products (exclusive of depreciation and amortization)

Cost of services and products (exclusive of depreciation and amortization) decreased by \$4 million, or less than 1%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. The decrease in costs of services and products (exclusive of depreciation and amortization) was primarily due to reductions in salaries and wages from lower headcount, professional fees, payment processing fees and customer premises equipment costs, which were substantially offset by increases in content costs for Prism TV (resulting from higher content volume and rates), network expense and USF rates. Cost of services and products (exclusive of depreciation and amortization) decreased by \$68 million, or 1%, for the year ended December 31, 2015 as compared to the year

ended December 31, 2014. Excluding the lower customer premises equipment costs, cost of services and products increased by \$56 million for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The increase in costs of services and products was primarily due to increases in pension and postretirement costs, USF rate increases, higher network expenses and increases in content costs for Prism TV. These increases were partially offset by decreases in salaries and wages from lower headcount, professional fees and contract labor costs.

### Selling, General and Administrative

Selling, general and administrative expenses increased by \$121 million, or 4%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. The increase in selling, general and administrative expenses was primarily due to increases in severance expenses associated with our recent workforce reduction, higher payments of employee health care claims, bad debt and other expenses (including fees related to the Level 3 acquisition), which were partially offset by reductions in professional fees and property and other taxes. Selling, general and administrative expenses decreased by \$19 million, or 1%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The decrease in selling, general and administrative expenses was primarily due to lower benefit expenses, insurance costs and asset impairment charges. These decreases were partially offset by increases in bad debt expense, external commissions and regulatory fines of \$15 million associated with a 911 system outage.

### Pension Lump Sum Offer

Our pension plan contains provisions that allow us, from time to time, to offer lump sum payment options to certain former employees in settlement of their future retirement benefits. These lump sum payments are paid from the trust that holds the plan's assets. Under pension settlement accounting, we record an accounting settlement charge associated with these lump sum payments only if, in the aggregate, they exceed the sum of the annual service and interest costs for the plan's net periodic pension benefit cost. There were no pension lump sum offerings in 2016, other than those to eligible employees who terminated during 2016. For the year ended December 31, 2015, we made cash settlement payments to former employees for lump sum offers of approximately \$356 million, but pension settlement accounting was not triggered in 2015. For the year ended December 31, 2014, we made cash settlement payments to former employees for lump sum offers of approximately \$460 million, which triggered pension settlement accounting and resulted in us recording additional pension expense of \$63 million. Pension expense is allocated to cost of services and products (exclusive of depreciation and amortization), selling, general and administrative and to capital projects. See Note 9—Employee Benefits to our consolidated financial statements in Item 8 of Part II of this annual report, for additional information on the pension lump sum offers.

### Depreciation and Amortization

The following tables provide detail of our depreciation and amortization expense:

	Years Ended December 31,		Increase / (Decrease)	% Change
	2016	2015		
	(Dollars in millions)			
Depreciation	\$ 2,691	2,836	(145)	(5)%
Amortization	1,225	1,353	(128)	(9)%
Total depreciation and amortization	\$ 3,916	4,189	(273)	(7)%

	Years Ended December 31,		Increase / (Decrease)	% Change
	2015	2014		
	(Dollars in millions)			
Depreciation	\$ 2,836	2,958	(122)	(4)%
Amortization	1,353	1,470	(117)	(8)%
Total depreciation and amortization	\$ 4,189	4,428	(239)	(5)%

Annual depreciation expense is impacted by several factors, including changes in our depreciable cost basis, changes in our estimates of the remaining economic life of certain network assets, the addition of new plant and our entry into an agreement to sell our data centers and colocation business. Depreciation expense decreased by \$145 million, or 5%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015 and decreased by \$122 million, or 4%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The depreciation expense related to our plant was lower for both periods due to full depreciation and retirement of certain plant placed in service prior to 2016 and 2015. Additionally, we ceased depreciating property, plant and equipment assets of our colocation business when we entered into the agreement to sell that business. We estimate that we would have recorded additional depreciation expense during 2016 of \$30 million if we had not agreed to sell the colocation business. The decrease in both periods was partially offset by an increase in depreciation expense attributable to new plant placed in service during the respective years.



Additionally, in 2015, the lower depreciation expense was further offset by the impact of changes in the estimated lives of certain property, plant and equipment which resulted in additional depreciation. The changes in the estimated lives of certain property, plant and equipment resulted in an increase in depreciation expense of approximately \$48 million for 2015, which was more than fully offset by the decrease in depreciation expense noted above. In addition, we developed a plan to migrate customers from one of our networks to another, which began in late 2014 and ended in late 2015. As a result, we implemented changes in estimates that reduced the remaining economic lives of certain network assets. The impact from the above-noted changes in estimates and network migration resulted in an increase in depreciation expense of approximately \$90 million for the year ended December 31, 2014.

Amortization expense decreased by \$128 million, or 9%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015 and decreased by \$117 million, or 8%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The decrease in amortization expense for both periods was primarily due to the use of accelerated amortization for a portion of our customer relationship assets and our entry into an agreement to sell our data centers and colocation business. The effect of using an accelerated amortization method results in an incremental decline in expense each period as the intangible assets amortize. We ceased amortizing the intangible assets of our colocation business when we entered into the agreement to sell that business. We estimate that we would have recorded additional amortization expense during 2016 of \$6 million if we had not agreed to sell the colocation business. In addition, amortization of capitalized software was lower in both periods due to software becoming fully amortized faster than new software was acquired or developed.

### Other Consolidated Results

The following tables summarize our total other expense, net and income tax expense:

	Years Ended December 31,		Increase / (Decrease)	% Change
	2016	2015		
	(Dollars in millions)			
Interest expense	\$ (1,318)	(1,312)	6	— %
Other income, net	7	23	(16)	(70)%
Total other expense, net	\$ (1,311)	(1,289)	22	2 %
Income tax expense	\$ 394	438	(44)	(10)%

	Years Ended December 31,		Increase / (Decrease)	% Change
	2015	2014		
	(Dollars in millions)			
Interest expense	\$ (1,312)	(1,311)	1	— %
Other income, net	23	11	12	109 %
Total other expense, net	\$ (1,289)	(1,300)	(11)	(1)%
Income tax expense	\$ 438	338	100	30 %

### Interest Expense

Interest expense increased by \$6 million, or less than 1%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. The increase in interest expense was substantially due to a reduction in the amount of net premium amortization recorded at acquisition due to the early retirement of several issuances of debt during the period, which has the effect of increasing interest expense and an increase in interest expense on unsecured notes related to the issuance of \$1.0 billion of new debt in April, 2016 in advance of a debt maturity in June, 2016. Interest expense increased by \$1 million, or less than 1%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The increase in interest expense was primarily due to a reduction in the amortization of debt premiums, which was substantially offset by higher capitalized interest, lower bond coupon rates and lower interest under our Credit Facility. See Note 5—Long-Term Debt and Credit Facilities to our consolidated financial statements in Item 8 of Part II of this annual report and Liquidity and Capital Resources below for additional information about our debt.

### Other Income, Net

Other income, net reflects certain items not directly related to our core operations, including our share of income from partnerships we do not control, interest income, gains and losses from non-operating asset dispositions and foreign currency gains and losses. Other income, net decreased by \$16 million, or 70%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. This decrease in other income, net was primarily due to losses on early retirement of debt, which was partially offset by the impact of nonrecurring funding from a state economic development program. Other income, net increased by \$12 million, or 109%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. This increase in other income, net was primarily due to the impact of a 2014 impairment charge of \$14 million recorded in connection with the sale of our 700 MHz A-Block Wireless Spectrum licenses, which was partially offset by a net loss on early retirement of debt in 2015.

### Income Tax Expense

Income tax expense decreased by \$44 million for the year ended December 31, 2016 as compared to the year ended December 31, 2015. Our income tax expense for the year ended December 31, 2015 increased by \$100 million from the amounts for the comparable prior year. For the years ended December 31, 2016, 2015 and 2014, our effective income tax rate was 38.6%, 33.3% and 30.5%, respectively. The effective tax rate for the year ended December 31, 2016 reflects a tax impact of \$18 million from an intercompany dividend payment from one of our foreign subsidiaries to its domestic parent company that was made as part of our corporate restructuring in preparation for the sale of our colocation business. The effective tax rate for the year ended December 31, 2015 reflects a tax benefit of approximately \$34 million related to affiliate debt rationalization, research and development tax credits of \$28 million for 2011 through 2015, and a \$16 million tax decrease due to changes in state taxes caused by apportionment changes, state tax rate changes and the changes in the expected utilization of net operating loss carryforwards ("NOLs"). The effective tax rate for the year ended December 31, 2014 reflects a \$60 million tax benefit associated with a worthless stock deduction for the tax basis in a wholly-owned foreign subsidiary as a result of developments in bankruptcy proceedings involving its sole asset, an indirect investment in KPNQwest, N.V. The subsidiary was acquired as part of the acquisition of Qwest and we assigned it no fair value in the acquisition due to the bankruptcy proceedings, which were then ongoing. The effective tax rate for the year ended December 31, 2014 also reflects a \$13 million tax decrease due to changes in state taxes caused by apportionment changes, state tax rate changes and the changes in the expected utilization of NOLs. The rate also reflects the absence of tax benefits from the impairment and disposition of our 700 MHz A-Block wireless spectrum licenses in 2014, because we are not likely to generate income of a character required to realize a tax benefit from the loss on disposition during the period permitted by law for utilization of that loss. See Note 13—Income Taxes to our consolidated financial statements in Item 8 of Part II of this annual report and "Critical Accounting Policies and Estimates—Income Taxes" below for additional information.

### Segment Results

The results for our business and consumer segments are summarized below for the years ended December 31, 2016, 2015 and 2014:

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
Total segment revenues	\$ 16,255	16,668	17,028
Total segment expenses	8,492	8,461	8,502
Total segment income	\$ 7,763	8,207	8,526
Total margin percentage	48%	49%	50%
Business segment:			
Revenues	\$ 10,352	10,646	11,030
Expenses	5,930	5,967	6,019
Income	\$ 4,422	4,679	5,011
Margin percentage	43%	44%	45%
Consumer segment:			
Revenues	\$ 5,903	6,022	5,998
Expenses	2,562	2,494	2,483
Income	\$ 3,341	3,528	3,515
Margin percentage	57%	59%	59%

The following table reconciles our total segment revenues and total segment income presented above to consolidated operating revenues and consolidated operating income reported in our consolidated statements of operations.

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
Total segment revenues	\$ 16,255	16,668	17,028
Other operating revenues	1,215	1,232	1,003
Operating revenues reported in our consolidated statements of operations	\$ 17,470	17,900	18,031
Total segment income	\$ 7,763	8,207	8,526
Other operating revenues	1,215	1,232	1,003
Depreciation and amortization	(3,916)	(4,189)	(4,428)
Other unassigned operating expenses	(2,731)	(2,645)	(2,691)
Operating income reported in our consolidated statements of operations	\$ 2,331	2,605	2,410

### Changes in Segment Reporting

During the first half of 2016, we implemented several changes with respect to the assignment of certain expenses to our reportable segments, including changes that increased our consumer segment expenses and decreased our business segment expenses in prior periods. We have recast our previously reported segment results for the years ended December 31, 2015 and 2014 to conform to the current presentation. See Note 14—Segment Information to our consolidated financial statements in Item 8 of Part II of this annual report for additional information on our changes in segment reporting.

### Allocation of Revenues and Expenses

Our segment revenues include all revenues from our strategic services, legacy services and data integration as described in more detail above. Segment revenues are based upon each customer's classification to an individual segment. We report our segment

revenues based upon all services provided to that segment's customers. For information on how we allocate expenses to our segments, as well as other additional information about our segments, see Note 14—Segment Information.

## Business Segment

The operations of our business segment have been impacted by several significant trends, including those described below:

- *Strategic services.* Our mix of total business segment revenues continues to migrate from legacy services to strategic services as our small, medium and enterprise business, wholesale and governmental customers increasingly demand integrated data, broadband, hosting and voice services. Our Ethernet-based services in the wholesale market face competition from cable companies and competitive fiber-based telecommunications providers. We anticipate continued pricing pressure for our colocation services as vendors continue to expand their enterprise colocation operations. In recent years, our competitors, as well as several large, diversified technology companies, have made substantial investments in cloud computing. This expansion in competitive cloud computing offerings has led to increased pricing pressure, a migration towards lower-priced cloud-based services and enhanced competition for contracts, and we expect these trends to continue. Customers' demand for new technology has also increased the number of competitors offering strategic services similar to ours. Price compression from each of these above-mentioned competitive pressures has negatively impacted the operating margins of our strategic services, and we expect this trend to continue. Operating costs also impact the operating margins of our strategic services, but to a lesser extent than price compression and customer disconnects. These operating costs include employee costs, sales commissions, software costs on selected services, installation costs and third-party facility costs. We believe increases in operating costs have generally had a greater impact on the operating margins of our strategic services as compared to our legacy services, principally because our strategic services rely more heavily upon the above-listed support functions;
- *Legacy services.* We continue to experience customers migrating away from our higher margin legacy services into lower margin strategic services. Our legacy services revenues have been, and we expect they will continue to be, adversely affected by access line losses and price compression. In particular, our access, local services and long-distance revenues have been, and we expect will continue to be, adversely affected by customer migration to more technologically advanced services, an increase in the use of non-voice communications and a related decrease in the demand for traditional voice services, industry consolidation and price compression caused by regulation and rate reductions. For example, many of our business segment customers are substituting cable, wireless and VoIP services for traditional voice telecommunications services, resulting in continued access revenue loss. Demand for our private line services (including special access) continues to decline due to our customers' optimization of their networks, industry consolidation and technological migration to higher-speed services. Although our legacy services generally face fewer direct competitors than certain of our strategic services, customer migration and, to a lesser degree, price compression from competitive pressures have negatively impacted our legacy revenues and the operating margins of our legacy services. We expect this trend to continue. Operating costs, such as installation costs and third-party facility costs, have also negatively impacted the operating margins of our legacy services, but to a lesser extent than customer loss, customer migration and price compression. Operating costs also tend to impact our legacy services to a lesser extent than our strategic services as noted above;
- *Data integration.* We expect both data integration revenue and the related costs will fluctuate from year to year as this offering tends to be more sensitive than others to changes in the economy and in spending trends of our federal, state and local governmental customers, many of whom have experienced substantial budget cuts over the past several years, with the possibility of additional future budget cuts. Our data integration operating margins are typically smaller than most of our other offerings; and
- *Operating efficiencies.* We continue to evaluate our segment operating structure and focus. This involves balancing our workforce in response to our workload requirements, productivity improvements and changes in industry, competitive, technological and regulatory conditions, while achieving operational efficiencies and improving our processes through automation. However, our ongoing efforts to increase revenue will continue to require that we incur higher costs in some areas. We also expect our business segment to benefit indirectly from enhanced efficiencies in our company-wide network operations.

The following tables summarize the results of operations from our business segment:

	<b>Business Segment</b>			
	<b>Years Ended December 31,</b>		<b>Increase / (Decrease)</b>	<b>% Change</b>
	<b>2016</b>	<b>2015</b>		
	<b>(Dollars in millions)</b>			
<b>Segment revenues:</b>				
<b>Strategic services</b>				
High-bandwidth data services (1)	\$ 2,990	2,816	174	6 %
Hosting services (2)	1,210	1,281	(71)	(6)%
Other strategic services (3)	703	624	79	13 %
<b>Total strategic services revenues</b>	<b>4,903</b>	<b>4,721</b>	<b>182</b>	<b>4 %</b>
<b>Legacy services</b>				
Voice services (4)	2,413	2,588	(175)	(7)%
Low-bandwidth data services (5)	1,382	1,594	(212)	(13)%
Other legacy services (6)	1,123	1,168	(45)	(4)%
<b>Total legacy services revenues</b>	<b>4,918</b>	<b>5,350</b>	<b>(432)</b>	<b>(8)%</b>
<b>Data integration</b>	531	575	(44)	(8)%
<b>Total revenues</b>	<b>10,352</b>	<b>10,646</b>	<b>(294)</b>	<b>(3)%</b>
<b>Segment expenses:</b>				
<b>Total expenses</b>	<b>5,930</b>	<b>5,967</b>	<b>(37)</b>	<b>(1)%</b>
<b>Segment income</b>	<b>\$ 4,422</b>	<b>4,679</b>	<b>(257)</b>	<b>(5)%</b>
<b>Segment margin percentage</b>	<b>43%</b>	<b>44%</b>		

(1) Includes MPLS and Ethernet revenue

(2) Includes colocation, hosting (including cloud hosting and managed hosting) and hosting area network revenue

(3) Includes primarily broadband, VoIP, video and IT services revenue

(4) Includes local and long-distance voice revenue

(5) Includes private line (including special access) revenue

(6) Includes UNEs, public access, switched access and other ancillary revenue

## Business Segment

	Years Ended December 31,		Increase / (Decrease)	% Change
	2015	2014		
	(Dollars in millions)			
Segment revenues:				
Strategic services				
High-bandwidth data services (1)	\$ 2,816	2,579	237	9 %
Hosting services (2)	1,281	1,316	(35)	(3)%
Other strategic services (3)	624	558	66	12 %
Total strategic services revenues	4,721	4,453	268	6 %
Legacy services				
Voice services (4)	2,588	2,777	(189)	(7)%
Low-bandwidth data services (5)	1,594	1,893	(299)	(16)%
Other legacy services (6)	1,168	1,219	(51)	(4)%
Total legacy services revenues	5,350	5,889	(539)	(9)%
Data integration	575	688	(113)	(16)%
Total revenues	10,646	11,030	(384)	(3)%
Segment expenses:				
Total expenses	5,967	6,019	(52)	(1)%
Segment income	\$ 4,679	5,011	(332)	(7)%
Segment margin percentage	44%	45%		

- (1) Includes MPLS and Ethernet revenue  
(2) Includes colocation, hosting (including cloud hosting and managed hosting) and hosting area network revenue  
(3) Includes primarily broadband, VoIP, video and IT services revenue  
(4) Includes local and long-distance voice revenue  
(5) Includes private line (including special access) revenue  
(6) Includes UNEs, public access, switched access and other ancillary revenue

*Segment Revenues*

Business segment revenues decreased by \$294 million, or 3%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. The decrease in business segment revenues was primarily due to declines in our legacy services revenues. The decline in legacy services revenues was attributable to a reduction in local service access lines and lower volumes of long-distance and access services for the reasons noted above and to reductions in the volume of private line (including special access) services. The increase in our strategic services revenues was primarily due to increases in MPLS unit growth and higher Ethernet and VOIP volumes, which were partially offset by declines in our hosting services. The decrease in our data integration revenues was primarily due to lower sales of customer premises equipment to governmental and business customers and to declines in maintenance services. Business segment revenues decreased by \$384 million, or 3%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The decrease in business segment revenues was primarily due to declines in legacy services revenues and data integration revenues, which were partially offset by the growth in our strategic services revenues. The decline in legacy services revenues was attributable to a reduction in local service access lines and lower volumes of long-distance, access and traditional WAN services for the reasons noted above and a reduction in private line (including special access) volumes, as well as a pricing reduction on private line services for a large wholesale customer in exchange for a longer term commitment. The growth in our strategic services revenues was primarily due to MPLS unit growth and higher Ethernet volumes, which were partially offset by a reduction in hosting services. The decrease in data integration revenues was primarily due to lower sales of customer premises equipment to governmental and business customers during the period.

### *Segment Expenses*

Business segment expenses decreased by \$37 million, or 1%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. The decrease in our business segment expenses was primarily due to decreases in salaries and wages, professional fees and payment processing fees, which were partially offset by increases in facility costs, network expense and real estate and power costs. Business segment expenses decreased by \$52 million, or 1%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The decrease was primarily due to lower customer premises equipment costs resulting from the lower sales noted above in segment revenues. Excluding the lower customer premises equipment costs, business expenses increased by \$62 million for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The increase is primarily due to increases in salaries and wages, benefits expense, external commissions, network expense and facility costs, which were partially offset by decreases in professional fees, materials and supplies and fleet expenses.

### *Segment Income*

Business segment income decreased by \$257 million, or 5%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015 and decreased by \$332 million, or 7%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The decrease in business segment income for both periods was due predominantly to the loss of customers and lower service volumes in our legacy services.

### **Consumer Segment**

The operations of our consumer segment have been impacted by several significant trends, including those described below:

- *Strategic services.* In order to remain competitive and attract additional residential broadband subscribers, we believe it is important to continually increase our broadband network's scope and connection speeds. As a result, we continue to invest in our broadband network, which allows for the delivery of higher-speed broadband services to a greater number of customers. We compete in a maturing broadband market in which most consumers already have broadband services and growth rates in new subscribers have slowed. Moreover, as described further in Item 1A of Part I of this annual report, certain of our competitors continue to provide broadband services at higher average transmission speeds than ours or through advanced wireless data service offerings, both of which we believe have impacted the competitiveness of certain of our broadband offerings. The offering of our facilities-based video services in our markets requires us to incur substantial start-up expenses in advance of marketing and selling the service. Also, our associated content costs continue to increase and the video business has become more competitive as more options become available to customers to access video services through new technologies. The demand for new technology has increased the number of competitors offering strategic services similar to ours. Price compression and new technology from our competitors have negatively impacted the operating margins of our strategic services and we expect this trend to continue. Operating costs also impact the operating margins of our strategic services. These operating costs include employee costs, marketing and advertising expenses, sales commissions, Prism TV content costs and installation costs. We believe increases in operating costs have generally had a greater impact on our operating margins of our strategic services as compared to our legacy services, principally because our strategic services rely more heavily upon the above-listed costs;
- *Legacy services.* Our voice revenues have been, and we expect they will continue to be, adversely affected by access line losses and lower long-distance voice service volumes. Intense competition and product substitution continue to drive our access line losses. For example, many consumers are substituting cable and wireless voice services and electronic mail, texting and social networking non-voice services for traditional voice telecommunications services. We expect that these factors will continue to negatively impact our business. As a result of the expected loss of higher margin services associated with access lines, we continue to offer our customers service bundling and other product promotions to help mitigate this trend, as described below. Customer migration and price compression from competitive pressures have not only negatively impacted our legacy revenues, but they have also negatively impacted the operating margins of our legacy services and we expect this trend to continue. Operating costs, such as installation costs and facility costs, have also negatively impacted the operating margins of our legacy services, but to a lesser extent than customer migration and price compression. Operating costs also tend to impact our legacy services margins to a lesser extent than our strategic services as noted above;
- *Service bundling and product promotions.* We offer our customers the ability to bundle multiple products and services. These customers can bundle broadband services with other services such as local voice, video, long-distance and wireless. While we believe our bundled service offerings can help retain customers, they also tend to lower our profit margins in the consumer segment due to the related discounts; and



- *Operating efficiencies.* We continue to evaluate our segment operating structure and focus. This involves balancing our workforce in response to our workload requirements, productivity improvements and changes in industry, competitive, technological and regulatory conditions. We also expect our consumer segment to benefit indirectly from enhanced efficiencies in our company-wide network operations.

The following tables summarize the results of operations from our consumer segment:

	Consumer Segment			
	Years Ended December 31,		Increase / (Decrease)	% Change
	2016	2015		
	(Dollars in millions)			
Segment revenues:				
Strategic services				
Broadband services (1)	\$ 2,689	2,611	78	3 %
Other strategic services (2)	458	421	37	9 %
Total strategic services revenues	3,147	3,032	115	4 %
Legacy services				
Voice services (3)	2,442	2,676	(234)	(9)%
Other legacy services (4)	312	312	—	— %
Total legacy services revenues	2,754	2,988	(234)	(8)%
Data integration	2	2	—	— %
Total revenues	5,903	6,022	(119)	(2)%
Segment expenses:				
Total expenses	2,562	2,494	68	3 %
Segment income	\$ 3,341	3,528	(187)	(5)%
Segment income margin percentage	57%	59%		

- (1) Includes broadband and related services revenue  
(2) Includes video and other revenue  
(3) Includes local and long-distance voice revenue  
(4) Includes other ancillary revenue

## Consumer Segment

	Years Ended December 31,		Increase / (Decrease)	% Change
	2015	2014		
	(Dollars in millions)			
Segment revenues:				
Strategic services				
Broadband services (1)	\$ 2,611	2,469	142	6 %
Other strategic services (2)	421	381	40	10 %
Total strategic services revenues	3,032	2,850	182	6 %
Legacy services				
Voice services (3)	2,676	2,865	(189)	(7)%
Other legacy services (4)	312	279	33	12 %
Total legacy services revenues	2,988	3,144	(156)	(5)%
Data integration	2	4	(2)	(50)%
Total revenues	6,022	5,998	24	— %
Segment expenses:				
Total expenses	2,494	2,483	11	— %
Segment income	\$ 3,528	3,515	13	— %
Segment income margin percentage	59%	59%		

- (1) Includes broadband and related services revenue  
(2) Includes video and other revenue  
(3) Includes local and long-distance voice revenue  
(4) Includes other ancillary revenue

*Segment Revenues*

Consumer segment revenues decreased by \$119 million, or 2%, for year ended December 31, 2016 as compared to the year ended December 31, 2015. The decrease in our consumer segment revenues was primarily due to the declines in our legacy services revenues, which were partially offset by increases in our strategic revenues. The decline in our legacy services revenues for both periods was primarily due to lower local and long-distance voice service volumes associated with access line losses resulting from the competitive and technological factors noted above. The increase in our strategic services revenues was primarily due to 2016 rate increases resulting from various pricing initiatives on broadband, Prism TV and other strategic products and services, and increases in the number of our Prism TV customers, which were partially offset by a decline in broadband customers. Consumer segment revenues increased by \$24 million, or less than 1%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. The increase in strategic services revenues was primarily due to increases in the number of Prism TV customers, as well as from 2015 price increases on various services. The decline in legacy services revenues was primarily due to declines in local and long-distance services volumes associated with access line losses resulting from the competitive and technological factors as further described above.

*Segment Expenses*

Consumer segment expenses increased by \$68 million, or 3%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. The increase in our consumer segment expenses was primarily due to increases in costs related to Prism TV (resulting from higher content volume and rates), professional fees, sales commissions, bad debt expense and network costs, which were partially offset by reductions in salaries and wages from lower headcount and payment processing fees. Consumer segment expenses increased by \$11 million, or less than 1%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. This increase was primarily due to increases in Prism TV content costs (resulting from higher volume and rates) and bad debt expense, which were partially offset by reductions in employee-related costs, facility costs, fleet expenses and network expenses.



### *Segment Income*

Consumer segment income decreased by \$187 million, or 5%, for the year ended December 31, 2016 as compared to the year ended December 31, 2015. This decrease was primarily due to loss of customers from legacy services and increases in the costs related to the growth in Prism TV. Consumer segment income increased by \$13 million, or less than 1%, for the year ended December 31, 2015 as compared to the year ended December 31, 2014. This increase was primarily due to price increases on various services.

### **Critical Accounting Policies and Estimates**

Our consolidated financial statements are prepared in accordance with accounting principles that are generally accepted in the United States. The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of our assets, liabilities, revenues and expenses. We have identified certain policies and estimates as critical to our business operations and the understanding of our past or present results of operations related to (i) goodwill, customer relationships and other intangible assets; (ii) property, plant and equipment; (iii) pension and post-retirement benefits; (iv) loss contingencies and litigation reserves; (v) Connect America Fund; and (vi) income taxes. These policies and estimates are considered critical because they had a material impact, or they have the potential to have a material impact, on our consolidated financial statements and because they require us to make significant judgments, assumptions or estimates. We believe that the estimates, judgments and assumptions made when accounting for the items described below were reasonable, based on information available at the time they were made. However, there can be no assurance that actual results will not differ from those estimates.

### *Goodwill, Customer Relationships and Other Intangible Assets*

We amortize customer relationships primarily over an estimated life of 10 to 15 years, using either the sum-of-the-years-digits or the straight-line methods, depending on the type of customer. We amortize capitalized software using the straight-line method over estimated lives ranging up to 7 years, except for approximately \$237 million of our capitalized software costs, which represents costs to develop an integrated billing and customer care system which is amortized using the straight-line method over a 20 year period. We annually review the estimated lives and methods used to amortize our other intangible assets, primarily capitalized software. The amount of future amortization expense may differ materially from current amounts, depending on the results of our annual reviews.

Our goodwill was derived from numerous acquisitions where the purchase price exceeded the fair value of the net assets acquired.

We are required to reassign goodwill to reporting units each time we reorganize our internal reporting structure which causes a change in the composition of our reporting units. We assign goodwill to the reporting units using a relative fair value approach. We utilize the trailing twelve months earnings before interest, taxes, depreciation and amortization as our allocation methodology as we believe that it represents a reasonable proxy for the fair value of the operations being reorganized. The use of other fair value assignment methods could result in materially different results. For additional information on our segments, see Note 14—Segment Information to our consolidated financial statements in Item 8 of Part II of this annual report.

We are required to assess goodwill for impairment at least annually, or more frequently, if an event occurs or circumstances change that would indicate an impairment may have occurred. We are required to write-down the value of goodwill in periods in which the recorded amount of goodwill exceeds the implied fair value of goodwill. Our reporting units are not discrete legal entities with discrete financial statements. Our assets and liabilities are employed in and relate to the operations of our reporting units. Therefore, the equity carrying value and future cash flows must be estimated each time a goodwill impairment analysis is performed on a reporting unit. As a result, our assets, liabilities and cash flows are assigned to reporting units using reasonable and consistent allocation methodologies. Certain estimates, judgments and assumptions are required to perform these assignments. We believe these estimates, judgments and assumptions to be reasonable, but changes in many of these can significantly affect each reporting unit's equity carrying value and future cash flows utilized for our goodwill impairment test. Our annual assessment date for testing goodwill impairment is October 31.

As of October 31, 2016, we assessed goodwill for impairment for our three reporting units, which we determined to be business (excluding wholesale), consumer and wholesale and determined that the estimated fair value of our wholesale reporting unit was substantially in excess of our carrying value of equity and the estimated fair value of our business and consumer reporting units exceeded our carrying value of equity by 28% and 18%, respectively.

For additional information on our goodwill balances by segment, see Note 4—Goodwill, Customer Relationships and Other Intangible Assets in Item 8 of Part II of this annual report.



We may be required to assess our goodwill for impairment before our next required assessment date of October 31, 2017 under certain circumstances, including any failure to meet our forecasted future operating results or any significant increases in our weighted average cost of capital. In addition, we cannot assure that adverse conditions will not trigger future goodwill impairment assessments or impairment charges. A number of factors, many of which we cannot control, could affect our financial condition, operating results and business prospects and could cause our actual results to differ from the estimates and assumptions we employed in our goodwill impairment assessment. These factors include, but are not limited to, (i) further weakening in the overall economy; (ii) a significant decline in our stock price and resulting market capitalization as a result of an adverse change to our overall business operations; (iii) changes in the discount rate we use in our testing; (iv) successful efforts by our competitors to gain market share in our markets; (v) adverse changes as a result of regulatory or legislative actions; (vi) a significant adverse change in our legal affairs or in the overall business climate; and (vii) recognition of a goodwill impairment loss in the financial statements of one or more of our subsidiaries that are a component of our segments. For additional information, see "Risk Factors" in Item 1A of Part I of this annual report. We will continue to monitor certain events that impact our operations to determine if an interim assessment of goodwill impairment should be performed prior to the next required assessment date of October 31, 2017.

### *Property, Plant and Equipment*

Property, plant and equipment acquired in connection with our acquisitions was recorded based on its estimated fair value as of its acquisition date, plus the estimated value of any associated legally or contractually required asset retirement obligation. Purchased and constructed property, plant and equipment is recorded at cost, plus the estimated value of any associated legally or contractually required asset retirement obligation. Renewals and betterments of plant and equipment are capitalized while repairs, as well as renewals of minor items, are charged to operating expense. Depreciation of property, plant and equipment is provided on the straight-line method using class or overall group rates. The group method provides for the recognition of the remaining net investment, less anticipated net salvage value, over the remaining useful life of the assets. This method requires the periodic revision of depreciation rates.

Normal retirements of property, plant and equipment are charged against accumulated depreciation, with no gain or loss recognized. We depreciate such property on the straight-line method over estimated service lives ranging from 3 to 45 years.

We perform annual internal reviews to evaluate the reasonableness of the depreciable lives for our property, plant and equipment. Our reviews utilize models that take into account actual usage, physical wear and tear, replacement history, assumptions about technology evolution and, in certain instances, actuarially determined probabilities to estimate the remaining life of our asset base.

Due to rapid changes in technology and the competitive environment, determining the estimated economic life of telecommunications plant and equipment requires a significant amount of judgment. We regularly review data on utilization of equipment, asset retirements and salvage values to determine adjustments to our depreciation rates. The effect of a hypothetical one year increase or decrease in the estimated remaining useful lives of our property, plant and equipment would have decreased depreciation expense by approximately \$390 million annually or increased depreciation expense by approximately \$550 million annually, respectively.

### *Pension and Post-retirement Benefits*

We sponsor a noncontributory qualified defined benefit pension plan (referred to as our qualified pension plan) for a substantial portion of our employees. In addition to this tax-qualified pension plan, we also maintain several non-qualified pension plans for certain eligible highly compensated employees. We also maintain post-retirement benefit plans that provide health care and life insurance benefits for certain eligible retirees.

In 2016, approximately 53% of the qualified pension plan's January 1, 2016 net actuarial loss balance of \$2.843 billion was subject to amortization as a component of net periodic expense over the average remaining service period of participating employees expected to receive benefits, which ranges from 9 to 10 years for the plan. The other 47% of the qualified pension plan's beginning net actuarial loss balance was treated as indefinitely deferred during 2016. The entire beginning net actuarial loss of \$147 million for the post-retirement benefit plans was treated as indefinitely deferred during 2016.

In 2015, approximately 45% of the qualified pension plan's January 1, 2015 net actuarial loss balance of \$2.740 billion was subject to amortization as a component of net periodic expense over the average remaining service period of participating employees expected to receive benefits, which ranges from 8 to 9 years for the plan. The other 55% of the qualified pension plan's beginning net actuarial loss balance was treated as indefinitely deferred during 2015. The entire beginning net actuarial loss of \$277 million for the post-retirement benefit plans was treated as indefinitely deferred during 2015.



In 2014, approximately 16% of the qualified pension plans' January 1, 2014 net actuarial loss balance of \$1.048 billion was subject to amortization as a component of net periodic expense over the average remaining service period of participating employees expected to receive benefits, which ranges from 8 to 9 years for the plans. The other 84% of the pension plans' beginning net actuarial loss balance was treated as indefinitely deferred during 2014. The entire beginning net actuarial loss of \$37 million for the post-retirement benefit plans was treated as indefinitely deferred during 2014.

In computing our pension and post-retirement health care and life insurance benefit obligations, our most significant assumptions are the discount rate and mortality rates. In computing our periodic pension and post-retirement benefit expense, our most significant assumptions are the discount rate and the expected rate of return on plan assets.

The discount rate for each plan is the rate at which we believe we could effectively settle the plan's benefit obligations as of the end of the year. We selected each plan's discount rate based on a cash flow matching analysis using hypothetical yield curves from U.S. corporate bonds rated high quality and projections of the future benefit payments that constitute the projected benefit obligation for the plans. This process establishes the uniform discount rate that produces the same present value of the estimated future benefit payments as is generated by discounting each year's benefit payments by a spot rate applicable to that year. The spot rates used in this process are derived from a yield curve created from yields on the 60th to 90th percentile of U.S. high quality bonds.

In 2016, we changed the method we use to estimate the service and interest components of net periodic benefit expense for pension and other postretirement benefit obligations. This change resulted in a decrease in the service and interest components in 2016. Beginning in 2016, we utilized a full yield curve approach in connection with estimating these components by applying the specific spot rates along the yield curve used in the determination of the benefit obligation to the relevant projected cash flows, as opposed to the single weighted-average discount rate derived from the yield curve that we have used in the past. We believe this change more precisely measures service and interest costs by improving the correlation between projected benefit cash flows to the corresponding spot yield curve rates. This change did not affect the measurement of our total benefit obligations but lowered our annual net periodic benefit cost by approximately \$149 million in 2016. This change was treated as a change in accounting estimate and, accordingly, we did not adjust the amounts recorded in 2015 or 2014.

Mortality rates help predict the expected life of plan participants and are based on historical demographic studies by the Society of Actuaries. In 2016, we adopted the revised mortality table and projection scale released by the Society of Actuaries ("SOA"), which decreased the projected benefit obligation of our benefit plans by \$268 million. The 2015 revised mortality table and projection scale decreased the 2015 projected benefit obligation of our benefit plans by \$379 million. In 2014, the SOA published new mortality rate tables reflecting increases in the projected life expectancies of North Americans since its publications of earlier tables. We adopted the new tables immediately. This resulted in an increase to the projected benefit obligation of approximately \$1.3 billion for our pension and post-retirement benefit plans. The change in the projected benefit obligation of our benefit plans was recognized as part of the net actuarial loss and is included in accumulated other comprehensive loss, a portion of which is subject to amortization over the remaining estimated life of plan participants, which was approximately 9 to 10 years as of December 31, 2016.

The expected rate of return on plan assets is the long-term rate of return we expect to earn on the plans' assets in the future, net of administrative expenses paid from plan assets. The rate of return is determined by the strategic allocation of plan assets and the long-term risk and return forecast for each asset class. The forecasts for each asset class are generated primarily from an analysis of the long-term expectations of various third party investment management organizations to which we then add a factor of 50 basis points to reflect the benefit we expect to result from our active management of the assets. The expected rate of return on plan assets is reviewed annually and revised, as necessary, to reflect changes in the financial markets and our investment strategy.

To compute the expected return on pension and post-retirement benefit plan assets, we apply an expected rate of return to the fair value of the pension plan assets and to the fair value of the post-retirement benefit plan assets adjusted for contribution timing and for projected benefit payments to be made from the plan assets. Annual market volatility for these assets (higher or lower than expected return) is reflected in the net actuarial losses.

Changes in any of the above factors could significantly impact operating expenses in the consolidated statements of operations and other comprehensive (loss) income in the consolidated statements of comprehensive income (loss) as well as the value of the liability and accumulated other comprehensive loss of stockholders' equity on our consolidated balance sheets. The expected return on plan assets is reflected as a reduction to our pension and post-retirement benefit expense. If our assumed expected rates of return for 2016 were 100 basis points lower, our qualified pension and post-retirement benefit expenses for 2016 would have increased by \$92 million. If our assumed discount rates for 2016 were 100 basis points lower, our qualified pension and post-retirement benefit expenses for 2016 would have increased by \$46 million and our projected benefit obligation for 2016 would have increased by approximately \$1.753 billion.



### *Loss Contingencies and Litigation Reserves*

We are involved in several material legal proceedings, as described in more detail in Note 16—Commitments and Contingencies to our consolidated financial statements in Item 8 of Part II of this annual report. We assess potential losses in relation to these and other pending or threatened tax and legal matters. For matters not related to income taxes, if a loss is considered probable and the amount can be reasonably estimated, we recognize an expense for the estimated loss. To the extent these estimates are more or less than the actual liability resulting from the resolution of these matters, our earnings will be increased or decreased accordingly. If the differences are material, our consolidated financial statements could be materially impacted.

For matters related to income taxes, if we determine in our judgment that the impact of an uncertain tax position is more likely than not to be sustained upon audit by the relevant taxing authority, then we recognize in our financial statements a benefit for the largest amount that is more likely than not to be sustained. No portion of an uncertain tax position will be recognized if we determine in our judgment that the position has less than a 50% likelihood of being sustained. Though the validity of any tax position is a matter of tax law, the body of statutory, regulatory and interpretive guidance on the application of the law is complex and often ambiguous. Because of this, whether a tax position will ultimately be sustained may be uncertain.

### *Connect America Fund*

In 2015, we accepted CAF funding from the FCC of approximately \$500 million per year for six years to fund the deployment of voice and broadband capable infrastructure for approximately 1.2 million rural households and businesses (living units) in 33 states under the CAF Phase 2 high-cost support program. This program provides a monthly high-cost subsidy similar to the support provided by the FCC's previous cost reimbursement programs. Although we believe that there is no specific authoritative U.S. GAAP guidance for the treatment of government assistance, we identified three acceptable methods to account for these funds: (1) recognize revenue when entitled to receive cash, (2) defer cash received until the living units are enabled to receive the service at the FCC specified level, or (3) record the cash received as contra capital. After assessing these alternatives, we have determined that we will recognize CAF Phase 2 funds each month as revenue when we are entitled to receive the cash less a deferred amount. The amount of revenue deferred in 2016 was approximately \$12 million. We believe our recognition methodology is consistent with other companies in our industry in the United States, but may not necessarily be consistent with companies outside the United States that receive similar government funding, and we cannot provide assurances to this effect.

In computing the amount of revenue to recognize, we assume that we will not be able to economically enable 100% of the required living units in every state with voice and broadband capabilities under the CAF Phase 2 program. We defer recognition of the funds related to potential living units that we estimate we will not enable until we can with reasonable assurance determine that we can fully meet the enablement targets. As disclosed elsewhere herein, in some limited instances, a portion of the funds must be returned if enablement targets are not attained. Based on estimated enablement, the effect of a hypothetical 1% decrease in our estimate of living units we will not enable with voice and broadband capabilities under the CAF Phase 2 program would have increased our revenue by \$3 million in 2016 and a 1% increase would have decreased our revenue by \$9 million in 2016.

For additional information about the CAF Phase 2 support program, see the discussion below in "Liquidity and Capital Resources—Connect America Fund."

### *Income Taxes*

Our provision for income taxes includes amounts for tax consequences deferred to future periods. We record deferred income tax assets and liabilities reflecting future tax consequences attributable to tax credit carryforwards, differences between the financial statement carrying value of assets and liabilities and the tax bases of those assets and liabilities and tax net operating loss carryforwards, or NOLs. Deferred taxes are computed using enacted tax rates expected to apply in the year in which the differences are expected to affect taxable income. The effect on deferred income tax assets and liabilities of a change in tax rate is recognized in earnings in the period that includes the enactment date.

The measurement of deferred taxes often involves the exercise of considerable judgment related to the realization of tax basis. Our deferred tax assets and liabilities reflect our assessment that tax positions taken in filed tax returns and the resulting tax basis are more likely than not to be sustained if they are audited by taxing authorities. Assessing tax rates that we expect to apply and determining the years when the temporary differences are expected to affect taxable income requires judgment about the future apportionment of our income among the states in which we operate. Any changes in our practices or judgments involved in the measurement of deferred tax assets and liabilities could materially impact our financial condition or results of operations.



In connection with recording deferred income tax assets and liabilities, we establish valuation allowances when necessary to reduce deferred income tax assets to amounts that we believe are more likely than not to be realized. We evaluate our deferred tax assets quarterly to determine whether adjustments to our valuation allowance are appropriate in light of changes in facts or circumstances, such as changes in tax law, interactions with taxing authorities and developments in case law. In making this evaluation, we rely on our recent history of pre-tax earnings. We also rely on our forecasts of future earnings and the nature and timing of future deductions and benefits represented by the deferred tax assets, all which involve the exercise of significant judgment. At December 31, 2016, we established a valuation allowance of \$375 million primarily related to state NOLs, as it is more likely than not that these NOLs will expire unused. If forecasts of future earnings and the nature and estimated timing of future deductions and benefits change in the future, we may determine that a valuation allowance for certain deferred tax assets is appropriate, which could materially impact our financial condition or results of operations. See Note 13—Income Taxes to our consolidated financial statements in Item 8 of Part II of this annual report for additional information.

## **Liquidity and Capital Resources**

### *Overview*

At December 31, 2016, we held cash and cash equivalents of \$222 million and we had \$1.630 billion of borrowing capacity available under our \$2 billion amended and restated revolving credit facility (referred to as our "Credit Facility", which is described further below). At December 31, 2016, cash and cash equivalents of \$44 million were held in foreign bank accounts for the purpose of funding our foreign operations. Due to various factors, our access to foreign cash is generally much more restricted than our access to domestic cash.

Our executive officers and our Board of Directors periodically review our sources and potential uses of cash in connection with our annual budgeting process. Generally speaking, our principal funding source is cash from operating activities, and our principal cash requirements include operating expenses, capital expenditures, income taxes, debt repayments, dividends, periodic stock repurchases, periodic pension contributions and other benefits payments. As discussed below, the amount we pay for income taxes is expected to increase for most of 2017, and the amount we pay for retiree healthcare benefits is expected to increase substantially in 2017. The potential impact of the pending sale of our colocation business and data centers and the potential impact of the pending acquisition of Level 3 are further described below.

Based on our current capital allocation objectives, during 2017 we anticipate expending approximately \$2.6 billion of cash for capital investment in property, plant and equipment and up to \$1.176 billion for dividends on our common stock, based on the current annual common stock dividend rate of \$2.16 and the current number of outstanding common shares, assuming solely for these purposes no impact from the Level 3 acquisition. During 2017, we have debt maturities of \$1.421 billion, scheduled debt principal payments of \$22 million and capital lease and other fixed payments of approximately \$100 million (including \$41 million of capital lease obligations related to the colocation operations), excluding liabilities that we expect to assume later in 2017 in connection with consummating the Level 3 acquisition. Each of the expenditures are described further below.

We will continue to monitor our future sources and uses of cash, and anticipate that we will make adjustments to our capital allocation strategies when, as and if determined by our Board of Directors. We typically use our revolving credit facility as a source of liquidity for operating activities and our other cash requirements.

### *Potential Impact of the Sale of Our Colocation Business and Data Centers*

If, as anticipated, we sell our colocation business and data centers in the manner discussed in Note 3—Pending Sale of Colocation Business and Data Centers to our consolidated financial statements in Item 8 of Part II of this annual report, we expect to receive net cash proceeds of approximately \$1.5 billion to \$1.7 billion from the sale, which is net of tax payments relating to the sale of approximately \$100 million to \$200 million, which we anticipate will be triggered by certain corporate restructuring actions we are taking in the first quarter of 2017 regarding certain subsidiaries involved in the colocation business. We also expect ongoing cash flows from operating activities will be negatively impacted by approximately \$30 million to \$45 million per quarter.

### ***Potential Impact of the Pending Acquisition of Level 3***

If, as anticipated, we complete the acquisition of Level 3 by the end of third quarter of 2017 in the manner discussed in Note 2—Pending Acquisition of Level 3 to our consolidated financial statements in Item 8 of Part II of this annual report, we expect our operations, financial position and cash flows to be significantly impacted following the closing of the transaction. We expect to issue a significant amount of new debt to finance the Level 3 acquisition, and we would assume approximately \$10.9 billion of Level 3's outstanding debt upon consummating the acquisition. With this additional debt, we would expect our cash paid for interest payments to be significantly higher following the closing of the transaction. We project that our capital expenditures would increase significantly; we anticipate, based on information included in Level 3's annual guidance regarding its estimated 2017 capital expenditures, that Level 3 will spend approximately \$100 million to \$125 million per month on average, in the period prior to closing, but that amount could be significantly different than amounts that we expect to spend in the months following the closing of the transaction. In connection with consummating the acquisition, we would expect to issue approximately 538 million shares of our common stock to Level 3 stockholders (including shares of CenturyLink common stock expected to be issued in exchange for outstanding Level 3 equity awards), based on the number of Level 3 shares held of record on January 27, 2017. Based on our current quarterly common stock dividend rate of \$0.54 per share, this issuance of additional shares would result in an additional incremental dividend payment of approximately \$290 million per quarter. Also, we expect our upcoming cash payments for transaction costs, integration costs and debt financing costs to be material primarily following the closing of the transaction. These above factors are expected to result in a net cash outflow for the period of 2017 following the closing. However, we expect we will have sufficient liquidity to more than offset the impact of the net cash outflows.

### ***Capital Expenditures***

We incur capital expenditures on an ongoing basis in order to enhance and modernize our networks, compete effectively in our markets and expand our service offerings. We evaluate capital expenditure projects based on a variety of factors, including expected strategic impacts (such as forecasted impact on revenue growth, productivity, expenses, service levels and customer retention) and our expected return on investment. The amount of capital investment is influenced by, among other things, demand for our services and products, cash flow generated by operating activities, cash required for other purposes and regulatory considerations (such as our CAF Phase 2 infrastructure buildout requirements). Based on current circumstances, we estimate that our total capital expenditures for 2017 will be approximately \$2.6 billion, inclusive of CAF Phase 2 related capital expenditures, but exclusive of additional capital expenditures with respect to the Level 3 operations that we expect to acquire later this year.

Our capital expenditures continue to be focused on our strategic services. For more information on our capital spending, see "Business" and "Risk Factors" in Items 1 and 1A, respectively, of Part I of this annual report.

### ***Debt and Other Financing Arrangements***

Subject to market conditions, we expect to continue to issue debt securities from time to time in the future to refinance a substantial portion of our maturing debt, including issuing Qwest Corporation debt securities to refinance its maturing debt to the extent feasible. The availability, interest rate and other terms of any new borrowings will depend on the ratings assigned to us and Qwest Corporation by credit rating agencies, among other factors. For further information on our debt maturities, see "Future Contractual Obligations" below.

As of the date of this annual report, the credit ratings for the senior unsecured debt of CenturyLink, Inc. and Qwest Corporation were as follows:

Agency	CenturyLink, Inc.	Qwest Corporation
Standard & Poor's	BB	BBB-
Moody's Investors Service, Inc. <sup>(1)</sup>	Ba3	Ba1
Fitch Ratings	BB+	BBB-

<sup>(1)</sup> On March 15, 2016, Moody's Investors Service, Inc. downgraded CenturyLink, Inc.'s rating from Ba2 to Ba3 and downgraded Qwest Corporation's rating from Baa3 to Ba1.

Our credit ratings are reviewed and adjusted from time to time by the rating agencies, and downgrades of CenturyLink, Inc.'s senior unsecured debt ratings could, under certain circumstances, incrementally increase the cost of our borrowing under the Credit

Facility. Moreover, any additional downgrades of CenturyLink, Inc.'s or Qwest Corporation's senior unsecured debt ratings could impact our access to debt capital or further raise our borrowing costs. See "Risk Factors—Risks Affecting our Liquidity and Capital Resources" in Item 1A of Part I of this annual report.

Following the announcement of our pending acquisition of Level 3, Standard & Poor's indicated that CenturyLink, Inc.'s current unsecured senior debt rating of BB has been placed on watch with negative implications, Moody's Investor Service, Inc. indicated that CenturyLink, Inc.'s current senior unsecured debt rating of Ba3 has been placed on review for downgrade and Fitch Ratings indicated that CenturyLink, Inc.'s current unsecured senior debt rating of BB+ has been placed on negative watch. Additionally, Qwest Corporation's current unsecured senior debt rating of Ba1 has been placed on review for downgrade by Moody's Investor Service, Inc. and its current unsecured senior debt rating of BBB- has been placed on negative watch by Fitch Ratings. It is expected that any downgrades would be made only following the completion of the Level 3 acquisition.

### *Net Operating Loss Carryforwards*

In recent years, we have been using Net Operating Loss ("NOL") carryforwards to offset a large portion of our federal taxable income. As of December 31, 2016, we have substantially utilized our federal NOL carryforwards. A portion of these remaining NOL carryforwards are subject to the limitations imposed by section 382 of the Internal Revenue Code ("Code"). As a result of the substantial utilization of the NOL carryforwards in prior years and the limitations imposed on portions of the remaining NOL carryforward balance, the amounts of our cash flows dedicated to or required for the payment of federal taxes has increased and is expected to continue to increase substantially during 2017 prior to our anticipated acquisition of additional NOLs later this year, as described further below. The amounts of our near-term tax payments will depend upon many factors, including our future earnings and tax circumstances. Based on current laws (including the extension of bonus depreciation) and our current estimates of 2017 earnings, we estimate our cash income tax liability related to 2017 will be between \$500 million to \$600 million, exclusive of (i) tax payments relating to the sale of our data centers and colocation business of approximately \$100 million to \$200 million, which we anticipate will be triggered by certain corporate restructuring actions we are taking in the first quarter of 2017 regarding certain subsidiaries involved in the colocation business and (ii) the impact of acquiring Level 3.

Based on information provided to us by Level 3, as of December 31, 2016, Level 3 had approximately \$9.0 billion of NOL carryforwards that we expect to acquire in connection with the Level 3 transaction. We cannot assure you that we will be able to use these NOL carryforwards fully, or at all. See "Risk Factors—Risk Relating to Our Pending Acquisition of Level 3—We cannot assure you, whether, when or in what amounts we will be able to use Level 3's net operating loss carryforwards following the Level 3 acquisition" in Item 1A of Part I of this annual report.

### *Dividends*

We currently expect to continue our current practice of paying quarterly cash dividends in respect of our common stock subject to our Board of Directors' discretion to modify or terminate this practice at any time and for any reason without prior notice. Our current quarterly common stock dividend rate is \$0.54 per share, as approved by our Board of Directors, which we believe is a dividend rate per share that gives us the flexibility to balance our multiple objectives of managing our business, paying our fixed commitments and returning cash to our shareholders. Assuming continued payment during 2017 at this rate of \$0.54 per share, our average total dividends paid each quarter prior to the Level 3 acquisition would be approximately \$294 million based on our current number of outstanding shares (which does not reflect shares that we expect to issue in connection with the Level 3 acquisition or any other shares that we might issue or repurchase in future periods). See "Risk Factors—Risks Affecting Our Business" in Item 1A of Part I of this annual report.

### *Credit Facility*

Our \$2 billion Credit Facility matures on December 3, 2019 and has 16 lenders, each with commitments ranging from \$3.5 million to \$198.5 million. The Credit Facility allows us to obtain revolving loans and to issue up to \$400 million of letters of credit, which upon issuance reduces the amount available for other extensions of credit. Interest is assessed on borrowings using either the LIBOR or the base rate (each as defined in the Credit Facility) plus an applicable margin between 1.00% and 2.25% per annum for LIBOR loans and 0.00% and 1.25% per annum for base rate loans depending on our then current senior unsecured long-term debt rating. Our obligations under the Credit Facility are guaranteed by nine of our subsidiaries. At December 31, 2016, we had \$370 million in borrowings and no amounts of letters of credit outstanding under the Credit Facility.

Under the Credit Facility, we, and our indirect subsidiary, Qwest Corporation, must maintain a debt to EBITDA (earnings before interest, taxes, depreciation and amortization, as defined in our Credit Facility) ratio of not more than 4.0:1.0 and 2.85:1.0, respectively, as of the last day of each fiscal quarter for the four quarters then ended. The Credit Facility also contains a negative pledge covenant, which generally requires us to secure equally and ratably any advances under the Credit Facility if we pledge assets or permit liens on our property for the benefit of other debtholders. The Credit Facility also has a cross payment default provision, and the Credit Facility and certain of our debt securities also have cross acceleration provisions. When present, these provisions could have a wider impact on liquidity than might otherwise arise from a default or acceleration of a single debt instrument. Our debt to EBITDA ratios could be adversely affected by a wide variety of events, including unforeseen expenses or contingencies. This could reduce our financing flexibility due to potential restrictions on incurring additional debt under certain provisions of our debt agreements or, in certain circumstances, could result in a default under certain provisions of such agreements.

#### *Term Loans and Revolving Letter of Credit*

At December 31, 2016, CenturyLink, Inc. owed \$336 million under a term loan maturing in 2019 and Qwest Corporation owed \$100 million under a term loan maturing in 2025. Both of these term loans include covenants substantially similar to those set forth in the Credit Facility.

We have a \$160 million uncommitted revolving letter of credit facility which enables us to provide letters of credit under terms that may be more favorable than those under the Credit Facility. At December 31, 2016, our outstanding letters of credit totaled \$105 million under this facility.

For information on our outstanding debt securities, see immediately below "Future Contractual Obligations" and Note 5—Long-Term Debt and Credit Facilities to our consolidated financial statements in Item 8 of Part II of this annual report.

#### *Level 3 Financing Commitment Letter*

In connection with entering into our merger agreement with Level 3, we obtained a debt commitment letter from a group of lenders. See Note 5—Long-Term Debt and Credit Facilities to our consolidated financial statements in Item 8 of Part II of this annual report, for additional information on the financing commitment letter.

### Future Contractual Obligations

The following table summarizes our estimated future contractual obligations as of December 31, 2016:

	2017	2018	2019	2020	2021	2022 and thereafter	Total
	(Dollars in millions)						
Long-term debt <sup>(1)(2)</sup>	\$ 1,544	280	1,131	1,032	2,329	14,003	20,319
Interest on long-term debt and capital leases <sup>(2)</sup>	1,202	1,164	1,137	1,069	893	15,434	20,899
Operating leases <sup>(3)</sup>	295	276	249	226	162	1,049	2,257
Purchase commitments <sup>(4)</sup>	166	109	44	26	15	67	427
Post-retirement benefit obligation <sup>(5)</sup>	97	94	90	87	83	775	1,226
Non-qualified pension obligations <sup>(5)</sup>	6	5	5	5	4	20	45
Unrecognized tax benefits <sup>(6)</sup>	—	—	—	—	—	51	51
Other	6	7	7	6	8	60	94
<b>Total future contractual obligations<sup>(7)</sup></b>	<b>\$ 3,316</b>	<b>1,935</b>	<b>2,663</b>	<b>2,451</b>	<b>3,494</b>	<b>31,459</b>	<b>45,318</b>

- (1) Includes current maturities and capital lease obligations, but excludes unamortized discounts, net and unamortized debt issuance costs. Also, includes \$305 million of capital lease obligations related to our colocation operations. See Note 16—Commitments and Contingencies to our consolidated financial statements in Item 8 of Part II of this annual report for additional information regarding the future commitments for capital leases related to our colocation operations.
- (2) Actual principal and interest paid in all years may differ due to future refinancing of outstanding debt or issuance of new debt. Interest on our floating rate debt was calculated for all years using the rates effective at December 31, 2016. Also, includes interest and executory costs of \$93 million associated with our capital lease obligations related to our colocation operations. See Note 16—Commitments and Contingencies to our consolidated financial statements in Item 8 of Part II of this annual report for additional information regarding the future commitments for capital leases related to our colocation operations.
- (3) Includes \$750 million of operating lease future rental commitments related to our colocation operations. See Note 16—Commitments and Contingencies to our consolidated financial statements in Item 8 of Part II of this annual report for additional information regarding the future commitments for operating leases related to our colocation operations.
- (4) We have various long-term, non-cancelable purchase commitments for advertising and promotion services, including advertising and marketing at sports arenas and other venues and events. We also have purchase commitments with third-party vendors for operating, installation and maintenance services for facilities. In addition, we have service-related commitments with various vendors for data processing, technical and software support services. Future payments under certain service contracts will vary depending on our actual usage. In the table above, we estimated payments for these service contracts based on estimates of the level of services we expect to receive. Includes \$80 million of purchase commitments related to our colocation operations. See Note 16—Commitments and Contingencies to our consolidated financial statements in Item 8 of Part II of this annual report for additional information regarding the purchase commitments related to our colocation operations.
- (5) Reflects only the portion of total obligation that is contractual in nature. See Note 7 below.
- (6) Represents the amount of tax and interest we would pay for our unrecognized tax benefits. The \$51 million is composed of unrecognized tax benefits of \$16 million and related estimated interest of \$35 million, which would result in future cash payments if our tax positions were not upheld. See Note 13—Income Taxes to our consolidated financial statements in Item 8 of Part II of this annual report for additional information. The timing of any payments for our unrecognized tax benefits cannot be predicted with certainty; therefore, such amount is reflected in the "2022 and thereafter" column in the above table.
- (7) The table is limited solely to contractual payment obligations and does not include
- contingent liabilities,
  - our open purchase orders as of December 31, 2016. These purchase orders are generally issued at fair value, and are generally cancelable without penalty,
  - other long-term liabilities, such as accruals for legal matters and other taxes that are not contractual obligations by nature. We cannot determine

with any degree of reliability the years in which these liabilities might ultimately settle,

- cash funding requirements for qualified pension benefits payable to certain eligible current and future retirees. Benefits paid by our qualified pension plan are paid through a trust. Cash funding requirements for this trust are not included in this table as we are not able to reliably estimate required contributions to this trust. Our funding projections are discussed further below.
- certain post-retirement benefits payable to certain eligible current and future retirees. Not all of our post-retirement benefit obligation amount is a contractual obligation and only the portion that we believe is a contractual obligation is reported in the table. See additional information on our benefits plans in Note 9—Employee Benefits to our consolidated financial statements in Item 8 of Part II of this annual report.

- contract termination fees. These fees are non-recurring payments, the timing and payment of which, if any, is uncertain. In the ordinary course of business and to optimize our cost structure, we enter into contracts with terms greater than one year to use the network facilities of other carriers and to purchase other goods and services. Our contracts to use other carriers' network facilities generally have no minimum volume requirements and pricing is based upon volumes and usage. Assuming we terminate these contracts in 2017, the contract termination fees would be \$359 million. Under the same assumption, we estimate that our termination fees for these contracts to purchase goods and services would be \$165 million. In the normal course of business, we do not believe payment of these fees is likely;
- service level commitments to our customers, the violation of which typically results in service credits rather than cash payments, and
- potential indemnification obligations to counterparties in certain agreements entered into in the normal course of business. The nature and terms of these arrangements vary.

For information on debt that we expect to assume or incur in connection with consummating the Level 3 acquisition, see "Risk Factors" in Item 1A of Part I of this annual report and Note 5—Long-Term Debt and Credit Facilities to our consolidated financial statements in Item 8 of Part II of this annual report.

### *Pension and Post-retirement Benefit Obligations*

We are subject to material obligations under our existing defined benefit pension plans and post-retirement benefit plans. At December 31, 2016, the accounting unfunded status of our qualified and non-qualified defined benefit pension plans and qualified post-retirement benefit plans was \$2.409 billion and \$3.360 billion, respectively. See Note 9—Employee Benefits to our consolidated financial statements in Item 8 of Part II of this annual report for additional information about our pension and post-retirement benefit arrangements.

Benefits paid by our qualified pension plan are paid through a trust that holds all of the plan's assets. Based on current laws and circumstances, we do not expect any contributions to be required for our qualified pension plan during 2017. The amount of required contributions to our qualified pension plan in 2018 and beyond will depend on a variety of factors, most of which are beyond our control, including earnings on plan investments, prevailing interest rates, demographic experience, changes in plan benefits and changes in funding laws and regulations. We occasionally make voluntary contributions to the trust in addition to required contributions, including voluntary contributions in the amount of \$100 million made in the third quarter of both 2016 and 2015. We currently expect to make a voluntary contribution of \$100 million to the trust in 2017.

Substantially all of our post-retirement health care and life insurance benefits plans are unfunded. Several trusts hold assets that have been used to help cover the health care costs of certain retirees. Assets in the post-retirement trusts have been substantially depleted as of December 31, 2016; however, we will continue to pay certain benefits through the trusts. The fair value of these trust assets was approximately \$53 million at December 31, 2016, with a portion comprised of investments with restricted liquidity. Benefits not paid through the trusts will be paid directly by us. As described further in Note 9—Employee Benefits to our consolidated financial statements in Item 8 of Part II of this annual report, aggregate benefits paid by us under these plans (net of participant contributions and direct subsidy receipts) were \$129 million, \$116 million and \$88 million for the years ended December 31, 2016, 2015 and 2014, respectively, while the amounts paid from the trust were \$145 million, \$163 million and \$219 million, respectively. For additional information on our expected future benefits payments for our post-retirement benefit plans, please see Note 9—Employee Benefits to our consolidated financial statements in Item 8 of Part II in this annual report.

For 2017, our estimated annual long-term rates of return are 6.5% and 5.0% for the pension plan trust assets and post-retirement plans' trust assets, respectively, based on the assets currently held. However, actual returns could be substantially different.

### Workforce Reductions

In response to the continued decline of our legacy services revenues and to better align our workforce with our workload requirements, we periodically implement workforce reduction programs. In the third quarter of 2016, we announced plans to reduce our workforce, initially through voluntary severance packages and the balance through involuntary reductions. We recognized in the fourth quarter of 2016 a charge for severance expenses and other one-time termination benefits of \$164 million, \$98 million of which remained to be paid as of December 31, 2016.

### Connect America Fund

In 2015, we accepted CAF funding from the FCC of approximately \$500 million per year for six years to fund the deployment of voice and broadband capable infrastructure for approximately 1.2 million rural households and businesses in 33 states under the CAF Phase 2 high-cost support program. The funding from the CAF Phase 2 support program has substantially replaced the funding from the interstate USF program that we previously utilized to support voice services in high-cost rural markets in these 33 states. In late 2015, we began receiving these monthly support payments from the FCC under the new CAF Phase 2 support program, which included (i) monthly support payments at a higher rate than under the interstate USF support program and (ii) a substantial one-time transitional payment, designed to align the prior USF payments with the new CAF Phase 2 payments for the full year 2015. For 2016, we continued to receive monthly support payments at the higher rate than under the interstate USF support program. We received \$214 million and \$209 million more cash from the CAF Phase 2 program for the years ended December 31, 2016 and 2015, respectively, than the projected amounts we would have otherwise received during the same periods under the interstate USF support program.

As a result of accepting CAF Phase 2 support payments for 33 states, we will be obligated to make substantial capital expenditures to build broadband infrastructure over the next several years. See "Capital Expenditures" above.

For additional information on the FCC's CAF order and the USF program, see "Business—Regulation" in Item 1 of Part I of this annual report and see "Risk Factors—Risks Affecting Our Liquidity and Capital Resources" in Item 1A of Part I of this annual report.

In 2013, under the CAF Phase 1 Round 2 program, we received \$40 million in funding for deployment of broadband services in rural areas. In compliance with program terms, during the second half of 2016 we returned \$23 million for failing to meet interim buildout milestones within the FCC specified time frames. As of December 31, 2016, we have included the remaining \$17 million of funding in deferred credits and other liabilities - other on our consolidated balance sheet. At the conclusion of the CAF 1 Round 2 program in the first quarter 2017, we will have an opportunity to reclaim a majority of the interim refund if we ultimately meet the CAF 1 Round 2 buildout targets.

### Historical Information

The following tables summarize our consolidated cash flow activities:

	Years Ended December 31,		Increase / (Decrease)
	2016	2015	
	(Dollars in millions)		
Net cash provided by operating activities	\$ 4,608	5,152	(544)
Net cash used in investing activities	(2,994)	(2,853)	141
Net cash used in financing activities	(1,518)	(2,301)	(783)

	Years Ended December 31,		Increase / (Decrease)
	2015	2014	
	(Dollars in millions)		
Net cash provided by operating activities	\$ 5,152	5,188	(36)
Net cash used in investing activities	(2,853)	(3,077)	(224)
Net cash used in financing activities	(2,301)	(2,151)	150

### Operating Activities

Net cash provided by operating activities decreased by \$544 million for the year ended December 31, 2016 as compared to the year ended December 31, 2015 primarily due to a significant negative variance in net income adjusted for non-cash items (attributable to higher cash taxes paid and lower profitability), which was partially offset by a positive variance in the change in accounts payable. Net cash provided by operating activities decreased by \$36 million for the year ended December 31, 2015 as compared to the year ended December 31, 2014 primarily due to a slight negative variance in net income adjusted for non-cash items along with negative variances in accounts payable and other noncurrent assets and liabilities, net. The decreases were substantially offset with positive variances in accrued income and other taxes and other current assets and liabilities, net, which was primarily due to a payment of approximately \$235 million in 2014 to settle certain litigation. Our net cash provided by operating activities in 2016 and 2015 were positively impacted by the cash received from the CAF Phase 2 support program, which was \$214 million and \$209 million greater in 2016 and 2015, respectively, than the projected amounts of cash we would have otherwise received during the same periods under the interstate USF support program. For additional information about our operating results, see "Results of Operations" above.

### Investing Activities

Net cash used in investing activities increased by \$141 million for the year ended December 31, 2016 as compared to the year ended December 31, 2015 substantially due to an increase in payments for property, plant and equipment. Net cash used in investing activities decreased by \$224 million for the year ended December 31, 2015 as compared to the year ended December 31, 2014 primarily due to a decrease in payments of property, plant and equipment and amounts paid for acquisitions in 2015.

### Financing Activities

Net cash used in financing activities decreased by \$783 million for the year ended December 31, 2016 as compared to the year ended December 31, 2015 primarily due to a reduction of common stock repurchases. Net cash used in financing activities increased by \$150 million for the year ended December 31, 2015 as compared to the year ended December 31, 2014 primarily due to additional common stock repurchases. Net debt repayments have been about the same for all three years.

On December 23, 2016, a subsidiary of Embarq Corporation redeemed \$5 million of its 8.375% Notes due 2025, which resulted in an immaterial loss.

On September 19, 2016, a subsidiary of Embarq Corporation redeemed all of its 8.77% Notes due 2017, which was less than \$4 million and resulted in an immaterial loss.

On September 15, 2016, Qwest Corporation redeemed \$287 million of its 7.5% Notes due 2051, which resulted in a loss of \$9 million.

On August 29, 2016, Qwest Corporation redeemed all \$661 million of its 7.375% Notes due 2051, which resulted in a loss of \$18 million.

On August 22, 2016, Qwest Corporation issued \$978 million aggregate principal amount of 6.5% Notes due 2056, including \$128 million principal amount that was sold pursuant to an over-allotment option, in exchange for net proceeds, after deducting underwriting discounts and other expenses, of \$946 million.

On June 1, 2016, Embarq Corporation paid at maturity the \$1.184 billion principal amount and accrued and unpaid interest due under its 7.082% Notes.

On May 2, 2016, Qwest Corporation paid at maturity the \$235 million principal amount and accrued and unpaid interest due under its 8.375% Notes.

On April 6, 2016, CenturyLink, Inc. issued \$1 billion aggregate principal amount of 7.5% Notes due 2024, in exchange for net proceeds, after deducting underwriting discounts and other expenses, of \$988 million.

On January 29, 2016, Qwest Corporation issued \$235 million aggregate principal amount of 7% Notes due 2056, in exchange for net proceeds, after deducting underwriting discounts and other expenses, of \$227 million.

See Note 5—Long-Term Debt and Credit Facilities to our consolidated financial statements in Item 8 of Part II of this annual report, for additional information on our outstanding debt securities.

### **Other Matters**

In February 2015, the FCC adopted new regulations that regulate broadband services as a public utility service under Title II of the Communications Act. In light of pending litigation and changes in the composition of the FCC, we believe it is premature for us to determine the ultimate impact of the new regulations on our operations. For additional information, see "Risk Factors—Risks Relating to Legal and Regulatory Matters" in Item 1A of Part I of this annual report.

We have cash management arrangements with certain of our principal subsidiaries, in which substantial portions of the subsidiaries' cash is regularly advanced to us. Although we periodically repay these advances to fund the subsidiaries' cash requirements throughout the year, at any given point in time we may owe a substantial sum to our subsidiaries under these advances, which, in accordance with generally accepted accounting principles, are eliminated in consolidation and therefore not recognized on our consolidated balance sheets.

We also are involved in various legal proceedings that could substantially impact our financial position. See Note 16—Commitments and Contingencies to our consolidated financial statements in Item 8 of Part II of this annual report for the current status of such legal proceedings.

### **Market Risk**

We are exposed to market risk from changes in interest rates on our variable rate long-term debt obligations and fluctuations in certain foreign currencies. We seek to maintain a favorable mix of fixed and variable rate debt in an effort to limit interest costs and cash flow volatility resulting from changes in rates.

Management periodically reviews our exposure to interest rate fluctuations and periodically implements strategies to manage the exposure. From time to time, we have used derivative instruments to (i) lock-in or swap our exposure to changing or variable interest rates for fixed interest rates or (ii) to swap obligations to pay fixed interest rates for variable interest rates. As of December 31, 2016, we had no such instruments outstanding. We have established policies and procedures for risk assessment and the approval, reporting and monitoring of derivative instrument activities. We do not hold or issue derivative financial instruments for trading or speculative purposes.

At December 31, 2016, we had approximately \$19.6 billion (excluding capital lease and other obligations with a carrying amount of \$440 million) of long-term debt outstanding, approximately 96% of which bears interest at fixed rates and is therefore not exposed to interest rate risk. At December 31, 2016, we had \$806 million floating rate debt exposed to changes in either the London InterBank Offered Rate (LIBOR) or the Prime Rate. A hypothetical increase of 100 basis points in LIBOR relative to this debt would decrease our annual pre-tax earnings by \$8 million.

By operating internationally, we are exposed to the risk of fluctuations in the foreign currencies used by our international subsidiaries, primarily the British Pound, and secondarily the Canadian Dollar, the Japanese Yen, the Hong Kong Dollar and the Singapore Dollar. Although the percentages of our consolidated revenues and costs that are denominated in these currencies are immaterial, future volatility in exchange rates and an increase in the number of transactions could adversely impact our consolidated results of operations. We use a sensitivity analysis to estimate our exposure to this foreign currency risk, measuring the change in financial position arising from a hypothetical 10% change in the exchange rates of these currencies, relative to the U.S. Dollar, with all other variables held constant. The aggregate potential change in the fair value of financial assets resulting from a hypothetical 10% change in these exchange rates was \$18 million at December 31, 2016.

Certain shortcomings are inherent in the method of analysis presented in the computation of exposures to market risks. Actual values may differ materially from those disclosed by us from time to time if market conditions vary from the assumptions used in the analyses performed. These analyses only incorporate the risk exposures that existed at December 31, 2016.

### **Off-Balance Sheet Arrangements**

We have no special purpose or limited purpose entities that provide off-balance sheet financing, liquidity, or market or credit risk support and we do not engage in leasing, hedging or other similar activities that expose us to any significant liabilities that are not (i) reflected on the face of the consolidated financial statements, (ii) disclosed in Note 16—Commitments and Contingencies to our consolidated financial statements in Item 8 of Part II of this annual report, or in the Future Contractual Obligations table included in this Item 7 of Part II above, or (iii) discussed under the heading "Market Risk" above.

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The information in "Management's Discussion and Analysis of Financial Condition and Results of Operations—Market Risk" in Item 7 of Part II of this annual report is incorporated herein by reference.

**ITEM 8. CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA****Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
CenturyLink, Inc.:

We have audited the accompanying consolidated balance sheets of CenturyLink, Inc. and subsidiaries (the Company) as of December 31, 2016 and 2015, and the related consolidated statements of operations, comprehensive income (loss), cash flows, and stockholders' equity for each of the years in the three-year period ended December 31, 2016. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), CenturyLink, Inc.'s internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 22, 2017 expressed an unqualified opinion on the effectiveness of CenturyLink, Inc.'s internal control over financial reporting.

/s/ KPMG LLP

Shreveport, Louisiana  
February 22, 2017

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
CenturyLink, Inc.:

We have audited CenturyLink, Inc.'s (the Company) internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting (Item 9A). Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of CenturyLink, Inc. and subsidiaries as of December 31, 2016 and 2015, and the related consolidated statements of operations, comprehensive income (loss), cash flows, and stockholders' equity for each of the years in the three-year period ended December 31, 2016, and our report dated February 22, 2017 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP

Shreveport, Louisiana  
February 22, 2017

## CENTURYLINK, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions, except per share amounts and shares in thousands)		
OPERATING REVENUES	\$ 17,470	17,900	18,031
OPERATING EXPENSES			
Cost of services and products (exclusive of depreciation and amortization)	7,774	7,778	7,846
Selling, general and administrative	3,449	3,328	3,347
Depreciation and amortization	3,916	4,189	4,428
Total operating expenses	15,139	15,295	15,621
OPERATING INCOME	2,331	2,605	2,410
OTHER (EXPENSE) INCOME			
Interest expense	(1,318)	(1,312)	(1,311)
Other income, net	7	23	11
Total other expense, net	(1,311)	(1,289)	(1,300)
INCOME BEFORE INCOME TAX EXPENSE	1,020	1,316	1,110
Income tax expense	394	438	338
NET INCOME	\$ 626	878	772
BASIC AND DILUTED EARNINGS PER COMMON SHARE			
BASIC	\$ 1.16	1.58	1.36
DILUTED	\$ 1.16	1.58	1.36
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING			
BASIC	539,549	554,278	568,455
DILUTED	540,679	555,093	569,739

See accompanying notes to consolidated financial statements.

## CENTURYLINK, INC.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
NET INCOME	\$ 626	878	772
OTHER COMPREHENSIVE (LOSS) INCOME:			
Items related to employee benefit plans:			
Change in net actuarial (loss) gain, net of \$113, \$(12) and \$742 tax	(168)	21	(1,200)
Change in net prior service credit (costs), net of \$(4), \$(47) and \$1 tax	6	76	(1)
Foreign currency translation adjustment and other, net of \$—, \$— and \$1 tax	(21)	(14)	(14)
Other comprehensive (loss) income	(183)	83	(1,215)
COMPREHENSIVE INCOME (LOSS)	\$ 443	961	(443)

See accompanying notes to consolidated financial statements.

## CENTURYLINK, INC.

## CONSOLIDATED BALANCE SHEETS

	As of December 31,	
	2016	2015
	(Dollars in millions and shares in thousands)	
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 222	126
Accounts receivable, less allowance of \$178 and \$152	2,017	1,943
Assets held for sale	2,376	8
Other	547	573
Total current assets	<u>5,162</u>	<u>2,650</u>
<b>NET PROPERTY, PLANT AND EQUIPMENT</b>		
Property, plant and equipment	39,194	38,785
Accumulated depreciation	(22,155)	(20,716)
Net property, plant and equipment	<u>17,039</u>	<u>18,069</u>
<b>GOODWILL AND OTHER ASSETS</b>		
Goodwill	19,650	20,742
Customer relationships, net	2,797	3,928
Other intangible assets, net	1,531	1,555
Other, net	838	660
Total goodwill and other assets	<u>24,816</u>	<u>26,885</u>
<b>TOTAL ASSETS</b>	<u>\$ 47,017</u>	<u>47,604</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Current maturities of long-term debt	\$ 1,503	1,503
Accounts payable	1,179	968
Accrued expenses and other liabilities		
Salaries and benefits	802	602
Income and other taxes	301	318
Interest	260	250
Other	213	220
Current liabilities associated with assets held for sale	419	—
Advance billings and customer deposits	672	743
Total current liabilities	<u>5,349</u>	<u>4,604</u>
<b>LONG-TERM DEBT</b>	<u>18,185</u>	<u>18,722</u>
<b>DEFERRED CREDITS AND OTHER LIABILITIES</b>		
Deferred income taxes, net	3,471	3,569
Benefit plan obligations, net	5,527	5,511
Other	1,086	1,138
Total deferred credits and other liabilities	<u>10,084</u>	<u>10,218</u>
<b>COMMITMENTS AND CONTINGENCIES (Note 16)</b>		
<b>STOCKHOLDERS' EQUITY</b>		
Preferred stock — non-redeemable, \$25.00 par value, authorized 2,000 shares, issued and	—	—

outstanding 7 and 7 shares		
Common stock, \$1.00 par value, authorized 1,600,000 and 1,600,000 shares, issued and outstanding 546,545 and 543,800 shares	547	544
Additional paid-in capital	14,970	15,178
Accumulated other comprehensive loss	(2,117)	(1,934)
(Accumulated deficit) retained earnings	(1)	272
Total stockholders' equity	<u>13,399</u>	<u>14,060</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$ 47,017</u>	<u>47,604</u>

See accompanying notes to consolidated financial statements.

## CENTURYLINK, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
<b>OPERATING ACTIVITIES</b>			
Net income	\$ 626	878	772
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	3,916	4,189	4,428
Impairment of assets	13	9	32
Deferred income taxes	6	350	291
Provision for uncollectible accounts	192	177	159
Net long-term debt issuance costs and premium amortization	2	(3)	(21)
Net loss on early retirement of debt	27	—	—
Share-based compensation	80	73	79
Changes in current assets and liabilities:			
Accounts receivable	(266)	(132)	(163)
Accounts payable	109	(168)	70
Accrued income and other taxes	(43)	32	(84)
Other current assets and liabilities, net	92	(53)	(270)
Retirement benefits	(152)	(141)	(184)
Changes in other noncurrent assets and liabilities, net	(18)	(78)	99
Other, net	24	19	(20)
Net cash provided by operating activities	4,608	5,152	5,188
<b>INVESTING ACTIVITIES</b>			
Payments for property, plant and equipment and capitalized software	(2,981)	(2,872)	(3,047)
Cash paid for acquisitions	(39)	(4)	(93)
Proceeds from sale of property and intangible assets	30	31	63
Other, net	(4)	(8)	—
Net cash used in investing activities	(2,994)	(2,853)	(3,077)
<b>FINANCING ACTIVITIES</b>			
Net proceeds from issuance of long-term debt	2,161	989	483
Payments of long-term debt	(2,462)	(966)	(800)
Net payments on credit facility and revolving line of credit	(40)	(315)	(4)
Early retirement of debt costs	—	(1)	—
Dividends paid	(1,167)	(1,198)	(1,228)
Proceeds from issuance of common stock	6	11	50
Repurchase of common stock and shares withheld to satisfy tax withholdings	(16)	(819)	(650)
Other, net	—	(2)	(2)
Net cash used in financing activities	(1,518)	(2,301)	(2,151)
Net increase (decrease) in cash and cash equivalents	96	(2)	(40)
Cash and cash equivalents at beginning of period	126	128	168
Cash and cash equivalents at end of period	\$ 222	126	128
Supplemental cash flow information:			

Income taxes paid, net	\$	(397)	(63)	(27)
Interest paid (net of capitalized interest of \$54, \$52 and \$47)	\$	(1,301)	(1,310)	(1,338)

See accompanying notes to consolidated financial statements.

## CENTURYLINK, INC.

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
<b>COMMON STOCK</b> (represents dollars and shares)			
Balance at beginning of period	\$ 544	569	584
Issuance of common stock through dividend reinvestment, incentive and benefit plans	3	2	4
Repurchase of common stock	—	(27)	(19)
Balance at end of period	547	544	569
<b>ADDITIONAL PAID-IN CAPITAL</b>			
Balance at beginning of period	15,178	16,324	17,343
Issuance of common stock through dividend reinvestment, incentive and benefit plans	7	9	46
Repurchase of common stock	—	(767)	(591)
Shares withheld to satisfy tax withholdings	(15)	(19)	(16)
Share-based compensation and other, net	79	77	82
Dividends declared	(279)	(446)	(540)
Balance at end of period	14,970	15,178	16,324
<b>ACCUMULATED OTHER COMPREHENSIVE LOSS</b>			
Balance at beginning of period	(1,934)	(2,017)	(802)
Other comprehensive (loss) income	(183)	83	(1,215)
Balance at end of period	(2,117)	(1,934)	(2,017)
<b>(ACCUMULATED DEFICIT) RETAINED EARNINGS</b>			
Balance at beginning of period	272	147	66
Net income	626	878	772
Dividends declared	(899)	(753)	(691)
Balance at end of period	(1)	272	147
<b>TOTAL STOCKHOLDERS' EQUITY</b>	<b>\$ 13,399</b>	<b>14,060</b>	<b>15,023</b>

See accompanying notes to consolidated financial statements.

## CENTURYLINK, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

*References in the Notes to "CenturyLink," "we," "us" and "our" refer to CenturyLink, Inc. and its consolidated subsidiaries, unless the content otherwise requires and except in Note 5, where such references refer solely to CenturyLink, Inc.*

**(1) Background and Summary of Significant Accounting Policies****General**

We are an integrated communications company engaged primarily in providing an array of services to our residential and business customers. Our communications services include local and long-distance voice, broadband, Multi-Protocol Label Switching ("MPLS"), private line (including special access), Ethernet, colocation, hosting (including cloud hosting and managed hosting), data integration, video, network, public access, Voice over Internet Protocol ("VoIP"), information technology and other ancillary services.

On October 31, 2016, we entered into a definitive merger agreement under which we agreed to acquire Level 3 Communications, Inc. ("Level 3") in a cash and stock transaction. See Note 2—Pending Acquisition of Level 3 for additional information. On November 3, 2016, we entered into a definitive stock purchase agreement with a consortium led by BC Partners, Inc. and Medina Capital under which we propose to sell our data centers and colocation business for a combination of cash and equity. See Note 3—Pending Sale of Colocation Business and Data Centers for additional information.

**Basis of Presentation**

The accompanying consolidated financial statements include our accounts and the accounts of our subsidiaries. Intercompany amounts and transactions with our consolidated subsidiaries have been eliminated.

To simplify the overall presentation of our consolidated financial statements, we report immaterial amounts attributable to noncontrolling interests in certain of our subsidiaries as follows: (i) income attributable to noncontrolling interests in other income, net, (ii) equity attributable to noncontrolling interests in additional paid-in capital and (iii) cash flows attributable to noncontrolling interests in other, net financing activities.

We reclassified certain prior period amounts to conform to the current period presentation, including the categorization of our revenues and our segment reporting. See Note 14—Segment Information for additional information. These changes had no impact on total operating revenues, total operating expenses or net income for any period presented.

**Connect America Fund**

In 2015, we accepted Connect America Fund ("CAF") funding from the Federal Communications Commission ("FCC") of approximately \$500 million per year for six years to fund the deployment of voice and broadband capable infrastructure for approximately 1.2 million rural households and businesses in 33 states under the CAF Phase 2 high-cost support program. The funding from the CAF Phase 2 support program has substantially replaced the funding from the interstate Universal Service Fund ("USF") program that we previously utilized to support voice services in high-cost rural markets in these 33 states. In late 2015, we began receiving these monthly support payments from the FCC under the new CAF Phase 2 support program, which included (i) monthly support payments at a higher rate than under the interstate USF support program and (ii) a substantial one-time transitional payment, designed to align the prior USF payments with the new CAF Phase 2 payments for the full year 2015. For 2016, we continued to receive the monthly support payments at the higher rate than under the interstate USF support program. We recorded \$201 million and \$215 million more revenue from the CAF Phase 2 program for the years ended December 31, 2016 and 2015, respectively, than the projected amounts we would have otherwise recorded during the same periods under the interstate USF support program.

## Changes in Estimates

In 2016, we changed the method we use to estimate the service and interest components of net periodic benefit expense for pension and other postretirement benefit obligations. This change resulted in a decrease in the service and interest components in 2016. Beginning in 2016, we utilized a full yield curve approach in connection with estimating these components by applying the specific spot rates along the yield curve used in the determination of the benefit obligation to the relevant projected cash flows, as opposed to the single weighted-average discount rate derived from the yield curve that we have used in the past. We believe this change more precisely measures service and interest costs by improving the correlation between projected benefit cash flows to the corresponding spot yield curve rates. This change did not affect the measurement of our total benefit obligations but lowered our annual net periodic benefit cost by approximately \$149 million in 2016. This change was treated as a change in accounting estimate and accordingly, we did not adjust the amounts recorded in 2015 or 2014. The reduction in expense described above, net of tax, increased net income by \$91 million, or \$0.17 per basic and diluted common share, for the year ended December 31, 2016.

## Summary of Significant Accounting Policies

### Use of Estimates

Our consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles. These accounting principles require us to make certain estimates, judgments and assumptions. We believe that the estimates, judgments and assumptions we make when accounting for specific items and matters, including, but not limited to, investments, long-term contracts, customer retention patterns, allowance for doubtful accounts, depreciation, amortization, asset valuations, internal labor capitalization rates, recoverability of assets (including deferred tax assets), impairment assessments, pension, post-retirement and other post-employment benefits, taxes, certain liabilities and other provisions and contingencies, are reasonable, based on information available at the time they are made. These estimates, judgments and assumptions can materially affect the reported amounts of assets, liabilities and components of stockholders' equity as of the dates of the consolidated balance sheets, as well as the reported amounts of revenues, expenses and components of cash flows during the periods presented in our other consolidated financial statements. We also make estimates in our assessments of potential losses in relation to threatened or pending tax and legal matters. See Note 13—Income Taxes and Note 16—Commitments and Contingencies for additional information.

For matters not related to income taxes, if a loss is considered probable and the amount can be reasonably estimated, we recognize an expense for the estimated loss. If we have the potential to recover a portion of the estimated loss from a third party, we make a separate assessment of recoverability and reduce the estimated loss if recovery is also deemed probable.

For matters related to income taxes, if we determine that the impact of an uncertain tax position is more likely than not to be sustained upon audit by the relevant taxing authority, then we recognize a benefit for the largest amount that is more likely than not to be sustained. No portion of an uncertain tax position will be recognized if the position has less than a 50% likelihood of being sustained. Interest is recognized on the amount of unrecognized benefit from uncertain tax positions.

For all of these and other matters, actual results could differ materially from our estimates.

### Revenue Recognition

We recognize revenue for services when the related services are provided. Recognition of certain payments received in advance of services being provided is deferred until the service is provided. These advance payments include activation and installation charges, which we recognize as revenue over the expected customer relationship period, which ranges from three years to over seven years depending on the service. We also defer costs for customer activations and installations. The deferral of customer activation and installation costs is limited to the amount of revenue deferred on advance payments. Costs in excess of advance payments are recorded as expense in the period such costs are incurred. Expected customer relationship periods are estimated using historical experience. In most cases, termination fees or other fees on existing contracts that are negotiated in conjunction with new contracts are deferred and recognized over the new contract term.

We offer bundle discounts to our customers who receive certain groupings of services. These bundle discounts are recognized concurrently with the associated revenue and are allocated to the various services in the bundled offering based on the estimated selling price of services included in each bundled combination.



Customer arrangements that include both equipment and services are evaluated to determine whether the elements are separable. If the elements are deemed separable and separate earnings processes exist, the revenue associated with the customer arrangement is allocated to each element based on the relative estimated selling price of the separate elements. We have estimated the selling prices of each element by reference to vendor-specific objective evidence of selling prices when the elements are sold separately. The revenue associated with each element is then recognized as earned. For example, if we receive an advance payment when we sell equipment and continuing service together, we immediately recognize as revenue the amount allocated to the equipment as long as all the conditions for revenue recognition have been satisfied. The portion of the advance payment allocated to the service based upon its relative selling price is recognized ratably over the longer of the contractual period or the expected customer relationship period.

We periodically transfer optical capacity assets on our network to other telecommunications service carriers. These transactions are structured as indefeasible rights of use, commonly referred to as IRUs, which are the exclusive right to use a specified amount of capacity or fiber for a specified term, typically 20 years. We account for the cash consideration received on transfers of optical capacity assets and on all of the other elements deliverable under an IRU, as revenue ratably over the term of the agreement. We do not recognize revenue on any contemporaneous exchanges of our optical capacity assets for other optical capacity assets.

In connection with offering products and services provided by third-party vendors, we review the relationship between us, the vendor and the end customer to assess whether revenue should be reported on a gross or net basis. In assessing whether revenue should be reported on a gross or net basis, we consider whether we act as a principal in the transaction, take title to the products, have risk and rewards of ownership or act as an agent or broker. Based on our agreements with DIRECTV and Verizon Wireless, we offer these services through sales agency relationships which are reported on a net basis.

We have service level commitments pursuant to contracts with certain of our customers. To the extent that such service levels are not achieved or are otherwise disputed due to performance or service issues or other service interruptions or conditions, we will estimate the amount of credits to be issued and record a reduction to revenues, with a corresponding increase in the credit reserve.

#### **USF Surcharges, Gross Receipts Taxes and Other Surcharges**

In determining whether to include in our revenues and expenses the taxes and surcharges collected from customers and remitted to government authorities, including USF surcharges, sales, use, value added and some excise taxes, we assess, among other things, whether we are the primary obligor or principal taxpayer for the taxes assessed in each jurisdiction where we do business. In jurisdictions where we determine that we are the principal taxpayer, we record the surcharges on a gross basis and include them in our revenues and costs of services and products. In jurisdictions where we determine that we are merely a collection agent for the government authority, we record the taxes on a net basis and do not include them in our revenues and costs of services and products.

#### **Advertising Costs**

Costs related to advertising are expensed as incurred and included in selling, general and administrative expenses in our consolidated statements of operations. Our advertising expense was \$216 million, \$210 million and \$214 million for the years ended December 31, 2016, 2015 and 2014, respectively.

#### **Legal Costs**

In the normal course of our business, we incur costs to hire and retain external legal counsel to advise us on regulatory, litigation and other matters. We expense these costs as the related services are received.

#### **Income Taxes**

We file a consolidated federal income tax return with our eligible subsidiaries. The provision for income taxes consists of an amount for taxes currently payable, an amount for tax consequences deferred to future periods and adjustments to our liabilities for uncertain tax positions. We record deferred income tax assets and liabilities reflecting future tax consequences attributable to tax net operating loss carryforwards ("NOLs"), tax credit carryforwards and differences between the financial statement carrying value of assets and liabilities and the tax bases of those assets and liabilities. Deferred taxes are computed using enacted tax rates expected to apply in the year in which the differences are expected to affect taxable income. The effect on deferred income tax assets and liabilities of a change in tax rate is recognized in earnings in the period that includes the enactment date.

We establish valuation allowances when necessary to reduce deferred income tax assets to the amounts that we believe are more likely than not to be recovered. Each quarter we evaluate the need to retain all or a portion of the valuation allowance on our deferred tax assets. See Note 13—Income Taxes for additional information.

### **Cash and Cash Equivalents**

Cash and cash equivalents include highly liquid investments that are readily convertible into cash and are not subject to significant risk from fluctuations in interest rates. As a result, the value at which cash and cash equivalents are reported in our consolidated financial statements approximates their fair value. In evaluating investments for classification as cash equivalents, we require that individual securities have original maturities of ninety days or less and that individual investment funds have dollar-weighted average maturities of ninety days or less. To preserve capital and maintain liquidity, we invest with financial institutions we deem to be of sound financial condition and in high quality and relatively risk-free investment products. Our cash investment policy limits the concentration of investments with specific financial institutions or among certain products and includes criteria related to credit worthiness of any particular financial institution.

Book overdrafts occur when checks have been issued but have not been presented to our controlled disbursement bank accounts for payment. Disbursement bank accounts allow us to delay funding of issued checks until the checks are presented for payment. Until the issued checks are presented for payment, the book overdrafts are included in accounts payable on our consolidated balance sheet. This activity is included in the operating activities section in our consolidated statements of cash flows.

### **Accounts Receivable and Allowance for Doubtful Accounts**

Accounts receivable are recognized based upon the amount due from customers for the services provided or at cost for purchased and other receivables less an allowance for doubtful accounts. The allowance for doubtful accounts receivable reflects our best estimate of probable losses inherent in our receivable portfolio determined on the basis of historical experience, specific allowances for known troubled accounts and other currently available evidence. We generally consider our accounts past due if they are outstanding over 30 days. Our collection process varies by the customer segment, amount of the receivable, and our evaluation of the customer's credit risk. Our past due accounts are written off against our allowance for doubtful accounts when collection is considered to be not probable. Any recoveries of accounts previously written off are generally recognized as a reduction in bad debt expense in the period received. The carrying value of accounts receivable net of the allowance for doubtful accounts approximates fair value.

### **Property, Plant and Equipment**

We record property, plant and equipment acquired in connection with our acquisitions based on its estimated fair value as of its acquisition date plus the estimated value of any associated legally or contractually required retirement obligations. We record purchased and constructed property, plant and equipment at cost, plus the estimated value of any associated legally or contractually required retirement obligations. Property, plant and equipment is depreciated primarily using the straight-line group method. Under the straight-line group method, assets dedicated to providing telecommunications services (which comprise the majority of our property, plant and equipment) that have similar physical characteristics, use and expected useful lives are pooled for purposes of depreciation and tracking. The equal life group procedure is used to establish each pool's average remaining useful life. Generally, under the straight-line group method, when an asset is sold or retired in the course of normal business activities, the cost is deducted from property, plant and equipment and charged to accumulated depreciation without recognition of a gain or loss. A gain or loss is recognized in our consolidated statements of operations only if a disposal is unusual. Leasehold improvements are amortized over the shorter of the useful lives of the assets or the expected lease term. Expenditures for maintenance and repairs are expensed as incurred. Interest is capitalized during the construction phase of network and other internal-use capital projects. Employee-related costs for construction of network and other internal use assets are also capitalized during the construction phase. Property, plant and equipment supplies used internally are carried at average cost, except for significant individual items for which cost is based on specific identification.

We perform annual internal reviews to evaluate the reasonableness of the depreciable lives for our property, plant and equipment. Our reviews utilize models that take into account actual usage, physical wear and tear, replacement history, assumptions about technology evolution and, in certain instances, actuarially determined probabilities to estimate the remaining useful life of our asset base. Our remaining useful life assessments anticipate the loss in service value of assets that may precede the physical retirement. Assets shared among many customers may lose service value as those customers leave the network. However, the asset is not retired until all customers no longer utilize the asset and we determine there is no alternative use for the asset.

We have asset retirement obligations associated with the legally or contractually required removal of a limited group of property, plant and equipment assets from leased properties and the disposal of certain hazardous materials present in our owned properties. When an asset retirement obligation is identified, usually in association with the acquisition of the asset, we record the fair value of the obligation as a liability. The fair value of the obligation is also capitalized as property, plant and equipment and then amortized over the

estimated remaining useful life of the associated asset. Where the removal obligation is not legally binding, the net cost to remove assets is expensed in the period in which the costs are actually incurred.

We review long-lived tangible assets for impairment whenever facts and circumstances indicate that the carrying amounts of the assets may not be recoverable. For assessment purposes, long-lived assets are grouped with other assets and liabilities at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities, absent a material change in operations. An impairment loss is recognized only if the carrying amount of the asset group is not recoverable and exceeds its fair value. Recoverability of the asset group to be held and used is assessed by comparing the carrying amount of the asset group to the estimated undiscounted future net cash flows expected to be generated by the asset group. If the asset group's carrying value is not recoverable, an impairment charge is recognized for the amount by which the carrying amount of the asset group exceeds its fair value. We determine fair values by using a combination of comparable market values and discounted cash flows, as appropriate.

### **Goodwill, Customer Relationships and Other Intangible Assets**

Intangible assets arising from business combinations, such as goodwill, customer relationships, capitalized software, trademarks and trade names, are initially recorded at estimated fair value. We amortize customer relationships primarily over an estimated life of 10 to 15 years, using either the sum-of-the-years-digits or the straight-line methods, depending on the type of customer. We amortize capitalized software using the straight-line method over estimated lives ranging up to 7 years, except for approximately \$237 million of our capitalized software costs, which represents costs to develop an integrated billing and customer care system which is amortized using the straight-line method over a 20 year period. We amortize our other intangible assets predominantly using the sum-of-the-years-digits method over an estimated life of 4 to 20 years. Other intangible assets not arising from business combinations are initially recorded at cost. Where there are no legal, regulatory, contractual or other factors that would reasonably limit the useful life of an intangible asset, we classify the intangible asset as indefinite-lived and such intangible assets are not amortized.

Internally used software, whether purchased or developed by us, is capitalized and amortized using the straight-line method over its estimated useful life. We have capitalized certain costs associated with software such as costs of employees devoting time to the projects and external direct costs for materials and services. Costs associated with software to be used for internal purposes are expensed until the point at which the project has reached the development stage. Subsequent additions, modifications or upgrades to internal-use software are capitalized only to the extent that they allow the software to perform a task it previously did not perform. Software maintenance, data conversion and training costs are expensed in the period in which they are incurred. We review the remaining economic lives of our capitalized software annually. Capitalized software is included in other intangible assets, net, in our consolidated balance sheets.

Our long-lived intangible assets, other than goodwill, with indefinite lives are assessed for impairment annually, or, under certain circumstances, more frequently, such as when events or changes in circumstances indicate there may be an impairment. These assets are carried at the estimated fair value at the time of acquisition and assets not acquired in acquisitions are recorded at historical cost. However, if their estimated fair value is less than the carrying amount, other indefinite-lived intangible assets are reduced to their estimated fair value through an impairment charge to our consolidated statements of operations.

We are required to assess goodwill for impairment at least annually, or more frequently, if an event occurs or circumstances change that would indicate an impairment may have occurred. We are required to write-down the value of goodwill in periods in which the recorded amount of goodwill exceeds the implied fair value of goodwill. Our reporting units are not discrete legal entities with discrete financial statements. Therefore, the equity carrying value and future cash flows must be estimated each time a goodwill impairment assessment is performed on a reporting unit. As a result, our assets, liabilities and cash flows are assigned to reporting units using reasonable and consistent allocation methodologies. Certain estimates, judgments and assumptions are required to perform these assignments. We believe these estimates, judgments and assumptions to be reasonable, but changes in many of these can significantly affect each reporting unit's equity carrying value and future cash flows utilized for our goodwill impairment assessment.

We are required to reassign goodwill to reporting units each time we reorganize our internal reporting structure which causes a change in the composition of our reporting units. Goodwill is reassigned to the reporting units using a relative fair value approach. We utilize the earnings before interest, taxes, depreciation and amortization of each reporting unit as our allocation methodology as it represents a reasonable proxy for the fair value of the operations being reorganized.

See Note 4—Goodwill, Customer Relationships and Other Intangible Assets for additional information.

## **Pension and Post-Retirement Benefits**

We recognize the funded status of our defined benefit and post-retirement plans as an asset or a liability on our consolidated balance sheet. Each year's actuarial gains or losses are a component of our other comprehensive (loss) income, which is then included in our accumulated other comprehensive loss. Pension and post-retirement benefit expenses are recognized over the period in which the employee renders service and becomes eligible to receive benefits. We make significant assumptions (including the discount rate, expected rate of return on plan assets, mortality and health care trend rates) in computing the pension and post-retirement benefits expense and obligations. See Note 9—Employee Benefits for additional information.

## **Foreign Currency**

Our results of operations include foreign subsidiaries, which are translated from the applicable functional currency to the United States Dollar using the average exchange rates during the reporting period, while assets and liabilities are translated at the reporting date. We include gains or losses from foreign currency remeasurement in other income, net in our consolidated statements of operations. Certain non-U.S. subsidiaries designate the local currency as their functional currency, and we record the translation of their assets and liabilities into U.S. Dollars at the balance sheet date as translation adjustments and include them as a component of accumulated other comprehensive loss in our consolidated balance sheets.

## **Common Stock**

At December 31, 2016, we had 4 million unissued shares of CenturyLink, Inc. common stock reserved for acquisitions, substantially all of which are reserved for issuance in connection with our pending acquisition of Level 3. In addition, we had 21 million shares authorized for future issuance under our equity incentive plans.

## **Preferred stock**

Holders of outstanding CenturyLink, Inc. preferred stock are entitled to receive cumulative dividends, receive preferential distributions equal to \$25 per share plus unpaid dividends upon CenturyLink, Inc.'s liquidation and vote as a single class with the holders of common stock.

## **Dividends**

We pay dividends out of retained earnings to the extent we have retained earnings on the date the dividend is declared. If the dividend is in excess of our retained earnings on the declaration date, then the excess is drawn from our additional paid-in capital.

## **Recent Accounting Pronouncements**

### *Income Taxes*

On October 24, 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-16, "Intra-Entity Transfers of Assets Other Than Inventory" ("ASU 2016-16"). ASU 2016-16 eliminates the current prohibition on the recognition of the income tax effects on the transfer of assets among our subsidiaries. After adoption of this ASU, the income tax effects associated with these asset transfers, except for the transfer of inventory, will be recognized in the period the asset is transferred versus the current deferral and recognition upon either the sale of the asset to a third party or over the remaining useful life of the asset. We are currently reviewing the requirements of this ASU and evaluating the impact on our consolidated financial statements.

We are required to adopt the provisions of ASU 2016-16 on January 1, 2018, but have the option to early adopt as of January 1, 2017. We plan to adopt the provision of ASU 2016-16 on January 1, 2018. The impact of adopting ASU 2016-16, if any, will be recognized through a cumulative adjustment to retained earnings as of the date of adoption.

### *Financial Instruments*

On June 16, 2016, the FASB issued ASU 2016-13, "Measurement of Credit Losses on Financial Instruments" ("ASU 2016-13"). The primary impact of ASU 2016-13 for us is a change in the model for the recognition of credit losses related to our financial instruments from an incurred loss model, which recognized credit losses only if it was probable that a loss had been incurred, to an expected loss model, which requires our management team to estimate the total credit losses expected on the portfolio of financial

instruments. We are currently reviewing the requirements of the standard and evaluating the impact on our consolidated financial statements.

We are required to adopt the provisions of ASU 2016-13 effective January 1, 2020, but could elect to early adopt the provisions as of January 1, 2019. We expect to recognize any impacts of adopting ASU 2016-13 through a cumulative adjustment to retained earnings as of the date of adoption. As of the date of this annual report, we have not yet determined the date we will adopt ASU 2016-13.

#### *Share-based Compensation*

On March 30, 2016, the FASB issued ASU 2016-09, "Improvement to Employee Share-Based Payment Accounting" ("ASU 2016-09"). ASU 2016-09 modifies the accounting and associated income tax accounting for share-based compensation in order to reduce the cost and complexity associated with current generally accepted accounting principles. ASU 2016-09 became effective as of January 1, 2017. ASU 2016-09 includes different transition requirements for the different changes implemented, including some provisions which allow retrospective application. We will implement this new standard on its effective date.

The primary provisions of ASU 2016-09 that we expect will affect our financial statements are: (1) a reclassification of the tax effect associated with the difference between the expense recognized for share-based payments and the associated tax deduction from additional paid-in capital to income tax expense; (2) a reclassification of the tax effect associated with the difference between compensation expense and associated deduction from financing cash flow to operating cash flow; and (3) a change in our accounting policy to account for forfeitures of share-based payment grants as they occur as opposed to our current policy of estimating the forfeitures on the grant date. The adoption of this accounting policy change will result in an immaterial increase in our retained earnings as of January 1, 2017. Although the provisions would not have had a material impact on our previously-issued financial statements, we cannot provide any assurance regarding their future impacts. Adoption of ASU 2016-09 may increase the volatility of income tax expense and cash flow from operating activities.

#### *Leases*

On February 25, 2016, the FASB issued ASU 2016-02, "Leases" ("ASU 2016-02"). The core principle of ASU 2016-02 will require lessees to present right-of-use assets and lease liabilities on their balance sheets for operating leases, which are currently not reflected on their balance sheets.

ASU 2016-02 is effective for annual and interim periods beginning January 1, 2019. Early adoption of ASU 2016-02 is permitted. Upon adoption of ASU 2016-02, we are required to recognize and measure leases at the beginning of the earliest period presented in our consolidated financial statements using a modified retrospective approach. The modified retrospective approach includes a number of optional practical expedients that we may elect to apply. We will implement this new standard on its effective date, but we have not yet decided which practical expedient options we will elect.

We are currently evaluating our existing lease accounting systems to determine whether our current systems will support the new accounting requirements or if upgrades or new systems will be required, and we are in the process of developing an implementation plan. We are also currently evaluating and assessing the impact ASU 2016-02 will have on us and our consolidated financial statements. As of the date of this annual report, we cannot provide any estimate of the impact of adopting ASU 2016-02.

#### *Revenue Recognition*

On May 28, 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09"). ASU 2014-09 replaces virtually all existing generally accepted accounting principles ("GAAP") on revenue recognition and replaces them with a principles-based approach for determining revenue recognition using a new five step model. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 also includes new accounting principles related to the deferral and amortization of contract acquisition and fulfillment costs. We currently do not defer any contract acquisition costs, but we expect we will defer certain contract acquisition costs in the future which could have the impact of lowering our operating expenses. We currently defer contract fulfillment costs only up to the extent of any revenue deferred. Under ASU 2014-09, in certain transactions our deferred contract fulfillment costs could exceed our deferred revenues, which could result in an increase in deferred costs and could also have the impact of lowering our operating expenses.

On July 9, 2015, the FASB approved the deferral of the effective date of ASU 2014-09 by one year until January 1, 2018, which is the date we plan to adopt this standard. ASU 2014-09 may be adopted by applying the provisions of this standard on a retrospective basis to the periods included in the financial statements or on a modified retrospective basis which would result in the recognition of a cumulative effect of adopting ASU 2014-09 in the first quarter of 2018. We have completed our initial assessment of our business and systems requirements and we are currently developing and implementing a new revenue recognition system to comply with the requirements of ASU 2014-09. Based on this initial assessment, we currently plan to adopt the new revenue recognition standard under the modified retrospective transition method. Until we are further along in implementing our new revenue recognition system, we do not anticipate being able to provide reasonably accurate estimates of the impact of ASU 2014-09 on the timing of our revenue recognition.

## (2) Pending Acquisition of Level 3

On October 31, 2016, we entered into a definitive merger agreement under which we propose to acquire Level 3 Communications, Inc. ("Level 3") in a cash and stock transaction. Under the terms of the agreement, Level 3 shareholders will receive \$26.50 per share in cash and 1.4286 of CenturyLink shares for each share of Level 3 common stock they own at closing. CenturyLink shareholders are expected to own approximately 51% and Level 3 shareholders are expected to own approximately 49% of the combined company at closing. On December 31, 2016, Level 3 had outstanding \$10.9 billion of long-term debt.

Completion of the transaction is subject to the receipt of regulatory approvals, including the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act, as well as approvals from the FCC and certain state regulatory authorities. The transaction is also subject to the approval of CenturyLink and Level 3 shareholders at meetings scheduled for March 16, 2017, as well as other customary closing conditions. Subject to these conditions, we anticipate closing this transaction by the end of the third quarter 2017. If the merger is terminated under certain circumstances, we may be obligated to pay Level 3 a termination fee of \$472 million, or Level 3 may be obligated to pay CenturyLink a termination fee of \$738 million.

## (3) Pending Sale of Colocation Business and Data Centers

On November 3, 2016, we entered into a definitive stock purchase agreement to sell our data centers and colocation business to a consortium led by BC Partners, Inc. and Medina Capital in exchange for cash and a minority stake in the consortium's newly-formed global secure infrastructure company. The sale is subject to regulatory approvals, including a review by the Committee of Foreign Investments in the United States, as well as other customary closing conditions.

Based on certain estimates and assumptions regarding the closing date and various tax matters, we currently project that the net cash proceeds from the divestiture will be approximately \$1.5 billion to \$1.7 billion. We plan to use a portion of these net cash proceeds to partly fund our acquisition of Level 3.

As a result of the pending sale of our colocation business and data centers, we reclassified the following assets and liabilities, which are now reflected as assets held for sale and current liabilities associated with the assets held for sale on our consolidated balance sheet, respectively, as of December 31, 2016:

	Dollars in millions
Goodwill	\$ 1,141
Property, plant and equipment	1,071
Other intangible assets	258
Other assets	45
Total amount reclassified to assets held for sale <sup>(1)</sup>	<u>\$ 2,515</u>
Capital lease obligations	305
Other liabilities	114
Total liabilities associated with assets held for sale	<u>\$ 419</u>

<sup>(1)</sup> A portion of the assets equivalent to our anticipated minority stake, which was based on an estimated fair value, in the consortium's newly-formed global secure infrastructure company is reflected in non-current other assets on our consolidated balance sheet



The colocation business has resided in our business reporting unit. The amount of goodwill allocated to the colocation business being sold was determined using a relative-fair-value approach. The amount of goodwill included in the carrying amount of assets held for sale was based on the relative fair value of the colocation business we agreed to sell and the portion of the business reporting unit to be retained by us. We used the sale price as the fair value of the colocation business and the relative business fair value for the portion of the business reporting unit we will retain. As of November 3, 2016, we performed a quantitative assessment of the goodwill remaining in the business reporting unit after the allocation to the colocation business and concluded the remaining goodwill was not impaired as of that date.

Effective with the date we entered into the agreement to sell the colocation business we ceased recording depreciation of the property, plant and equipment to be sold and amortization of the intangible assets. We estimate that we would have recorded \$36 million of depreciation and amortization expense in the two months subsequent to entering into the agreement to sell the colocation business if we had not met the held-for-sale criteria.

We have estimated that after factoring in the costs to sell the colocation business the net carrying value of the assets and liabilities being sold closely approximates the estimated value of the proceeds we will receive upon closing. We further estimate, due to corporate actions we plan to take in the first quarter of 2017 regarding certain subsidiaries involved in the colocation business, that we will trigger tax expense relating to the sale of approximately \$100 million to \$200 million.

For additional information on our goodwill, see Note 4—Goodwill, Customer Relationships and Other Intangible Assets.

#### (4) Goodwill, Customer Relationships and Other Intangible Assets

Goodwill, customer relationships and other intangible assets consisted of the following:

	As of December 31,	
	2016	2015
	(Dollars in millions)	
Goodwill	\$ 19,650	20,742
Customer relationships, less accumulated amortization of \$6,318 and \$5,648	2,797	3,928
Indefinite-life intangible assets	269	269
Other intangible assets subject to amortization:		
Capitalized software, less accumulated amortization of \$2,019 and \$1,778	1,227	1,248
Trade names and patents, less accumulated amortization of \$23 and \$20	35	38
Total other intangible assets, net	\$ 1,531	1,555

Total amortization expense for intangible assets for the years ended December 31, 2016, 2015 and 2014 was \$1.225 billion, \$1.353 billion and \$1.470 billion, respectively. As of December 31, 2016, the gross carrying amount of goodwill, customer relationships, indefinite-life and other intangible assets was \$32.338 billion.

We estimate that total amortization expense for intangible assets for the years ending December 31, 2017 through 2021 will be as follows:

	(Dollars in millions)	
2017	\$	1,044
2018		925
2019		808
2020		703
2021		268

Our goodwill was derived from numerous acquisitions where the purchase price exceeded the fair value of the net assets acquired.

We assess our goodwill and other indefinite-lived intangible assets for impairment annually, or, under certain circumstances, more frequently, such as when events or changes in circumstances indicate there may be impairment. We are required to write down the value of goodwill only when our assessment determines the recorded amount of goodwill exceeds the fair value. Our annual impairment assessment date for goodwill is October 31, at which date we assessed our reporting units, which are business (excluding wholesale), consumer and wholesale. Our annual impairment assessment date for indefinite-lived intangible assets other than goodwill is December 31.

Our reporting units are not discrete legal entities with discrete financial statements. Our assets and liabilities are employed in and relate to the operations of multiple reporting units. For each reporting unit, we compare its estimated fair value of equity to its carrying value of equity that we assign to the reporting unit. If the estimated fair value of the reporting unit is greater than the carrying value, we conclude that no impairment exists. If the estimated fair value of the reporting unit is less than the carrying value, a second calculation is required in which the implied fair value of goodwill is compared to the carrying value of goodwill that we assigned to the reporting unit. If the implied fair value of goodwill is less than its carrying value, goodwill must be written down to its implied fair value.

At October 31, 2016, we utilized a level 3 valuation technique to estimate the fair value of our business (excluding wholesale), consumer and wholesale reporting units by considering both a market approach and a discounted cash flow method. The market approach method includes the use of comparable multiples of publicly traded companies whose services are comparable to ours. The discounted cash flow method is based on the present value of projected cash flows and a terminal value, which represents the expected normalized cash flows of the reporting units beyond the cash flows from the discrete projection period. We discounted the estimated cash flows for our consumer and wholesale reporting units using a rate that represents their estimated weighted average cost of capital, which we determined to be approximately 6.0% as of the assessment date (which was comprised of an after-tax cost of debt of 2.8% and a cost of equity of 6.2%). We discounted the estimated cash flows of our business (excluding wholesale) reporting unit using a rate that represents its estimated weighted average cost of capital, which we determined to be approximately 7.0% as of the assessment date (which was comprised of an after-tax cost of debt of 2.8% and a cost of equity of 6.8%). We also reconciled the estimated fair values of the reporting units to our market capitalization as of October 31, 2016 and concluded that the indicated implied control premium of approximately 33.8% was reasonable based on recent transactions in the market place. As of October 31, 2016, based on our assessment performed with respect to these reporting units as described above, we concluded that our goodwill for our three reporting units was not impaired as of that date.

The following table shows the rollforward of goodwill assigned to our reportable segments from December 31, 2014 through December 31, 2016.

	Business	Consumer	Total
	(Dollars in millions)		
As of December 31, 2014 <sup>(1)</sup>	\$ 10,477	10,278	20,755
Purchase accounting and other adjustments	(13)	—	(13)
As of December 31, 2015 <sup>(1)</sup>	10,464	10,278	20,742
Purchase accounting and other adjustments	49	—	49
Goodwill attributable to the colocation business and data centers reclassified to assets held for sale	(1,141)	—	(1,141)
As of December 31, 2016 <sup>(1)</sup>	\$ 9,372	\$ 10,278	\$ 19,650

<sup>(1)</sup> Goodwill is net of accumulated impairment losses of \$1.1 billion that related to our former hosting segment now included in our business segment.

During 2016, we acquired all of the outstanding stock of three companies for total consideration of \$53 million, including future deferred or contingent cash payments of \$14 million, of which \$49 million has initially been attributed to goodwill. The valuation for these three acquisitions is preliminary and subject to change during the measurement period, which will end one year from the date of each acquisition. These acquisitions were consummated to expand the product offerings of our business segment and therefore the goodwill has been assigned to that segment. The majority of the goodwill is attributed primarily to expected future increases in business segment revenue from the sale of new products. The majority of the goodwill from these acquisitions is expected to be deductible for tax purposes.

None of the above-described acquisitions materially impacted the consolidated results of operations from the dates of the acquisitions and would not materially impact pro forma results of operations.

For additional information on our segments, see Note 14—Segment Information.

We completed our qualitative assessment of our indefinite-lived intangible assets other than goodwill as of December 31, 2016 and concluded it is more likely than not that our indefinite-lived intangible assets are not impaired; thus, no impairment charge was recorded in 2016.



As of October 31, 2015, based on our assessment performed, we concluded that our goodwill for our then three reporting units was not impaired as of that date. As of October 31, 2014, based on our assessment performed, we concluded that our goodwill for our then four reporting units was not impaired as of that date.

### (5) Long-Term Debt and Credit Facilities

Long-term debt, including unamortized discounts and premiums and unamortized debt issuance costs, consisting of borrowings by CenturyLink, Inc. and certain of its subsidiaries, including Qwest Corporation, Qwest Capital Funding, Inc. and Embarq Corporation and its subsidiaries ("Embarq"), were as follows:

	Interest Rates	Maturities	As of December 31,	
			2016	2015
(Dollars in millions)				
<b>CenturyLink, Inc.</b>				
Senior notes	5.150% - 7.650%	2017 - 2042	\$ 8,975	7,975
Credit facility and revolving line of credit <sup>(1)</sup>	4.500%	2019	370	410
Term loan	2.520%	2019	336	358
<b>Subsidiaries</b>				
Qwest Corporation				
Senior notes	6.125% - 7.750%	2017 - 2056	7,259	7,229
Term loan	2.520%	2025	100	100
Qwest Capital Funding, Inc.				
Senior notes	6.500% - 7.750%	2018 - 2031	981	981
Embarq Corporation and subsidiaries				
Senior note	7.995%	2036	1,485	2,669
First mortgage bonds	7.125% - 8.770%	2017 - 2025	223	232
Other	9.000%	2019	150	150
Capital lease and other obligations	Various	Various	440	425
Unamortized discounts, net			(133)	(125)
Unamortized debt issuance costs			(193)	(179)
Total long-term debt			19,993	20,225
Less current maturities not associated with assets held for sale			(1,503)	(1,503)
Less capital lease obligations associated with assets held for sale <sup>(2)</sup>			(305)	—
Long-term debt, excluding current maturities and capital lease obligations associated with assets held for sale			\$ 18,185	18,722

(1) The aggregate amount outstanding on our Credit Facility and revolving line of credit borrowings at December 31, 2016 and 2015 was \$370 million and \$410 million, respectively, with weighted-average interest rates of 4.500% and 2.756%, respectively. These amounts change on a regular basis.

(2) If, as anticipated, we sell our colocation business and data centers in the manner discussed in Note 3—Pending Sale of Colocation Business and Data Centers, \$305 million of the capital lease obligations as of December 31, 2016 will be assumed by the Purchaser. See Note 3—Pending Sale of Colocation Business and Data Centers for additional information.

*New Issuances***2016**

On August 22, 2016, Qwest Corporation issued \$978 million aggregate principal amount of 6.5% Notes due 2056, including \$128 million principal amount that was sold pursuant to an over-allotment option, in exchange for net proceeds, after deducting underwriting discounts and other expenses, of \$946 million. All of the 6.5% Notes are unsecured obligations and may be redeemed by Qwest Corporation, in whole or in part, on or after September 1, 2021, at a redemption price equal to 100% of the principal amount redeemed plus accrued and unpaid interest to the redemption date.

On April 6, 2016, CenturyLink, Inc. issued \$1 billion aggregate principal amount of 7.5% Notes due 2024, in exchange for net proceeds, after deducting underwriting discounts and other expenses, of \$988 million. All of the 7.5% Notes are unsecured obligations and may be redeemed by CenturyLink, Inc., in whole or in part, on or after January 1, 2024, at a redemption price equal to 100% of the principal amount redeemed plus accrued and unpaid interest to the redemption date. At any time before January 1, 2024, the Notes are redeemable, in whole or in part, at CenturyLink, Inc.'s option, at a redemption price equal to the greater of 100% of the principal amount of the Notes to be redeemed or the sum of the present values of the remaining scheduled payments of principal and interest on the Notes to be redeemed, discounted to the redemption date in the manner described in the Notes, plus accrued and unpaid interest to the redemption date. In addition, at any time on or prior to April 1, 2019, CenturyLink, Inc. may redeem up to 35% of the aggregate principal amount of the Notes at a redemption price of 107.5% of the principal amount thereof, plus accrued and unpaid interest to the redemption date, with the net proceeds of certain equity offerings. Under certain circumstances, CenturyLink, Inc. will be required to make an offer to repurchase the Notes at a price of 101% of the aggregate principal amount plus accrued and unpaid interest to the repurchase date.

On January 29, 2016, Qwest Corporation issued \$235 million aggregate principal amount of 7% Notes due 2056, in exchange for net proceeds, after deducting underwriting discounts and other expenses, of \$227 million. All of the 7% Notes are unsecured obligations and may be redeemed by Qwest Corporation, in whole or in part, on or after February 1, 2021, at a redemption price equal to 100% of the principal amount redeemed plus accrued and unpaid interest to the redemption date.

**2015**

On September 21, 2015, Qwest Corporation issued \$400 million aggregate principal amount of 6.625% Notes due 2055, in exchange for net proceeds, after deducting underwriting discounts and other expenses, of approximately \$386 million. On September 30, 2015, Qwest Corporation issued an additional \$10 million aggregate principal amount of the 6.625% Notes under an over-allotment option granted to the underwriter for this offering. All of the 6.625% Notes are unsecured obligations and may be redeemed by Qwest Corporation, in whole or in part, on or after September 15, 2020, at a redemption price equal to 100% of the principal amount redeemed plus accrued and unpaid interest to the redemption date.

On March 19, 2015, CenturyLink, Inc. issued in a private offering \$500 million aggregate principal amount of 5.625% Notes due 2025, in exchange for net proceeds, after deducting underwriting discounts and other expenses, of approximately \$494 million. The Notes are senior unsecured obligations and may be redeemed, in whole or in part, at any time before January 1, 2025 at a redemption price equal to the greater of 100% of the principal amount of the Notes or the sum of the present value of the remaining scheduled payments of principal and interest on the Notes, discounted to the redemption date in the manner described in the Notes, plus accrued and unpaid interest to the redemption date. At any time on or after January 1, 2025, CenturyLink, Inc. may redeem the Notes at par plus accrued and unpaid interest to the redemption date. In addition, at any time on or prior to April 1, 2018, CenturyLink, Inc. may redeem up to 35% of the principal amount of the Notes at a redemption price equal to 105.625% of the principal amount thereof, plus accrued and unpaid interest to the redemption date, with net cash proceeds of certain equity offerings. Under certain circumstances, CenturyLink, Inc. will be required to make an offer to repurchase the Notes at a price of 101% of the aggregate principal amount plus accrued and unpaid interest to the repurchase date. In October 2015, CenturyLink, Inc. exchanged all of the unregistered Notes issued on March 19, 2015 for fully-registered Notes.

## *Repayments*

### **2016**

On December 23, 2016, a subsidiary of Embarq Corporation redeemed \$5 million of its 8.375% Notes due 2025, which resulted in an immaterial loss.

On September 19, 2016, a subsidiary of Embarq Corporation redeemed all of its 8.77% Notes due 2017, which was less than \$4 million and resulted in an immaterial loss.

On September 15, 2016, Qwest Corporation redeemed \$287 million of its 7.5% Notes due 2051, which resulted in a loss of \$9 million.

On August 29, 2016, Qwest Corporation redeemed all \$661 million of its 7.375% Notes due 2051, which resulted in a loss of \$18 million.

On June 1, 2016, Embarq Corporation paid at maturity the \$1.184 billion principal amount and accrued and unpaid interest due under its 7.082% Notes.

On May 2, 2016, Qwest Corporation paid at maturity the \$235 million principal amount and accrued and unpaid interest due under its 8.375% Notes.

### **2015**

On October 13, 2015, Qwest Corporation redeemed all \$250 million of its 7.2% Notes due 2026, which resulted in an immaterial gain, and redeemed \$150 million of its 6.875% Notes due 2033, which resulted in an immaterial loss.

On June 15, 2015, Qwest Corporation paid at maturity the \$92 million principal amount of its 7.625% Notes.

On February 17, 2015, CenturyLink, Inc. paid at maturity the \$350 million principal and accrued and unpaid interest due under its Series M 5.00% Notes.

## *Credit Facility*

Our \$2 billion revolving credit facility (as amended, the "Credit Facility") matures on December 3, 2019 and has 16 lenders, each with commitments ranging from \$3.5 million to \$198.5 million. The Credit Facility allows us to obtain revolving loans and to issue up to \$400 million of letters of credit, which upon issuance reduce the amount available for other extensions of credit. Interest is assessed on borrowings using either the LIBOR or the base rate (each as defined in the Credit Facility) plus an applicable margin between 1.00% and 2.25% per annum for LIBOR loans and 0.00% and 1.25% per annum for base rate loans depending on our then current senior unsecured long-term debt rating. Our obligations under the Credit Facility are guaranteed by nine of our subsidiaries.

### *Term Loans, Revolving Line of Credit and Revolving Letter of Credit*

The CenturyLink, Inc. term loan matures on April 18, 2019. In 2015, CenturyLink amended its term loan agreement to reduce the interest rate payable by it thereunder and to modify some covenants to provide additional flexibility.

In 2015, Qwest Corporation entered into a term loan in the amount of \$100 million with CoBank, ACB. The outstanding unpaid principal amount of this term loan plus any accrued and unpaid interest is due on February 20, 2025. Interest is paid monthly based upon either the London Interbank Offered Rate ("LIBOR") or the base rate (as defined in the credit agreement) plus an applicable margin between 1.50% to 2.50% per annum for LIBOR loans and 0.50% to 1.50% per annum for base rate loans depending on Qwest Corporation's then current senior unsecured long-term debt rating. At both December 31, 2016 and 2015, the outstanding principal balance on this term loan was \$100 million.

In 2016, our \$85 million uncommitted revolving line of credit with one of the lenders under the Credit Facility was suspended as a result of this lender's additional borrowing commitment towards the pending acquisition of Level 3. Interest is paid monthly based upon the LIBOR plus an applicable margin between 1.00% and 2.25% per annum. At December 31, 2016, CenturyLink, Inc. had no

borrowings outstanding under this uncommitted revolving line of credit and at December 31, 2015, CenturyLink, Inc. had \$80 million borrowings outstanding under this uncommitted revolving line of credit.

In April 2011, we entered into a \$160 million uncommitted revolving letter of credit facility which enables us to provide letters of credit under terms that may be more favorable than those under the Credit Facility. At December 31, 2016 and 2015, our outstanding letters of credit totaled \$105 million and \$109 million, respectively, under this facility.

### Aggregate Maturities of Long-Term Debt

Set forth below is the aggregate principal amount of our long-term debt (excluding unamortized discounts, net and unamortized debt issuance costs) maturing during the following years:

	(Dollars in millions) <sup>(1)</sup>
2017	\$ 1,544
2018	280
2019	1,131
2020	1,032
2021	2,329
2022 and thereafter	14,003
Total long-term debt	<u>\$ 20,319</u>

(1) Actual principal paid in any year may differ due to the possible future refinancing of outstanding debt or the issuance of new debt. The projected amounts in the table also exclude any impacts from the sale of our colocation business or any further acquisitions.

### Interest Expense

Interest expense includes interest on total long-term debt. The following table presents the amount of gross interest expense, net of capitalized interest:

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
Interest expense:			
Gross interest expense	\$ 1,372	1,364	1,358
Capitalized interest	(54)	(52)	(47)
Total interest expense	<u>\$ 1,318</u>	<u>1,312</u>	<u>1,311</u>

### Covenants

Certain of our loan agreements contain various restrictions, as described more fully below. Under current circumstances, we believe the covenants currently in effect place no significant restriction on the transfer of funds from our consolidated subsidiaries to CenturyLink.

The senior notes of CenturyLink, Inc. were issued under an indenture dated March 31, 1994. This indenture restricts our ability to (i) incur, issue or create liens upon the property of CenturyLink, Inc. and (ii) consolidate with or merge into, or transfer or lease all or substantially all of our assets to any other party. The indenture does not contain any provisions that are impacted by our credit ratings or that restrict the issuance of new securities in the event of a material adverse change to us. However, if the credit ratings relating to certain of our long-term debt securities issued under this indenture are downgraded in the manner specified thereunder in connection with a "change of control" of CenturyLink, Inc., then we will be required to offer to repurchase such debt securities.

The senior notes of Qwest Corporation were issued under indentures dated April 15, 1990 and October 15, 1999. These indentures contain restrictions on the incurrence of liens and the consummation of certain transactions substantially similar to the above-described covenants in CenturyLink, Inc.'s March 31, 1994 indenture. The senior notes of Qwest Capital Funding, Inc. were issued under an indenture dated June 29, 1998 containing terms substantially similar to those set forth in Qwest Corporation's indentures.

Embarq's senior note was issued pursuant to an indenture dated as of May 17, 2006. While Embarq is generally prohibited from creating liens on its property unless its senior notes are secured equally and ratably, Embarq can create liens on its property without equally and ratably securing its senior notes so long as the sum of all indebtedness so secured does not exceed 15% of Embarq's

consolidated net tangible assets. The indenture contains customary events of default, none of which are impacted by Embarq's credit rating.

None of the above-listed indentures of CenturyLink, Inc., Qwest Corporation, Qwest Capital Funding, Inc. and Embarq contain any financial covenants or restrictions on the ability to issue new securities in accordance with the terms of the indenture.

Several of our Embarq subsidiaries have outstanding first mortgage bonds. Each issue of these first mortgage bonds is secured by substantially all of the property, plant and equipment of the issuing subsidiary. Approximately 10% of our net property, plant and equipment is pledged to secure the long-term debt of subsidiaries.

Under the Credit Facility, we, and our indirect subsidiary, Qwest Corporation, must maintain a debt to EBITDA (earnings before interest, taxes, depreciation and amortization, as defined in our Credit Facility) ratio of not more than 4.0:1.0 and 2.85:1.0, respectively, as of the last day of each fiscal quarter for the four quarters then ended. The Credit Facility also contains a negative pledge covenant, which generally requires us to secure equally and ratably any advances under the Credit Facility if we pledge assets or permit liens on our property for the benefit of other debtholders. The Credit Facility also has a cross payment default provision, and the Credit Facility and certain of our debt securities also have cross acceleration provisions. When present, these provisions could have a wider impact on liquidity than might otherwise arise from a default or acceleration of a single debt instrument. Our debt to EBITDA ratios could be adversely affected by a wide variety of events, including unforeseen expenses or contingencies. This could reduce our financing flexibility due to potential restrictions on incurring additional debt under certain provisions of our debt agreements or, in certain circumstances, could result in a default under certain provisions of such agreements.

CenturyLink, Inc. and Qwest Corporation are both indebted under term loans, each of which includes covenants substantially similar to those set forth in the Credit Facility.

At December 31, 2016, we believe we were in compliance with all of the provisions and covenants contained in our Credit Facility and other material debt agreements.

### ***Guarantees***

We do not guarantee the debt of any unaffiliated parties, but certain of our subsidiaries guarantee the outstanding senior notes issued by other subsidiaries. In addition, nine of our largest wholly owned subsidiaries guarantee the obligations of CenturyLink, Inc. under the Credit Facility and its term loan.

### ***Level 3 Financing Commitment Letter***

In connection with entering into our merger agreement with Level 3 (discussed further in Note 2), on October 31, 2016, we obtained a debt commitment letter, which was amended and restated on November 13, 2016, and further amended on November 15, 2016 (the "Debt Commitment Letter"), from Bank of America, N.A., Morgan Stanley Senior Funding, Inc., The Bank of Tokyo-Mitsubishi UFJ, Ltd., Barclays Bank PLC, JPMorgan Chase Bank, N.A., Wells Fargo Bank, National Association, Royal Bank of Canada, Goldman Sachs Bank USA, SunTrust Bank, Mizuho Bank, Ltd., Regions Bank, Fifth Third Bank, Credit Suisse AG, Cayman Islands Branch, and U.S. Bank, National Association (collectively the "Commitment Parties"), pursuant to which the Commitment Parties or certain of their affiliates agreed to provide a \$2.0 billion senior secured revolving credit facility, a \$1.5 billion senior secured term loan "A" credit facility, a \$4.5 billion senior secured term loan "B" credit facility and a \$2.225 billion senior secured bridge loan facility (collectively, the "Commitment Facilities"), together with certain backstop commitments designed to provide additional acquisition-related financing in certain limited instances. The secured bridge loan facility will only be drawn to the extent we are unable to raise such amounts by issuing senior secured notes or other debt securities at or prior to the closing of the Level 3 acquisition. The senior secured revolving credit facility is designed to replace the Credit Facility. Bank of America, N.A. and Morgan Stanley Senior Funding, Inc., affiliates of BofA Merrill Lynch and Morgan Stanley, will be entitled to receive financing fees in connection with the debt commitment letter, the amount of which will vary based on, among other things, when the debt financing is incurred, whether the previously-announced divestiture of our data centers and colocation business closes prior to the Level 3 acquisition and whether the bridge loan facility is drawn. The financing fees to be payable to Bank of America, N.A. and Morgan Stanley Senior Funding, Inc. are expected to be quite substantial.

Each Commitment Party's commitments to provide the Commitment Facilities and each Commitment Party's agreements to perform the services described in the Commitment Letter will automatically terminate on the earliest of (i) the date of termination of our merger agreement with Level 3 in accordance with its terms, (ii) the closing of the Level 3 acquisition with or without the use of such Commitment Facilities and (iii) 11:59 p.m. on October 31, 2017 (or, if the "Termination Date" as defined in the merger agreement is extended in certain circumstances, the date to which it is extended that is not later than 11:59 p.m. on January 31, 2018).



The definitive documentation governing the Level 3 debt financing has not been finalized and, accordingly, the actual terms of the debt financing may differ from those described above. Although the debt financing described above is not subject to due diligence or a "market out," such financing may not be considered assured. The obligation of the Commitment Parties to provide debt financing under the debt commitment letter is subject to a number of conditions, and it is anticipated that the definitive debt financing documentation will also include certain funding conditions. There is a risk that these conditions will not be satisfied and the debt financing may not be available when required. In addition, we have the right to substitute the proceeds of other debt financing, or commitments for other debt financing, for all or any portion of the Commitment Facilities. As of the date of this annual report, no such other debt financing has been arranged.

#### (6) Accounts Receivable

The following table presents details of our accounts receivable balances:

	As of December 31,	
	2016	2015
	(Dollars in millions)	
Trade and purchased receivables	\$ 1,882	1,789
Earned and unbilled receivables	299	288
Other	14	18
Total accounts receivable	2,195	2,095
Less: allowance for doubtful accounts	(178)	(152)
Accounts receivable, less allowance	\$ 2,017	1,943

We are exposed to concentrations of credit risk from residential and business customers within our local service area, business customers outside of our local service area and from other telecommunications service providers. We generally do not require collateral to secure our receivable balances. We have agreements with other telecommunications service providers whereby we agree to bill and collect on their behalf for services rendered by those providers to our customers within our local service area. We purchase accounts receivable from other telecommunications service providers primarily on a recourse basis and include these amounts in our accounts receivable balance. We have not experienced any significant loss associated with these purchased receivables.

The following table presents details of our allowance for doubtful accounts:

	Beginning Balance	Additions	Deductions	Ending Balance
	(Dollars in millions)			
2016	\$ 152	192	(166)	178
2015	\$ 162	177	(187)	152
2014	\$ 155	159	(152)	162

**(7) Property, Plant and Equipment**

Net property, plant and equipment is composed of the following:

	Depreciable Lives	As of December 31,	
		2016	2015
		(Dollars in millions)	
Land	N/A	\$ 563	571
Fiber, conduit and other outside plant <sup>(1)</sup>	15-45 years	16,996	16,166
Central office and other network electronics <sup>(2)</sup>	3-10 years	13,768	14,144
Support assets <sup>(3)</sup>	3-30 years	6,623	7,000
Construction in progress <sup>(4)</sup>	N/A	1,244	904
Gross property, plant and equipment		39,194	38,785
Accumulated depreciation		(22,155)	(20,716)
Net property, plant and equipment		\$ 17,039	18,069

- (1) Fiber, conduit and other outside plant consists of fiber and metallic cable, conduit, poles and other supporting structures.
- (2) Central office and other network electronics consists of circuit and packet switches, routers, transmission electronics and electronics providing service to customers.
- (3) Support assets consist of buildings, data centers, computers and other administrative and support equipment.
- (4) Construction in progress includes inventory held for construction and property of the aforementioned categories that has not been placed in service as it is still under construction.

See Note 3—Pending Sale of Colocation Business and Data Centers for additional information on our colocation assets and data centers reclassified to assets held for sale.

We recorded depreciation expense of \$2.691 billion, \$2.836 billion and \$2.958 billion for the years ended December 31, 2016, 2015 and 2014, respectively.

In 2014, we recorded an impairment charge of \$17 million in connection with a sale-leaseback transaction involving an office building that we closed in the fourth quarter of 2014. This impairment charge is included in selling, general and administrative expense in our consolidated statement of operations for the year ended December 31, 2014.

Additionally, in 2014 we sold an office building for \$12 million.

**Asset Retirement Obligations**

At December 31, 2016, our asset retirement obligations balance was primarily related to estimated future costs of removing equipment from leased properties and estimated future costs of properly disposing of asbestos and other hazardous materials upon remodeling or demolishing buildings. Asset retirement obligations are included in other long-term liabilities on our consolidated balance sheets.

The following table provides asset retirement obligation activity:

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
Balance at beginning of year	\$ 91	107	106
Accretion expense	6	7	7
Liabilities incurred	—	—	6

Liabilities settled	(2)	(2)	(2)
Change in estimate	—	(21)	(10)
Balance at end of year	<u>\$ 95</u>	<u>91</u>	<u>107</u>

If, as anticipated, we sell our colocation business and data centers in the manner discussed in Note 3, \$19 million of the asset retirement obligation as of December 31, 2016 will be assumed by the Purchaser.

Our estimates for the cost of removal of network equipment, asbestos remediation and other obligations remained unchanged for the year ended December 31, 2016. During 2015 and 2014, we revised our estimates for the cost of removal of network equipment, asbestos remediation, and other obligations by \$21 million and \$10 million, respectively. These revisions resulted in a reduction of the asset retirement obligation and offsetting reduction to gross property, plant and equipment, and revisions to assets specifically identified are recorded as a reduction to accretion expense.

#### (8) Severance and Leased Real Estate

Periodically, we reduce our workforce and accrue liabilities for the related severance costs. These workforce reductions resulted primarily from the progression or completion of our post-acquisition integration plans, increased competitive pressures, cost reduction initiatives, process improvements through automation and reduced workload demands due to the loss of customers purchasing certain services.

We report severance liabilities within accrued expenses and other liabilities - salaries and benefits in our consolidated balance sheets and report severance expenses in selling, general and administrative expenses in our consolidated statements of operations. As noted in Note 14—Segment Information, we do not allocate these severance expenses to our segments.

We have recognized liabilities to reflect our estimates of the fair values of the existing lease obligations for real estate which we have ceased using, net of estimated sublease rentals. Our fair value estimates were determined using discounted cash flow methods. We recognize expense to reflect accretion of the discounted liabilities and periodically we adjust the expense when our actual subleasing experience differs from our initial estimates. We report the current portion of liabilities for ceased-use real estate leases in accrued expenses and other liabilities-other and report the noncurrent portion in deferred credits and other liabilities in our consolidated balance sheets. We report the related expenses in selling, general and administrative expenses in our consolidated statements of operations. At December 31, 2016, the current and noncurrent portions of our leased real estate accrual were \$8 million and \$59 million, respectively. The remaining lease terms range from 1.2 years to 9.0 years, with a weighted average of 7.8 years.

Changes in our accrued liabilities for severance expenses and leased real estate were as follows:

	Severance	Real Estate
	(Dollars in millions)	
Balance at December 31, 2014	\$ 26	96
Accrued to expense	96	—
Payments, net	(108)	(13)
Reversals and adjustments	—	(3)
Balance at December 31, 2015	14	80
Accrued to expense	173	4
Payments, net	(89)	(20)
Reversals and adjustments	—	3
Balance at December 31, 2016	\$ 98	67

#### (9) Employee Benefits

##### *Pension, Post-Retirement and Other Post-Employment Benefits*

We sponsor various defined benefit pension plans (qualified and non-qualified), which in the aggregate cover a substantial portion of our employees including legacy CenturyLink, legacy Qwest Communications International, Inc. ("Qwest") and legacy Embarq employees. On December 31, 2014, we merged our existing qualified pension plans, which included merging the Qwest Pension Plan and Embarq Retirement Pension Plan into the CenturyLink Retirement Plan. The CenturyLink Retirement Plan was renamed the CenturyLink Combined Pension Plan ("Combined Plan"). Pension benefits for participants of the new Combined Plan who are represented by a collective bargaining agreement are based on negotiated schedules. All other participants' pension benefits are based on each individual participant's years of service and compensation. We also maintain non-qualified pension plans for certain current and former highly compensated employees. We maintain post-retirement benefit plans that provide health care and life insurance benefits for certain eligible retirees. We also provide other post-employment benefits for certain eligible former employees. We use a December 31 measurement date for all our plans.



## Pension Benefits

Current funding laws require a company with a pension shortfall to fund the annual cost of benefits earned in addition to a seven-year amortization of the shortfall. Our funding policy for our Combined Plan is to make contributions with the objective of accumulating sufficient assets to pay all qualified pension benefits when due under the terms of the plan. The accounting unfunded status of our qualified pension plan was \$2.352 billion and \$2.215 billion as of December 31, 2016 and 2015, respectively.

We made a voluntary cash contribution of \$100 million in both 2016 and 2015 to our qualified pension plan and paid \$7 million and \$6 million of benefits directly to participants of our non-qualified pension plans in 2016 and 2015, respectively. Based on current laws and circumstances, we are not required to make any contributions to our qualified pension plan in 2017, but we estimate that we will pay \$6 million of benefits directly to participants of our non-qualified pension plans. We currently expect to make a voluntary contribution of \$100 million to the trust for our qualified pension plan in 2017.

Our pension plans contain provisions that allow us, from time to time, to offer lump sum payment options to certain former employees in settlement of their future retirement benefits. Additionally, eligible employees who terminate employment may elect to receive a lump sum payout. We record these payments as a settlement only if, in the aggregate, they exceed the sum of the annual service and interest costs for the plan's net periodic pension benefit costs, which represents the settlement threshold. There were no pension lump sum offerings in 2016, other than those to eligible employees who terminated during 2016. In 2015, we made cash settlement payments of \$356 million through a lump sum offering to a group of former employees. The total amount of the lump sum settlement payments for the year ended December 31, 2015, which included the lump sum offer and lump sum elections from employees who terminated employment during the year, was less than the settlement threshold, therefore settlement accounting was not triggered in 2015. In 2014, lump sum pension settlement payments to terminated, but not-yet-retired legacy Qwest participants was \$460 million, which exceeded the settlement threshold of \$418 million. As a result, we were required to recognize a settlement charge of \$63 million in 2014 to accelerate the recognition of a portion of the previously unrecognized actuarial losses in the qualified pension plan, which has been allocated and reflected in cost of services and products (exclusive of depreciation and amortization) and selling, general and administrative in our consolidated statement of operations for the year ended December 31, 2014. This charge reduced our recorded net income and retained earnings, with an offset to accumulated other comprehensive loss in shareholders' equity. The amount of any future non-cash settlement charges will depend on the level of lump sum benefit payments made in 2017 and beyond.

## Post-Retirement Benefits

Our post-retirement benefit plans provide post-retirement benefits to qualified retirees and allow (i) eligible employees retiring before certain dates to receive benefits at no or reduced cost and (ii) eligible employees retiring after certain dates to receive benefits on a shared cost basis. The post-retirement benefits not paid by the trust are funded by us and we expect to continue funding these post-retirement obligations as benefits are paid. The accounting unfunded status of our qualified post-retirement benefit plan was \$3.360 billion and \$3.374 billion as of December 31, 2016 and 2015, respectively.

Assets in the post-retirement trusts have been substantially depleted as of December 31, 2016; however we will continue to pay certain post-retirement benefits through the trusts. No contributions were made to the post-retirement trusts in 2016, and we do not expect to make a contribution in 2017. In 2016, we paid \$129 million of post-retirement benefits, net of participant contributions and direct subsidies. In 2017, we expect to pay \$275 million of post-retirement benefits, net of participant contributions and direct subsidies. The increase in anticipated post-retirement benefit payments is the result of substantially depleting the plan assets held in the trust.

We expect our health care cost trend rate to range from 5.0% to 5.5% in 2017 to 5.0% to 6.0% in 2018 and 2019 and grading to 4.50% by 2025. Our post-retirement benefit expense, for certain eligible legacy Qwest retirees and certain eligible legacy CenturyLink retirees, is capped at a set dollar amount. Therefore, those health care benefit obligations are not subject to increasing health care trends after the effective date of the caps.

A change of 100 basis points in the assumed initial health care cost trend rate would have had the following effects in 2016:

	100 Basis Points Change	
	Increase	(Decrease)
	(Dollars in millions)	
Effect on the aggregate of the service and interest cost components of net periodic post-retirement benefit expense (consolidated statement of operations)	\$ 2	(2)
Effect on benefit obligation (consolidated balance sheet)	66	(61)

### Expected Cash Flows

The qualified pension, non-qualified pension and post-retirement health care benefit payments and premiums and life insurance premium payments are paid by us or distributed from plan assets. The estimated benefit payments provided below are based on actuarial assumptions using the demographics of the employee and retiree populations and have been reduced by estimated participant contributions.

	Pension Plans	Post-Retirement Benefit Plans	Medicare Part D Subsidy Receipts
	(Dollars in millions)		
Estimated future benefit payments:			
2017	\$ 1,277	295	(6)
2018	987	284	(6)
2019	968	275	(6)
2020	948	267	(6)
2021	928	259	(6)
2022 - 2026	4,280	1,160	(26)

### Net Periodic Benefit Expense

In 2016, we changed the method we use to estimate the service and interest components of net periodic benefit expense for pension and other postretirement benefit obligations. This change resulted in a decrease in the service and interest components in 2016. Beginning in 2016, we utilized a full yield curve approach in connection with estimating these components by applying the specific spot rates along the yield curve used in the determination of the benefit obligation to the relevant projected cash flows, as opposed to the single weighted-average discount rate derived from the yield curve that we have used in the past. We believe this change more precisely measures service and interest costs by improving the correlation between projected benefit cash flows to the corresponding spot yield curve rates. This change did not affect the measurement of our total benefit obligations but lowered our annual net periodic benefit cost by approximately \$149 million in 2016. This change was treated as a change in accounting estimate and accordingly, we did not adjust the amounts recorded in 2015 or 2014.

The actuarial assumptions used to compute the net periodic benefit expense for our qualified pension, non-qualified pension and post-retirement benefit plans are based upon information available as of the beginning of the year, as presented in the following table.

	Pension Plans			Post-Retirement Benefit Plans		
	2016	2015	2014	2016	2015	2014
Actuarial assumptions at beginning of year:						
Discount rate	3.50% - 4.50%	3.50% - 4.10%	4.20% - 5.10%	4.15%	3.80%	4.50%
Rate of compensation increase	3.25%	3.25%	3.25%	N/A	N/A	N/A
Expected long-term rate of return on plan assets	7.00%	7.50%	7.50%	7.00%	7.50%	6.00% - 7.50%
Initial health care cost trend rate	N/A	N/A	N/A	5.00% / 5.25%	6.00% / 6.50%	6.00% / 6.50%
Ultimate health care cost trend rate	N/A	N/A	N/A	4.50%	4.50%	4.50%
Year ultimate trend rate is reached	N/A	N/A	N/A	2025	2025	2024

N/A-Not applicable

Net periodic benefit (income) expense for our qualified and non-qualified pension plans includes the following components:

	<b>Pension Plans</b>		
	<b>Years Ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
	<b>(Dollars in millions)</b>		
Service cost	\$ 64	83	77
Interest cost	427	568	602
Expected return on plan assets	(732)	(898)	(891)
Settlements	—	—	63
Special termination benefits charge	13	—	—
Recognition of prior service (credit) cost	(8)	5	5
Recognition of actuarial loss	175	161	22
Net periodic pension benefit income	<u>\$ (61)</u>	<u>(81)</u>	<u>(122)</u>

Net periodic benefit expense (income) for our post-retirement benefit plans includes the following components:

	<b>Post-Retirement Plans</b>		
	<b>Years Ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
	<b>(Dollars in millions)</b>		
Service cost	\$ 19	24	22
Interest cost	111	140	159
Expected return on plan assets	(7)	(21)	(33)
Special termination benefits charge	3	—	—
Recognition of prior service cost	20	19	20
Net periodic post-retirement benefit expense	<u>\$ 146</u>	<u>162</u>	<u>168</u>

We report net periodic benefit (income) expense for our qualified pension, non-qualified pension and post-retirement benefit plans in cost of services and products and selling, general and administrative expenses in our consolidated statements of operations for the years ended December 31, 2016, 2015 and 2014. In the third quarter of 2016, we announced plans to reduce our workforce, initially through voluntary severance packages and the balance through involuntary reductions. We recognized in the fourth quarter of 2016, a one-time charge of \$16 million for special termination benefit enhancements paid to certain eligible employees upon voluntary retirement.

### ***Benefit Obligations***

The actuarial assumptions used to compute the funded status for the plans are based upon information available as of December 31, 2016 and 2015 and are as follows:

	<b>Pension Plans</b>		<b>Post-Retirement Benefit Plans</b>	
	<b>December 31,</b>		<b>December 31,</b>	
	<b>2016</b>	<b>2015</b>	<b>2016</b>	<b>2015</b>
Actuarial assumptions at end of year:				
Discount rate	3.50% - 4.10%	3.50% - 4.50%	3.90%	4.15%
Rate of compensation increase	3.25%	3.25%	N/A	N/A
Initial health care cost trend rate	N/A	N/A	5.00% / 5.50%	5.00% / 5.25%
Ultimate health care cost trend rate	N/A	N/A	4.50%	4.50%
Year ultimate trend rate is reached	N/A	N/A	2025	2025

N/A-Not applicable

In 2016, we adopted the revised mortality table and projection scale released by the Society of Actuaries ("SOA"), which decreased the projected benefit obligation of our benefit plans by \$268 million. The 2015 revised mortality table and projection scale decreased the 2015 projected benefit obligation of our benefit plans by \$379 million. In 2014, to better reflect the expected lifetimes of our plan participants, we adopted a new mortality table for our defined benefit plan. The table used was based on SOA tables and increased the projected benefit obligation of our benefit plans by approximately \$1.3 billion. The change in the projected benefit obligation of our benefit plans was recognized as part of the net actuarial loss and is included in accumulated other comprehensive loss, a portion of which is subject to amortization over the remaining estimated life of plan participants, which was approximately 9 to 10 years as of December 31, 2016.

The following tables summarize the change in the benefit obligations for the pension and post-retirement benefit plans:

	<b>Pension Plans</b>		
	<b>Years Ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
	(Dollars in millions)		
Change in benefit obligation			
Benefit obligation at beginning of year	\$ 13,349	15,042	13,401
Service cost	64	83	77
Interest cost	427	568	602
Plan amendments	2	(100)	4
Special termination benefits charge	13	—	—
Actuarial loss (gain)	487	(800)	2,269
Settlements	—	—	(460)
Benefits paid by company	(7)	(6)	(6)
Benefits paid from plan assets	(1,034)	(1,438)	(845)
Benefit obligation at end of year	<u>\$ 13,301</u>	<u>13,349</u>	<u>15,042</u>

	<b>Post-Retirement Benefit Plans</b>		
	<b>Years Ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
	(Dollars in millions)		
Change in benefit obligation			
Benefit obligation at beginning of year	\$ 3,567	3,830	3,688
Service cost	19	24	22
Interest cost	111	140	159
Participant contributions	57	57	69
Plan amendments	—	—	23
Direct subsidy receipts	5	8	9
Special termination benefits charge	3	—	—
Actuarial (gain) loss	(13)	(148)	245
Benefits paid by company	(191)	(181)	(166)
Benefits paid from plan assets	(145)	(163)	(219)
Benefit obligation at end of year	<u>\$ 3,413</u>	<u>3,567</u>	<u>3,830</u>

Our aggregate benefit obligation as of December 31, 2016, 2015 and 2014 was \$16.714 billion, \$16.916 billion and \$18.872 billion, respectively.

### Plan Assets

We maintain plan assets for our qualified pension plan and certain post-retirement benefit plans. The qualified pension plan's assets are used for the payment of pension benefits and certain eligible plan expenses. The post-retirement benefit plan's assets are used to pay health care benefits and premiums on behalf of eligible retirees and to pay certain eligible plan expenses. As discussed further above, the liquid plan assets in our post-retirement trust have been substantially depleted as of December 31, 2016. The expected rate of return on plan assets is the long-term rate of return we expect to earn on the plans' assets, net of administrative expenses paid from plan assets. The rate of return is determined by the strategic allocation of plan assets and the long-term risk and return forecast for each asset class. The forecasts for each asset class are generated primarily from an analysis of the long-term expectations of various third party investment management organizations. The expected rate of return on plan assets is reviewed annually and revised, as necessary, to reflect changes in the financial markets and our investment strategy.

The following tables summarize the change in the fair value of plan assets for the pension and post-retirement benefit plans:

	Pension Plans		
	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
Change in plan assets			
Fair value of plan assets at beginning of year	\$ 11,072	12,571	12,346
Return on plan assets	754	(161)	1,373
Employer contributions	100	100	157
Settlements	—	—	(460)
Benefits paid from plan assets	(1,034)	(1,438)	(845)
Fair value of plan assets at end of year	\$ 10,892	11,072	12,571

	Post-Retirement Benefit Plans		
	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
Change in plan assets			
Fair value of plan assets at beginning of year	\$ 193	353	535
Return on plan assets	5	3	37
Benefits paid from plan assets	(145)	(163)	(219)
Fair value of plan assets at end of year	\$ 53	193	353

*Pension Plans:* Our investment objective for the qualified pension plan assets is to achieve an attractive risk-adjusted return over time that will provide for the payment of benefits and minimize the risk of large losses. Our pension plan investment strategy is designed to meet this objective by broadly diversifying plan assets across numerous strategies with differing expected returns, volatilities and correlations. The pension plan assets have target allocations of 45% to interest rate sensitive investments and 55% to investments designed to provide higher expected returns than the interest rate sensitive investments. Interest rate sensitive investments include 30% of plan assets targeted primarily to long-duration investment grade bonds, 10% targeted to high yield and emerging market bonds and 5% targeted to diversified strategies, which primarily have exposures to global bonds, as well as some exposures to global stocks and commodities. Assets expected to provide higher returns than the interest rate sensitive assets include broadly diversified equity investments with targets of approximately 15% to U.S. equity markets and 15% to non-U.S. developed and emerging markets. Approximately 7% is targeted to broadly diversified multi-asset class strategies that have the flexibility to adjust exposures to different asset classes. Approximately 10% is allocated to private markets investments including funds primarily invested in private equity, private debt and hedge funds. Real estate investments are targeted at 8% of plan assets. At the beginning of 2017, our expected annual long-term rate of return on pension assets before consideration of administrative expenses is assumed to be 7.0%. However, projected increases in PBGC (Pension Benefit Guaranty Corporation) premium rates have now become large enough to reduce the annual long-term expected return net of administrative expenses to 6.5%.

Our non-qualified pension plans are not funded. We pay benefits directly to the participants of these plans.

*Post-Retirement Benefit Plans:* Our investment objective for the post-retirement benefit plans' assets is to achieve an attractive risk-adjusted return and minimize the risk of large losses over the expected life of the assets. At the beginning of 2017, our expected annual long-term rate of return on post-retirement benefit plan assets is assumed to be 5.0%.

*Permitted investments:* Plan assets are managed consistent with the restrictions set forth by the Employee Retirement Income Security Act of 1974, as amended, which requires diversification of assets and also generally prohibits defined benefit and welfare plans from investing more than 10% of their assets in securities issued by the sponsor company. At December 31, 2016 and 2015, the pension and post-retirement benefit plans did not directly own any shares of our common stock and less than 1% of the assets were held in CenturyLink debt.

*Derivative instruments:* Derivative instruments are used to reduce risk as well as provide return. The pension and post-retirement benefit plans use exchange traded futures and swaps to gain exposure to equity and interest rate markets consistent with target asset allocations and to reduce risk relative to measurement of the benefit obligation, which is sensitive to interest rate changes. Foreign exchange forward contracts are used to manage currency exposures. Credit default swaps are used to manage credit risk exposures in a cost effective and targeted manner relative to transacting with physical corporate fixed income securities. Options are currently used to manage interest rate exposure taking into account the implied volatility and current pricing of the specific underlying market instrument. Some derivative instruments subject the plans to counterparty risk. The external investment managers, along with Plan Management, monitor counterparty exposure and mitigate this risk by diversifying the exposure among multiple high credit quality counterparties, requiring collateral and limiting exposure by periodically settling contracts.

The gross notional exposure of the derivative instruments directly held by the pension benefit plan is shown below. The notional amount of the derivatives corresponds to market exposure but does not represent an actual cash investment. Our post-retirement plans were not invested in derivative instruments for the years ended December 31, 2016 or 2015.

	Gross Notional Exposure	
	Pension Plans	
	Years Ended December 31,	
	2016	2015
	(Dollars in millions)	
<u>Derivative instruments:</u>		
Exchange-traded U.S. equity futures	\$ 104	79
Exchange-traded Treasury and other interest rate futures	1,813	1,767
Interest rate swaps	260	550
Credit default swaps	240	189
Foreign exchange forwards	778	992
Options	206	285

*Fair Value Measurements:* Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between independent and knowledgeable parties who are willing and able to transact for an asset or liability at the measurement date. We use valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs when determining fair value and then we rank the estimated values based on the reliability of the inputs used following the fair value hierarchy set forth by the FASB. For additional information on the fair value hierarchy, see Note 12—Fair Value Disclosure.

At December 31, 2016, we used the following valuation techniques to measure fair value for assets. There were no changes to these methodologies during 2016:

- Level 1—Assets were valued using the closing price reported in the active market in which the individual security was traded.
- Level 2—Assets were valued using quoted prices in markets that are not active, broker dealer quotations, net asset value of shares held by the plans and other methods by which all significant inputs were observable at the measurement date.
- Level 3—Assets were valued using unobservable inputs in which little or no market data exists as reported by the respective institutions at the measurement date.



The tables below present the fair value of plan assets by category and the input levels used to determine those fair values at December 31, 2016. It is important to note that the asset allocations do not include market exposures that are gained with derivatives. Investments include dividend and interest receivables, pending trades and accrued expenses.

<b>Fair Value of Pension Plan Assets at December 31, 2016</b>				
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
	(Dollars in millions)			
Investment grade bonds (a)	\$ 420	1,404	—	\$ 1,824
High yield bonds (b)	7	597	11	615
Emerging market bonds (c)	212	212	—	424
Convertible bonds (d)	2	—	—	2
U.S. stocks (f)	1,144	1	—	1,145
Non-U.S. stocks (g)	721	1	—	722
Multi-asset strategies (m)	389	—	—	389
Cash equivalents and short-term investments (o)	—	207	—	207
Total investments, excluding investments valued at NAV	<u>\$ 2,895</u>	<u>2,422</u>	<u>11</u>	<u>5,328</u>
Investments valued at NAV				5,564
Total pension plan assets				<u>\$ 10,892</u>

<b>Fair Value of Post-Retirement Plan Assets at December 31, 2016</b>				
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
	(Dollars in millions)			
Investment grade bonds (a)	\$ 1	2	—	\$ 3
High yield bonds (b)	—	1	—	1
U.S. stocks (f)	2	—	—	2
Non-U.S. stocks (g)	1	—	—	1
Cash equivalents and short-term investments (o)	—	5	—	5
Total investments, excluding investments valued at NAV	<u>\$ 4</u>	<u>8</u>	<u>—</u>	<u>12</u>
Investments valued at NAV				41
Total post-retirement plan assets				<u>\$ 53</u>

The tables below present the fair value of plan assets by category and the input levels used to determine those fair values at December 31, 2015. It is important to note that the asset allocations do not include market exposures that are gained with derivatives. Investments include dividend and interest receivable, pending trades and accrued expenses.

<b>Fair Value of Pension Plan Assets at December 31, 2015</b>				
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
	<b>(Dollars in millions)</b>			
Investment grade bonds (a)	\$ 841	1,045	—	\$ 1,886
High yield bonds (b)	—	544	13	557
Emerging market bonds (c)	208	232	1	441
Convertible bonds (d)	—	2	—	2
U.S. stocks (f)	1,201	—	—	1,201
Non-U.S. stocks (g)	1,127	1	—	1,128
Multi-asset strategies (m)	376	—	—	376
Derivatives (n)	2	(6)	—	(4)
Cash equivalents and short-term investments (o)	—	192	—	192
Total investments, excluding investments valued at NAV	<u>\$ 3,755</u>	<u>2,010</u>	<u>14</u>	<u>5,779</u>
Investments valued at NAV				5,293
Total pension plan assets				<u>\$ 11,072</u>

<b>Fair Value of Post-Retirement Plan Assets at December 31, 2015</b>				
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
	<b>(Dollars in millions)</b>			
Investment grade bonds (a)	\$ 2	1	—	\$ 3
High yield bonds (b)	—	1	—	1
U.S. stocks (f)	16	—	—	16
Non-U.S. stocks (g)	12	—	—	12
Emerging market stocks (h)	4	—	—	4
Cash equivalents and short-term investments (o)	—	4	—	4
Total investments, excluding investments valued at NAV	<u>\$ 34</u>	<u>6</u>	<u>—</u>	<u>40</u>
Investments valued at NAV				153
Total post-retirement plan assets				<u>\$ 193</u>

In 2015, we adopted Accounting Standards Update 2015-07 (“ASU 2015-07”), which retrospectively changed the disclosure requirements for certain investments that are valued based upon net asset value (“NAV”) as a practical expedient. ASU 2015-07 was issued to eliminate diversity among entities on what level in the fair value hierarchy such investments were assigned. Under ASU 2015-07, investments valued using NAV as a practical expedient are no longer assigned to a level in the fair value hierarchy. The value associated with these investments is disclosed in the reconciliation of the total investments measured at fair value shown below.

The table below presents the fair value of plan assets valued at NAV by category for our pension and post-retirement plans at December 31, 2016 and 2015.

	Fair Value of Plan Assets Valued at NAV			
	Pension Plans at December 31,		Post-Retirement Benefit Plans at December 31,	
	2016	2015	2016	2015
	(Dollars in millions)			
Investment grade bonds (a)	\$ 106	115	—	35
High yield bonds (b)	521	512	1	1
Emerging market bonds (c)	6	9	—	—
Diversified strategies (e)	522	516	1	54
U.S. stocks (f)	58	70	—	—
Non-U.S. stocks (g)	560	289	1	—
Emerging market stocks (h)	76	64	—	—
Private equity (i)	506	526	14	21
Private debt (j)	369	371	1	2
Market neutral hedge funds (k)	739	825	1	17
Directional hedge funds (k)	657	594	1	1
Real estate (l)	926	968	8	20
Multi-asset strategies (m)	412	386	—	—
Cash equivalents and short-term investments (o)	106	48	13	2
Total investments valued at NAV	\$ 5,564	5,293	41	153

The plans' assets are invested in various asset categories utilizing multiple strategies and investment managers. Interests in commingled funds are valued using the net asset value ("NAV") per unit of each fund. The NAV reported by the fund manager is based on the market value of the underlying investments owned by each fund, minus its liabilities, divided by the number of shares outstanding. Commingled funds can be redeemed at NAV, generally within a year of the financial statement date. Investments in private funds, primarily limited partnerships, represent long-term commitments with a fixed maturity date and are also valued at NAV. Valuation inputs for these private fund interests are generally based on assumptions and other information not observable in the market. The assumptions and valuation methodologies of the pricing vendors, account managers, fund managers and partnerships are monitored and evaluated for reasonableness. Below is an overview of the asset categories, the underlying strategies and valuation inputs used to value the assets in the preceding tables:

(a) *Investment grade bonds* represent investments in fixed income securities as well as commingled bond funds comprised of U.S. Treasury securities, agencies, corporate bonds, mortgage-backed securities, asset-backed securities and commercial mortgage-backed securities. Treasury securities are valued at the bid price reported in the active market in which the security is traded and are classified as Level 1. The valuation inputs of other investment grade bonds primarily utilize observable market information and are based on a spread to U.S. Treasury securities and consider yields available on comparable securities of issuers with similar credit ratings. The primary observable inputs include references to the new issue market for similar securities, the secondary trading markets and dealer quotes. Option adjusted spread models are utilized to evaluate securities such as asset backed securities that have early redemption features. These securities are classified as Level 2. The commingled funds are valued at NAV based on the market value of the underlying fixed income securities using the same valuation inputs previously described.

(b) *High yield bonds* represent investments in below investment grade fixed income securities as well as commingled high yield bond funds. The valuation inputs for the securities primarily utilize observable market information and are based on a spread to U.S. Treasury securities and consider yields available on comparable securities of issuers with similar credit ratings. These securities are primarily classified as Level 2. The commingled funds are valued at NAV based on the market value of the underlying high yield instruments using the same valuation inputs previously described.

(c) *Emerging market bonds* represent investments in securities issued by governments and other entities located in developing countries as well as registered mutual funds and commingled emerging market bond funds. The valuation inputs for the securities utilize observable market information and are primarily based on dealer quotes or a spread relative to the local government bonds. The registered mutual fund is classified as Level 1 while individual securities are classified as Level 2. The commingled funds are valued at NAV based on the market value of the underlying emerging market bonds using the same valuation inputs previously described.

(d) *Convertible bonds* primarily represent investments in corporate debt securities that have features that allow the debt to be converted into equity securities under certain circumstances. The valuation inputs for the individual convertible bonds primarily utilize observable market information including a spread to U.S. Treasuries and the value and volatility of the underlying equity security. Convertible bonds are classified as Level 1.

(e) *Diversified strategies* represent an investment in a commingled fund that primarily has exposures to global government, corporate and inflation linked bonds, global stocks and commodities. The commingled fund is valued at NAV based on the market value of the underlying investments. The valuation inputs utilize observable market information including published prices for exchange traded securities, bid prices for government bonds, and spreads and yields available for comparable fixed income securities with similar credit ratings.

(f) *U.S. stocks* represent investments in stocks of U.S. based companies as well as commingled U.S. stock funds. The valuation inputs for U.S. stocks are based on the last published price reported on the major stock market on which the securities are traded and are primarily classified as Level 1. The commingled funds are valued at NAV based on the market value of the underlying investments using the same valuation inputs described above.

(g) *Non-U.S. stocks* represent investments in stocks of companies based in developed countries outside the U.S. as well as commingled funds. The valuation inputs for non-U.S. stocks are based on the last published price reported on the major stock market on which the securities are traded and are primarily classified as Level 1. The commingled funds are valued at NAV based on the market value of the underlying investments using the same valuation inputs described above.

(h) *Emerging market stocks* represent investments in an exchange traded fund and commingled funds comprised of stocks of companies located in developing markets. Exchange traded funds are based on the last published price reported on the major stock market on which the securities are traded and are classified as Level 1. The commingled funds are valued at NAV based on the market value of the underlying investments using the same valuation inputs described previously for individual stocks.

(i) *Private equity* represents non-public investments in domestic and foreign buy out and venture capital funds. Private equity funds are primarily structured as limited partnerships and are valued according to the valuation policy of each partnership, subject to prevailing accounting and other regulatory guidelines. The partnerships are valued at NAV using valuation methodologies that give consideration to a range of factors, including but not limited to the price at which investments were acquired, the nature of the investments, market conditions, trading values on comparable public securities, current and projected operating performance, and financing transactions subsequent to the acquisition of the investments. These valuation methodologies involve a significant degree of judgment.

(j) *Private debt* represents non-public investments in distressed or mezzanine debt funds. Mezzanine debt instruments are debt instruments that are subordinated to other debt issues and may include embedded equity instruments such as warrants. Private debt funds are primarily structured as limited partnerships and are valued at NAV according to the valuation policy of each partnership, subject to prevailing accounting and other regulatory guidelines. The valuation of underlying fund investments are based on factors including the issuer's current and projected credit worthiness, the security's terms, reference to the securities of comparable companies, and other market factors. These valuation methodologies involve a significant degree of judgment.

(k) *Market neutral hedge funds* hold investments in a diversified mix of instruments that are intended in combination to exhibit low correlations to market fluctuations. These investments are typically combined with futures to achieve uncorrelated excess returns over various markets. *Directional hedge funds*—This asset category represents investments that may exhibit somewhat higher correlations to market fluctuations than the market neutral hedge funds. Investments in hedge funds include both direct investments and investments in diversified funds of funds. Hedge funds are valued at NAV based on the market value of the underlying investments which include publicly traded equity and fixed income securities and privately negotiated debt securities. The hedge funds are valued by third party administrators using the same valuation inputs previously described.



(l) *Real estate* represents investments in commingled funds and limited partnerships that invest in a diversified portfolio of real estate properties. These investments are valued at NAV according to the valuation policy of each fund or partnership, subject to prevailing accounting and other regulatory guidelines. The valuation inputs of the underlying properties are generally based on third-party appraisals that use comparable sales or a projection of future cash flows to determine fair value.

(m) *Multi-asset strategies* represent broadly diversified strategies that have the flexibility to tactically adjust exposures to different asset classes through time. This asset category includes investments in a registered mutual fund which is classified as Level 1 and a commingled fund which is valued at NAV based on the market value of the underlying investments.

(n) *Derivatives* include exchange traded futures contracts which are classified as Level 1, as well as privately negotiated over-the-counter swaps and options that are valued based on the change in interest rates or a specific market index and are classified as Level 2. The market values represent gains or losses that occur due to fluctuations in interest rates, foreign currency exchange rates, security prices, or other factors.

(o) *Cash equivalents and short-term investments* represent investments that are used in conjunction with derivatives positions or are used to provide liquidity for the payment of benefits or other purposes. The valuation inputs of securities are based on a spread to U.S. Treasury Bills, the Federal Funds Rate, or London Interbank Offered Rate and consider yields available on comparable securities of issuers with similar credit ratings and are classified as Level 2. The commingled funds are valued at NAV based on the market value of the underlying investments using the same valuation inputs described above.

*Concentrations of Risk:* Investments, in general, are exposed to various risks, such as significant world events, interest rate, credit, foreign currency and overall market volatility risk. These risks are managed by broadly diversifying assets across numerous asset classes and strategies with differing expected returns, volatilities and correlations. Risk is also broadly diversified across numerous market sectors and individual companies. Financial instruments that potentially subject the plans to concentrations of counterparty risk consist principally of investment contracts with high quality financial institutions. These investment contracts are typically collateralized obligations and/or are actively managed, limiting the amount of counterparty exposure to any one financial institution. Although the investments are well diversified, the value of plan assets could change materially depending upon the overall market volatility, which could affect the funded status of the plans.

The table below presents a rollforward of the pension plan assets valued using Level 3 inputs:

	Pension Plan Assets Valued Using Level 3 Inputs		
	High Yield Bonds	Emerging Market Bonds	Total
	(Dollars in millions)		
Balance at December 31, 2014	\$ 7	—	7
Net transfers	4	1	5
Acquisitions	4	—	4
Dispositions	(2)	—	(2)
Balance at December 31, 2015	13	1	14
Net transfers	(2)	—	(2)
Acquisitions	1	—	1
Dispositions	(1)	(1)	(2)
Balance at December 31, 2016	\$ 11	—	11

Certain gains and losses are allocated between assets sold during the year and assets still held at year-end based on transactions and changes in valuations that occurred during the year. These allocations also impact our calculation of net acquisitions and dispositions.

For the year ended December 31, 2016, the investment program produced actual gains on qualified pension and post-retirement plan assets of \$759 million as compared to expected returns of \$739 million for a difference of \$20 million. For the year ended December 31, 2015, the investment program produced actual losses on pension and post-retirement plan assets of \$158 million as compared to the expected returns of \$919 million for a difference of \$1.077 billion. The short-term annual returns on plan assets will

almost always be different from the expected long-term returns and the plans could experience net gains or losses, due primarily to the volatility occurring in the financial markets during any given year.

*Unfunded Status*

The following table presents the unfunded status of the pensions and post-retirement benefit plans:

	Pension Plans		Post-Retirement Benefit Plans	
	Years Ended December 31,		Years Ended December 31,	
	2016	2015	2016	2015
	(Dollars in millions)			
Benefit obligation	\$ (13,301)	(13,349)	(3,413)	(3,567)
Fair value of plan assets	10,892	11,072	53	193
Unfunded status	(2,409)	(2,277)	(3,360)	(3,374)
Current portion of unfunded status	\$ (6)	(5)	(236)	(135)
Non-current portion of unfunded status	\$ (2,403)	(2,272)	(3,124)	(3,239)

The current portion of our post-retirement benefit obligations is recorded on our consolidated balance sheets in accrued expenses and other current liabilities-salaries and benefits.

*Accumulated Other Comprehensive Loss-Recognition and Deferrals*

The following table presents cumulative items not recognized as a component of net periodic benefits expense as of December 31, 2015, items recognized as a component of net periodic benefits expense in 2016, additional items deferred during 2016 and cumulative items not recognized as a component of net periodic benefits expense as of December 31, 2016. The items not recognized as a component of net periodic benefits expense have been recorded on our consolidated balance sheets in accumulated other comprehensive loss:

	As of and for the Years Ended December 31,				
	2015	Recognition	Deferrals	Net	2016
		of Net Periodic Benefits Expense		Change in AOCL	
	(Dollars in millions)				
Accumulated other comprehensive loss:					
Pension plans:					
Net actuarial (loss) gain	\$ (2,857)	175	(466)	(291)	(3,148)
Prior service benefit (cost)	72	(8)	(2)	(10)	62
Deferred income tax benefit (expense)	1,070	(67)	188	121	1,191
Total pension plans	(1,715)	100	(280)	(180)	(1,895)
Post-retirement benefit plans:					
Net actuarial (loss) gain	(147)	—	10	10	(137)
Prior service (cost) benefit	(147)	20	—	20	(127)
Deferred income tax benefit (expense)	114	(8)	(4)	(12)	102
Total post-retirement benefit plans	(180)	12	6	18	(162)
Total accumulated other comprehensive loss	\$ (1,895)	112	(274)	(162)	(2,057)

The following table presents cumulative items not recognized as a component of net periodic benefits expense as of December 31, 2014, items recognized as a component of net periodic benefits expense in 2015, additional items deferred during 2015 and cumulative items not recognized as a component of net periodic benefits expense as of December 31, 2015. The items not recognized as a component of net periodic benefits expense have been recorded on our consolidated balance sheets in accumulated other comprehensive loss:

As of and for the Years Ended December 31,					
2014	Recognition of Net Periodic Benefits Expense	Deferrals	Net Change in AOCL	2015	
(Dollars in millions)					
Accumulated other comprehensive loss:					
Pension plans:					
Net actuarial (loss) gain	\$ (2,760)	161	(258)	(97)	(2,857)
Prior service (cost) benefit	(32)	5	99	104	72
Deferred income tax benefit (expense)	1,072	(63)	61	(2)	1,070
Total pension plans	(1,720)	103	(98)	5	(1,715)
Post-retirement benefit plans:					
Net actuarial (loss) gain	(277)	—	130	130	(147)
Prior service (cost) benefit	(166)	19	—	19	(147)
Deferred income tax benefit (expense)	171	(7)	(50)	(57)	114
Total post-retirement benefit plans	(272)	12	80	92	(180)
Total accumulated other comprehensive loss	\$ (1,992)	115	(18)	97	(1,895)

The following table presents estimated items to be recognized in 2017 as a component of net periodic benefit expense of the pension, non-qualified pension and post-retirement benefit plans:

	Pension Plans	Post- Retirement Plans
(Dollars in millions)		
Estimated recognition of net periodic (cost) benefit income in 2017:		
Net actuarial loss	\$ (202)	—
Prior service income (cost)	8	(20)
Deferred income tax benefit	74	8
Estimated net periodic benefit expense to be recorded in 2017 as a component of other comprehensive (loss) income	\$ (120)	(12)

#### *Medicare Prescription Drug, Improvement and Modernization Act of 2003*

We sponsor post-retirement health care plans with several benefit options that provide prescription drug benefits that we deem actuarially equivalent to or exceeding Medicare Part D. We recognize the impact of the federal subsidy received under the Medicare Prescription Drug, Improvement and Modernization Act of 2003 in the calculation of our post-retirement benefit obligation and net periodic post-retirement benefit expense.

## Other Benefit Plans

### Health Care and Life Insurance

We provide health care and life insurance benefits to essentially all of our active employees. We are largely self-funded for the cost of the health care plan. Our health care benefit expense for current employees was \$399 million, \$381 million and \$381 million for the years ended December 31, 2016, 2015 and 2014, respectively. Union-represented employee benefits are based on negotiated collective bargaining agreements. Employees contributed \$127 million, \$125 million and \$136 million for the years ended December 31, 2016, 2015 and 2014, respectively. Our group basic life insurance plans are fully insured and the premiums are paid by us.

### 401(k) Plans

We sponsor qualified defined contribution plans covering substantially all of our employees. Under these plans, employees may contribute a percentage of their annual compensation up to certain maximums, as defined by the plans and by the Internal Revenue Service ("IRS"). Currently, we match a percentage of employee contributions in cash. At December 31, 2016 and 2015, the assets of the plans included approximately 7 million shares and 8 million shares, respectively, of our common stock all of which were the result of the combination of previous employer match and participant directed contributions. We recognized expenses related to these plans of \$79 million, \$83 million and \$81 million and for the years ended December 31, 2016, 2015 and 2014, respectively.

### Deferred Compensation Plans

We sponsored non-qualified deferred compensation plans for various groups that included certain of our current and former highly compensated employees. The value of liabilities related to these plans was not significant.

### (10) Share-based Compensation

We maintain equity programs that allow our Board of Directors (through its Compensation Committee or our Chief Executive Officer as its delegate) to grant incentives to certain employees and our outside directors in any one or a combination of several forms, including incentive and non-qualified stock options, stock appreciation rights, restricted stock awards, restricted stock units and market and performance shares. Stock options generally expire ten years from the date of grant. Until June 30, 2014, we offered an employee stock purchase plan, which allowed eligible employees to purchase our common stock at a 15% discount based on the lower of the beginning or ending stock price during recurring six month offering periods.

#### Stock Options

The following table summarizes activity involving stock option awards for the year ended December 31, 2016:

	Number of Options (in thousands)	Weighted- Average Exercise Price
Outstanding and Exercisable at December 31, 2015	3,525	\$ 39.67
Exercised	(31)	26.34
Forfeited/Expired	(486)	37.96
Outstanding and Exercisable at December 31, 2016	<u>3,008</u>	<u>40.08</u>

The aggregate intrinsic value of our options outstanding and exercisable at December 31, 2016 was approximately \$1 million. The weighted-average remaining contractual term for such options was 1.0 years.

During 2016, we received net cash proceeds of approximately \$1 million in connection with our option exercises. The tax benefit realized from these exercises was less than \$1 million. The total intrinsic value of options exercised for the years ended December 31, 2015 and 2014, was \$4 million and \$9 million, respectively. The total intrinsic value of options exercised for the year ended December 31, 2016 was less than \$1 million.



### *Restricted Stock Awards*

For equity based awards that contain only service conditions for vesting, we calculate the award fair value based on the closing stock price on the accounting grant date. We also grant equity based restricted stock awards which contain market conditions or performance conditions, in addition to service conditions. For equity based restricted stock awards that contain market conditions, the award fair value is calculated through Monte-Carlo simulations. These awards, with service and market or performance conditions, represent the number of target shares for the award, as each recipient has the opportunity to ultimately receive a number of shares between 0% and 200% of the target restricted stock award. For the awards with market conditions, the percentage received depends on our total shareholder return versus that of selected peer companies during the three-year term of the award and for the awards with performance conditions, the percentage received depends upon the attainment of two financial performance targets during the three-year term of the award.

During the first quarter of 2016, we granted approximately 766 thousand shares of restricted stock to certain executive level employees as part of our long-term incentive program, of which approximately 306 thousand contained only service conditions and will vest on a straight-line basis on February 23, 2017, 2018 and 2019. The remaining awards contain service conditions and either market or performance conditions and are scheduled to vest on February 23, 2019.

During the first quarter of 2016, we also granted approximately 1.9 million shares to certain key employees as part of our annual equity compensation program, of which approximately 1.7 million contained only service conditions and will vest on a straight-line basis on February 25, 2017, 2018 and 2019. The remaining awards contain service conditions and either market or performance conditions and are scheduled to vest on February 25, 2019. During the first and third quarter of 2016, we granted shares to certain key employees as part of our long-term equity retention program. These awards will vest over a three to seven year period with approximately 113 thousand, 322 thousand and 209 thousand shares vesting on August 16, 2019, 2021 and 2023, respectively, and 22 thousand shares vesting on January 13, 2021 and 22 thousand shares vesting on January 13, 2023. The remaining awards granted throughout 2016 to certain other key employees and our outside directors were made as part of our equity compensation and retention programs. These awards require only service conditions for vesting and typically vest equally over a three year period.

During the first quarter of 2015, we granted approximately 496 thousand shares of restricted stock to certain executive-level employees as part of our long-term incentive program, of which approximately 198 thousand contained only service conditions and will vest on a straight-line basis on February 23, 2016, 2017 and 2018. The remaining awards contain service conditions and market or performance conditions and are scheduled to vest on February 23, 2018.

At the end of the first quarter of 2015, we granted approximately 1.2 million shares to certain key employees as part of our annual equity compensation program. These awards contained only service conditions and will vest on a straight-line basis on March 12, 2016, 2017 and 2018. During the third quarter of 2015 we granted shares to certain key employees as part of our long-term equity retention program. These awards will vest over a three to seven year period with approximately 193 thousand, 423 thousand and 230 thousand shares vesting on August 14, 2018, 2020 and 2022, respectively, and 55 thousand shares vesting equally on August 14, 2017, 2019, and 2021. The remaining awards granted throughout 2015 to certain other key employees and our outside directors were made as part of our equity compensation and retention programs. These awards require only service conditions for vesting and typically vest equally over a three year period.

During the first quarter of 2014, we granted approximately 440 thousand shares of restricted stock to certain executive-level employees as part of our long-term incentive program, of which approximately 250 thousand contained only service conditions and will vest on a straight-line basis on February 20, 2015, 2016 and 2017. The remaining awards contain service conditions and market or performance conditions and are scheduled to vest on February 20, 2017.

During the second quarter of 2014, we granted approximately 1.5 million shares to certain key employees as part of our annual equity compensation program. These awards contained only service conditions and will vest on a straight-line basis on March 26, 2015, 2016 and 2017. During the third quarter of 2014 we granted shares to certain key employees as part of our long-term equity retention program. These awards will vest over a three to seven year period with approximately 105 thousand, 325 thousand and 220 thousand vesting on August 4, 2017, 2019 and 2021, respectively. The remaining awards granted throughout 2014 to certain other key employees and our outside directors were made as part of our equity compensation and retention programs. These awards require only service conditions for vesting and typically vest equally over a three year period.

The following table summarizes activity involving restricted stock and restricted stock unit awards for the year ended December 31, 2016:

	Number of Shares	Weighted- Average Grant Date Fair Value
	(in thousands)	
Non-vested at December 31, 2015	4,902	33.86
Granted	3,564	30.83
Vested	(1,547)	34.82
Forfeited	(971)	33.23
Non-vested at December 31, 2016	<u>5,948</u>	31.89

During 2015, we granted 2.9 million shares of restricted stock and restricted stock unit awards at a weighted-average price of \$31.83. The total fair value of restricted stock that vested during 2016, 2015 and 2014, was \$47 million, \$59 million and \$53 million, respectively.

#### *Compensation Expense and Tax Benefit*

We recognize compensation expense related to our market and performance share-based awards with graded vesting that only have a service condition on a straight-line basis over the requisite service period for the entire award. Total compensation expense for all share-based payment arrangements for the years ended December 31, 2016, 2015 and 2014, was \$80 million, \$73 million and \$75 million, respectively. Our tax benefit recognized in the consolidated statements of operations for our share-based payment arrangements for the years ended December 31, 2016, 2015 and 2014, was \$31 million, \$28 million and \$29 million, respectively. At December 31, 2016, there was \$137 million of total unrecognized compensation expense related to our share-based payment arrangements, which we expect to recognize over a weighted-average period of 2.6 years.

**(11) Earnings Per Common Share**

Basic and diluted earnings per common share for the years ended December 31, 2016, 2015 and 2014 were calculated as follows:

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions, except per share amounts, shares in thousands)		
Income (Numerator):			
Net income	\$ 626	878	772
Earnings applicable to non-vested restricted stock	—	—	—
Net income applicable to common stock for computing basic earnings per common share	626	878	772
Net income as adjusted for purposes of computing diluted earnings per common share	\$ 626	878	772
Shares (Denominator):			
Weighted average number of shares:			
Outstanding during period	545,946	559,260	572,748
Non-vested restricted stock	(6,397)	(4,982)	(4,313)
Weighted average shares outstanding for computing basic earnings per common share	539,549	554,278	568,435
Incremental common shares attributable to dilutive securities:			
Shares issuable under convertible securities	10	10	10
Shares issuable under incentive compensation plans	1,120	805	1,294
Number of shares as adjusted for purposes of computing diluted earnings per common share	540,679	555,093	569,739
Basic earnings per common share	\$ 1.16	1.58	1.36
Diluted earnings per common share	\$ 1.16	1.58	1.36

Our calculation of diluted earnings per common share excludes shares of common stock that are issuable upon exercise of stock options when the exercise price is greater than the average market price of our common stock. We also exclude unvested restricted stock awards that are antidilutive as a result of unrecognized compensation cost. Such shares averaged 3.3 million, 3.1 million and 2.5 million for 2016, 2015 and 2014, respectively.

**(12) Fair Value Disclosure**

Our financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and long-term debt, excluding capital lease and other obligations. Due to their short-term nature, the carrying amounts of our cash and cash equivalents, accounts receivable and accounts payable approximate their fair values.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between independent and knowledgeable parties who are willing and able to transact for an asset or liability at the measurement date. We use valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs when determining fair value and then we rank the estimated values based on the reliability of the inputs used following the fair value hierarchy set forth by the FASB.

We determined the fair values of our long-term debt, including the current portion, based on quoted market prices where available or, if not available, based on discounted future cash flows using current market interest rates.

The three input levels in the hierarchy of fair value measurements are defined by the FASB generally as follows:

Input Level	Description of Input
-------------	----------------------

- Level 1      Observable inputs such as quoted market prices in active markets.
- Level 2      Inputs other than quoted prices in active markets that are either directly or indirectly observable.
- Level 3      Unobservable inputs in which little or no market data exists.

The following table presents the carrying amounts and estimated fair values of our long-term debt, excluding capital lease and other obligations, as well as the input level used to determine the fair values indicated below:

Input Level	As of December 31, 2016		As of December 31, 2015		
	Carrying Amount	Fair Value	Carrying Amount	Fair Value	
(Dollars in millions)					
Liabilities-Long-term debt, excluding capital lease and other obligations	2	\$ 19,553	19,639	19,800	19,473

### (13) Income Taxes

	Years Ended December 31,		
	2016	2015	2014
(Dollars in millions)			
Income tax expense was as follows:			
Federal			
Current	\$ 335	28	18
Deferred	5	329	305
State			
Current	27	40	26
Deferred	8	21	(14)
Foreign			
Current	26	16	3
Deferred	(7)	4	—
Total income tax expense	\$ 394	438	338

	Years Ended December 31,		
	2016	2015	2014
(Dollars in millions)			
Income tax expense was allocated as follows:			
Income tax expense in the consolidated statements of operations:			
Attributable to income	\$ 394	438	338
Stockholders' equity:			
Compensation expense for tax purposes in excess of amounts recognized for financial reporting purposes	(2)	(5)	(5)
Tax effect of the change in accumulated other comprehensive loss	(109)	59	(744)

The following is a reconciliation from the statutory federal income tax rate to our effective income tax rate:

	Years Ended December 31,		
	2016	2015	2014
	(Percentage of pre-tax income)		
Statutory federal income tax rate	35.0 %	35.0 %	35.0 %
State income taxes, net of federal income tax benefit	2.3 %	2.6 %	2.7 %
Change in liability for unrecognized tax position	0.2 %	0.4 %	0.4 %
Net foreign income taxes	0.1 %	0.7 %	0.4 %
Foreign dividend paid to a domestic parent company	1.8 %	— %	— %
Affiliate debt rationalization	— %	(2.6)%	— %
Research and development credits	(0.6)%	(2.1)%	— %
Loss on worthless investment in foreign subsidiary	— %	— %	(5.4)%
Other, net	(0.2)%	(0.7)%	(2.6)%
Effective income tax rate	38.6 %	33.3 %	30.5 %

The 2016 effective tax rate is 38.6% compared to 33.3% for 2015. The effective tax rate for the year ended December 31, 2016 reflects a tax impact of \$18 million from an intercompany dividend payment from one of our foreign subsidiaries to its domestic parent company that was made as part of our corporate restructuring in preparation for the sale of our colocation business. The 2015 rate reflects a tax benefit of approximately \$34 million related to affiliate debt rationalization, research and development tax credits of \$28 million for 2011 through 2015 and a \$16 million tax decrease due to changes in state taxes caused by apportionment changes, state tax rate changes and the changes in the expected utilization of net operating loss carryforwards ("NOLs"). The 2014 rate reflects a \$60 million tax benefit associated with a deduction for tax basis for worthless stock in a wholly-owned foreign subsidiary as a result of developments in bankruptcy proceedings involving its sole asset and a \$13 million tax decrease due to changes in the state taxes caused by apportionment changes, state tax rate changes and the changes in the expected utilization of NOLs.

The tax effects of temporary differences that gave rise to significant portions of the deferred tax assets and deferred tax liabilities were as follows:

	As of December 31,	
	2016	2015
	(Dollars in millions)	
Deferred tax assets		
Post-retirement and pension benefit costs	\$ 2,175	2,154
Net operating loss carryforwards	473	487
Other employee benefits	125	182
Other	342	458
Gross deferred tax assets	3,115	3,281
Less valuation allowance	(375)	(380)
Net deferred tax assets	2,740	2,901
Deferred tax liabilities		
Property, plant and equipment, primarily due to depreciation differences	(3,626)	(3,841)
Goodwill and other intangible assets	(2,577)	(2,588)
Other	—	(38)
Gross deferred tax liabilities	(6,203)	(6,467)
Net deferred tax liability	\$ (3,463)	(3,566)

Of the \$3.463 billion and \$3.566 billion net deferred tax liability at December 31, 2016 and 2015, respectively, \$3.471 billion and \$3.569 billion is reflected as a long-term liability and \$8 million and \$3 million is reflected as a net noncurrent deferred tax asset at December 31, 2016 and 2015, respectively.



At December 31, 2016, we had federal NOLs of \$61 million and state NOLs of \$11.9 billion. If unused, the NOLs will expire between 2017 and 2032; however, no significant amounts expire until 2021. At December 31, 2016, we had an immaterial amount of federal tax credits. Additionally, we had \$39 million (\$25 million net of federal income tax) of state investment tax credit carryforwards that will expire between 2017 and 2026 if not utilized. In addition, at December 31, 2016, we have fully utilized all remaining federal alternative minimum tax, or AMT, credits. Our acquisitions of Qwest and SAVVIS, Inc. ("Savvis") caused "ownership changes" within the meaning of Section 382 of the Internal Revenue Code ("Section 382"). As a result, our ability to use these NOLs and AMT credits are subject to annual limits imposed by Section 382. Despite this, we expect to use substantially all of these tax attributes to reduce our future federal tax liabilities, although the timing of that use will depend upon our future earnings and future tax circumstances.

We establish valuation allowances when necessary to reduce the deferred tax assets to amounts we expect to realize. As of December 31, 2016, a valuation allowance of \$375 million was established as it is more likely than not that this amount of net operating loss and tax credit carryforwards will not be utilized prior to expiration. Our valuation allowance at December 31, 2016 and 2015 is primarily related to state NOL carryforwards. This valuation allowance decreased by \$5 million during 2016.

A reconciliation of the change in our gross unrecognized tax benefits (excluding both interest and any related federal benefit) from January 1 to December 31 for 2016 and 2015 is as follows:

	2016	2015
	(Dollars in millions)	
Unrecognized tax benefits at beginning of year	\$ 15	17
Increase in tax positions taken in the current year	1	1
Increase in tax positions taken in the prior year	—	7
Decrease due to the reversal of tax positions taken in a prior year	—	(9)
Decrease from the lapse of statute of limitations	—	(1)
Unrecognized tax benefits at end of year	<u>\$ 16</u>	<u>15</u>

The total amount of unrecognized tax benefits that, if recognized, would impact the effective income tax rate was \$34 million and \$32 million at December 31, 2016 and 2015, respectively.

Our policy is to reflect interest expense associated with unrecognized tax benefits in income tax expense. We had accrued interest (presented before related tax benefits) of approximately \$35 million and \$33 million at December 31, 2016 and 2015, respectively.

We file income tax returns, including returns for our subsidiaries, with federal, state and local jurisdictions. Our uncertain income tax positions are related to tax years that are currently under or remain subject to examination by the relevant taxing authorities.

Beginning with the 2013 tax year, our federal consolidated returns are subject to annual examination by the IRS.

Our open income tax years by major jurisdiction are as follows at December 31, 2016:

Jurisdiction	Open Tax Years
Federal	2013—current
State	
Arizona	2010—current
Other states	2012—current

Since the period for assessing additional liability typically begins upon the filing of a return, it is possible that certain jurisdictions could assess tax for years prior to the open tax years disclosed above. Additionally, it is possible that certain jurisdictions in which we do not believe we have an income tax filing responsibility, and accordingly did not file a return, may attempt to assess a liability, or that other jurisdictions to which we pay taxes may attempt to assert that we owe additional taxes.

Based on our current assessment of various factors, including (i) the potential outcomes of these ongoing examinations, (ii) the expiration of statute of limitations for specific jurisdictions, (iii) the negotiated settlement of certain disputed issues, and (iv) the

administrative practices of applicable taxing jurisdictions, it is reasonably possible that the related unrecognized tax benefits for uncertain tax positions previously taken may decrease by up to \$11 million within the next 12 months. The actual amount of such decrease, if any, will depend on several future developments and events, many of which are outside our control.

**(14) Segment Information**

We are organized into operating segments based on customer type, business and consumer. These operating segments are our two reportable segments in our consolidated financial statements:

- *Business Segment.* Consists generally of providing strategic, legacy and data integration products and services to small, medium and enterprise business, wholesale and governmental customers, including other communication providers. Our strategic products and services offered to these customers include our MPLS, Ethernet, colocation, hosting (including cloud hosting and managed hosting), broadband, VoIP, information technology ("IT") and other ancillary services. Our legacy services offered to these customers primarily include local and long-distance voice, including the sale of unbundled network elements ("UNEs"), private line (including special access), switched access and other ancillary services. Our data integration offerings include the sale of telecommunications equipment located on customers' premises and related products and professional services, all of which are described further below under the heading "Products and Services Categories"; and
- *Consumer Segment.* Consists generally of providing strategic and legacy products and services to residential customers. Our strategic products and services offered to these customers include our broadband, video (including our Prism TV services) and other ancillary services. Our legacy services offered to these customers include local and long-distance voice and other ancillary services.

The following table summarizes our segment results for 2016, 2015 and 2014 based on the segment categorization we were operating under at December 31, 2016.

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
Total segment revenues	\$ 16,255	16,668	17,028
Total segment expenses	8,492	8,461	8,502
Total segment income	\$ 7,763	8,207	8,526
Total margin percentage	48%	49%	50%
Business segment:			
Revenues	\$ 10,352	10,646	11,030
Expenses	5,930	5,967	6,019
Income	\$ 4,422	4,679	5,011
Margin percentage	43%	44%	45%
Consumer segment:			
Revenues	\$ 5,903	6,022	5,998
Expenses	2,562	2,494	2,483
Income	\$ 3,341	3,528	3,515
Margin percentage	57%	59%	59%

**Changes in Segment Reporting**

We continually review, evaluate and refine our expense allocations to better reflect how we view and manage our operations, and as a result, during the first half of 2016, we implemented several changes with respect to the assignment of certain expenses to our reportable segments. We have recast our previously-reported segment results for the years ended December 31, 2015 and 2014, to conform to the current presentation. The nature of the most significant changes to segment expenses are as follows:

- Certain marketing and advertising expenses were reassigned from the business segment to the consumer segment;
- Certain service delivery costs were reassigned from the consumer segment to the business segment;

- Centralized human resources training costs were reassigned from the business and consumer segments to corporate overhead; and

- Marketing direct mail costs and certain printing expenses were reassigned from corporate overhead to the business and consumer segments.

For the year ended December 31, 2015, the segment expense recast resulted in an increase in consumer expenses of \$69 million and a decrease in business expenses of \$67 million. For the year ended December 31, 2014, the segment expense recast resulted in an increase in consumer expenses of \$63 million and a decrease in business expenses of \$70 million.

### Product and Service Categories

From time to time, we change the categorization of our products and services, and we may make similar changes in the future. During the second quarter of 2016, we determined that because of declines due to customer migration to other strategic products and services, certain of our business low-bandwidth data services, specifically our private line (including special access) services in our business segment, are more closely aligned with our legacy services than with our strategic services. As a result, we reflect these operating revenues as legacy services, and we have reclassified certain prior period amounts to conform to this change. The revision resulted in a reduction of revenue from strategic services and a corresponding increase in revenue from legacy services of \$1.586 billion and \$1.861 billion (net of \$9 million and \$33 million of deferred revenue included in other business legacy services) for the years ended December 31, 2015 and 2014, respectively. In addition, our business broadband services remain a strategic service and are now included in our other business strategic services.

We categorize our products, services and revenues among the following four categories:

- *Strategic services*, which include primarily broadband, MPLS, Ethernet, colocation, hosting (including cloud hosting and managed hosting), video (including our facilities-based video services, which we offer in 16 markets), VoIP, information technology and other ancillary services;
- *Legacy services*, which include primarily local and long-distance voice, including the sale of UNEs, private line (including special access), Integrated Services Digital Network ("ISDN") (which use regular telephone lines to support voice, video and data applications), switched access and other ancillary services;
- *Data integration*, which includes the sale of telecommunications equipment located on customers' premises and related products and professional services, such as network management, installation and maintenance of data equipment and building of proprietary fiber-optic broadband networks for our governmental and business customers; and
- *Other operating revenues*, which consist primarily of CAF support payments, USF support payments and USF surcharges. We receive federal support payments from both Phase 1 and Phase 2 of the CAF program, and support payments from both federal and state USF programs. These support payments are government subsidies designed to reimburse us for various costs related to certain telecommunications services, including the costs of deploying, maintaining and operating voice and broadband infrastructure in high-cost rural areas where we are not able to fully recover our costs from our customers. We also collect USF surcharges based on specific items we list on our customers' invoices to fund the FCC's universal service programs. We also generate other operating revenues from the leasing and subleasing of space in our office buildings, warehouses and other properties. Because we centrally manage the activities that generate these other operating revenues, these revenues are not included in our segment revenues.

Our operating revenues for our products and services consisted of the following categories for the years ended December 31, 2016, 2015 and 2014:

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
<b>Strategic services</b>			
Business high-bandwidth data services (1)	\$ 2,990	2,816	2,579
Business hosting services (2)	1,210	1,281	1,316
Other business strategic services (3)	703	624	558
Consumer broadband services (4)	2,689	2,611	2,469
Other consumer strategic services (5)	458	421	381
Total strategic services revenues	8,050	7,753	7,303
<b>Legacy services</b>			
Business voice services (6)	2,413	2,588	2,777
Business low-bandwidth data services (7)	1,382	1,594	1,893
Other business legacy services (8)	1,123	1,168	1,219
Consumer voice services (6)	2,442	2,676	2,865
Other consumer legacy services (9)	312	312	279
Total legacy services revenues	7,672	8,338	9,033
<b>Data integration</b>			
Business data integration	531	575	688
Consumer data integration	2	2	4
Total data integration revenues	533	577	692
<b>Other revenues</b>			
High-cost support revenue (10)	688	732	528
Other revenue (11)	527	500	475
Total other revenues	1,215	1,232	1,003
<b>Total revenues</b>	<b>\$ 17,470</b>	<b>17,900</b>	<b>18,031</b>

- (1) Includes MPLS and Ethernet revenue
- (2) Includes colocation, hosting (including cloud hosting and managed hosting) and hosting area network revenue
- (3) Includes primarily broadband, VoIP, video and IT services revenue
- (4) Includes broadband and related services revenue
- (5) Includes video and other revenue
- (6) Includes local and long-distance voice revenue
- (7) Includes private line (including special access) revenue
- (8) Includes UNEs, public access, switched access and other ancillary revenue
- (9) Includes other ancillary revenue
- (10) Includes CAF Phase 1, CAF Phase 2 and federal and state USF support revenue
- (11) Includes USF surcharges



We recognize revenues in our consolidated statements of operations for certain USF surcharges and transaction taxes that we bill to our customers. Our consolidated statements of operations also reflect the offsetting expense for the amounts we remit to the government agencies. The total amount of such surcharges and transaction taxes that we included in revenues aggregated to \$572 million, \$544 million and \$526 million for the years ended December 31, 2016, 2015 and 2014, respectively. These USF surcharges, where we record revenue, are included in "other" operating revenues and transaction taxes are included in "legacy services" revenues. We also act as a collection agent for certain other USF and transaction taxes that we are required by government agencies to bill our customers, for which we do not record any revenue or expense because we only act as a pass-through agent.

#### Allocations of Revenues and Expenses

Our segment revenues include all revenues from our strategic, legacy and data integration operations as described in more detail above. Segment revenues are based upon each customer's classification as either business or consumer. We report our segment revenues based upon all services provided to that segment's customers. Our segment expenses for our two segments include specific expenses incurred as a direct result of providing services and products to segment customers, along with selling, general and administrative expenses that are (i) directly associated with specific segment customers or activities, and (ii) allocated expenses which include network expenses, facilities expenses and other expenses such as fleet and real estate expenses. We do not assign depreciation and amortization expense or impairments to our segments, as the related assets and capital expenditures are centrally managed and are not monitored by or reported to the chief operating decision maker ("CODM") by segment. Generally speaking, severance expenses, restructuring expenses and certain centrally managed administrative functions (such as finance, information technology, legal and human resources) are not assigned to our segments. Interest expense is also excluded from segment results because we manage our financing on a consolidated basis and have not allocated assets or debt to specific segments. Other income and expense items are not monitored as a part of our segment operations and are therefore excluded from our segment results.

The following table reconciles segment income to net income for the years ended December 31, 2016, 2015 and 2014:

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
Total segment income	\$ 7,763	8,207	8,526
Other operating revenues	1,215	1,232	1,003
Depreciation and amortization	(3,916)	(4,189)	(4,428)
Other unassigned operating expenses	(2,731)	(2,645)	(2,691)
Other expenses, net	(1,311)	(1,289)	(1,300)
Income before income tax expense	1,020	1,316	1,110
Income tax expense	(394)	(438)	(338)
Net income	\$ 626	878	772

We do not have any single customer that provides more than 10% of our total consolidated operating revenues. Substantially all of our consolidated revenues come from customers located in the United States.

**(15) Quarterly Financial Data (Unaudited)**

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
(Dollars in millions, except per share amounts)					
<b>2016</b>					
Operating revenues	\$ 4,401	4,398	4,382	4,289	17,470
Operating income	694	650	595	392	2,331
Net income	236	196	152	42	626
Basic earnings per common share	0.44	0.36	0.28	0.08	1.16
Diluted earnings per common share	0.44	0.36	0.28	0.08	1.16
<b>2015</b>					
Operating revenues	\$ 4,451	4,419	4,554	4,476	17,900
Operating income	649	549	656	751	2,605
Net income	192	143	205	338	878
Basic earnings per common share	0.34	0.26	0.37	0.62	1.58
Diluted earnings per common share	0.34	0.26	0.37	0.62	1.58

During the fourth quarter of 2016, we recognized \$164 million of severance expenses and other one-time termination benefits associated with our workforce reductions and \$52 million of expenses related to our pending acquisition of Level 3.

During the third quarter of 2015, we recognized an incremental \$158 million of revenue associated with the FCC's CAF Phase 2 high-cost support program (primarily impacted by the one-time transitional payment), and an additional incremental \$57 million in the fourth quarter of 2015. During the fourth quarter of 2015, we also recognized a tax benefit of approximately \$34 million related to affiliate debt rationalization, research and development tax credits of \$28 million for 2011 through 2015, and a \$16 million tax decrease due to changes in state taxes caused by apportionment changes, state tax rate changes and the changes in the expected utilization of net operating loss carryforwards ("NOLs").

**(16) Commitments and Contingencies**

We are vigorously defending against all of the matters described below under the headings "Pending Matters" and "Other Proceedings and Disputes." As a matter of course, we are prepared both to litigate these matters to judgment, as well as to evaluate and consider all reasonable settlement opportunities. In this Note, when we refer to a class action as "putative" it is because a class has been alleged, but not certified in that matter. We have established accrued liabilities for these matters described below where losses are deemed probable and reasonably estimable.

***Pending Matters***

CenturyLink and the members of the CenturyLink Board have been named as defendants in a putative shareholder class action lawsuit filed on January 11, 2017 in the 4th Judicial District Court of the State of Louisiana, Ouachita Parish, captioned Jeffery Tomasulo v. CenturyLink, Inc., et al., Docket No. C-20170110. The complaint asserts, among other things, that the members of CenturyLink's Board allegedly breached their fiduciary duties to the CenturyLink shareholders in approving the Level 3 merger agreement and, more particularly, that: the consideration that CenturyLink agreed to pay to Level 3 stockholders in the transaction is allegedly unfairly high; the CenturyLink directors allegedly had conflicts of interest in negotiating and approving the transaction; and the disclosures set forth in our preliminary joint proxy statement/prospectus filed in December 2016 are insufficient in that they allegedly fail to contain material information concerning the transaction. The complaint seeks, among other things, a declaration that the members of the CenturyLink Board have breached their fiduciary duties, corrective disclosure, rescissory or other damages and equitable relief, including rescission of the transaction. On February 13, 2017, the parties entered into a memorandum of understanding providing for the settlement of the lawsuit. The proposed settlement is subject to court approval, among other conditions.

In *William Douglas Fulghum, et al. v. Embarq Corporation, et al.*, filed on December 28, 2007 in the United States District Court for the District of Kansas, a group of retirees filed a class action lawsuit challenging the decision to make certain modifications in retiree benefits programs relating to life insurance, medical insurance and prescription drug benefits, generally effective January 1, 2006 and January 1, 2008 (which, at the time of the modifications, was expected to reduce estimated future expenses for the subject benefits by more than \$300 million). Defendants include Embarq, certain of its benefit plans, its Employee Benefits Committee and the individual plan administrator of certain of its benefits plans. Additional defendants include Sprint Nextel and certain of its benefit plans. The court certified classes on the claims for vested benefits and age discrimination, but rejected class certification on the claims for breach of fiduciary duty. On October 14, 2011, the Fulghum lawyers filed a new, related lawsuit, *Abbott et al. v. Sprint Nextel et al.* In *Abbott*, approximately 1,500 plaintiffs alleged breach of fiduciary duty in connection with the changes in retiree benefits that were at issue in *Fulghum*. After extensive district court proceedings in *Fulghum*, and an interlocutory appeal to the United States Court of Appeals for the Tenth Circuit, defendants prevailed in 2015 on all age discrimination claims and on the majority of claims for vested benefits. The district court in *Fulghum* subsequently granted judgment in favor of defendants on all remaining vested benefits claims, and in July 2016 ordered that any affected class members could appeal this ruling. No appeal was taken, and all claims for vested benefits thus have lapsed. On August 31, 2016, the parties reached a settlement in principle on all remaining claims in *Fulghum* and *Abbott*. Assuming its terms are successfully implemented, we believe the settlement is likely to be final in mid 2017. We have accrued a liability that we believe is probable for these matters; the amount is not material to our consolidated financial statements.

Subsidiaries of CenturyLink, Inc. are among hundreds of companies in an industry-wide dispute, raised in nearly 100 federal lawsuits (filed between 2014 and 2016) that have been consolidated in the United States District Court for the District of Northern Texas for pretrial procedures. The disputes relate to switched access charges that local exchange carriers ("LECs") collect from interexchange carriers ("IXCs") for IXCs' use of LEC's access services. In the lawsuits, three IXCs, Sprint Communications Company L.P. ("Sprint"), affiliates of Verizon Communications Inc. ("Verizon") and affiliates of Level 3 Communications LLC ("Level 3"), assert that federal and state laws bar LECs from collecting access charges when IXCs exchange certain types of calls between mobile and wireline devices that are routed through an IXC. Some of these IXCs have asserted claims seeking refunds of payments for access charges previously paid and relief from future access charges. In addition, Level 3 has ceased paying switched access charges on these calls.

In November 2015, the federal court agreed with the LECs and rejected the IXCs' contention that federal law prohibits these particular access charges, and also allowed the IXCs to refile state-law claims. Since then, many of the LECs and IXCs have filed revised pleadings and additional motions, which remain pending. Separately, some of the defendants, including CenturyLink, Inc.'s LECs, have petitioned the FCC to address these issues on an industry-wide basis.

As both an IXC and a LEC, we both pay and assess significant amounts of the charges in question. The outcome of these disputes and lawsuits, as well as any related regulatory proceedings that could ensue, are currently not predictable. If we are required to stop assessing these charges or to pay refunds of any such charges, our financial results could be negatively affected.

CenturyLink, Inc. and several of its subsidiaries are defendants in lawsuits filed over the past few years in the Circuit Court of St. Louis County, Missouri by numerous Missouri municipalities alleging underpayment of taxes. These municipalities are seeking, among other things, (i) a declaratory judgment regarding the extent of our obligations to pay certain business license and gross receipts taxes and (ii) a monetary award of back taxes covering 2007 to the present, plus penalties and interest. In an April 2016 ruling in connection with one of these pending cases, the court made findings which, if not overturned, will result in a tax liability to us well in excess of the contingent liability we have established. Following further proceedings at the district court, we plan to file an appeal and continue to vigorously defend against these claims. For a variety of reasons, we expect the outcome of our appeal to significantly reduce our ultimate exposure, although we can provide no assurances to this effect.

### *Other Proceedings and Disputes*

From time to time, we are involved in other proceedings incidental to our business, including patent infringement allegations, administrative hearings of state public utility commissions relating primarily to our rates or services, actions relating to employee claims, various tax issues, environmental law issues, grievance hearings before labor regulatory agencies and miscellaneous third party tort actions.

We are currently defending several patent infringement lawsuits asserted against us by non-practicing entities, many of which are seeking substantial recoveries. These cases have progressed to various stages and one or more may go to trial in the coming 24 months if they are not otherwise resolved. Where applicable, we are seeking full or partial indemnification from our vendors and suppliers. As with all litigation, we are vigorously defending these actions and, as a matter of course, are prepared to litigate these matters to judgment, as well as to evaluate and consider all reasonable settlement opportunities.

We are subject to various foreign, federal, state and local environmental protection and health and safety laws. From time to time, we are subject to judicial and administrative proceedings brought by various governmental authorities under these laws. Several such proceedings are currently pending, but none is reasonably expected to exceed \$100,000 in fines and penalties.

The outcome of these other proceedings is not predictable. However, based on current circumstances, we do not believe that the ultimate resolution of these other proceedings, after considering available defenses and any insurance coverage or indemnification rights, will have a material adverse effect on our financial position, results of operations or cash flows.

### *Capital Leases*

We lease certain facilities and equipment under various capital lease arrangements. Depreciation of assets under capital leases is included in depreciation and amortization expense in our consolidated statements of operations. Payments on capital leases are included in repayments of long-term debt, including current maturities in our consolidated statements of cash flows.

The tables below summarize our capital lease activity:

	Years Ended December 31,		
	2016	2015	2014
	(Dollars in millions)		
Assets acquired through capital leases	45	17	37
Depreciation expense	70	96	126
Cash payments towards capital leases	58	89	118

	As of December 31,	
	2016	2015
	(Dollars in millions)	
Assets included in property, plant and equipment	705	722
Accumulated depreciation	351	352

The future annual minimum payments under capital lease arrangements as of December 31, 2016 were as follows:

	<b>Future Minimum Payments</b>	
	<u>(Dollars in millions)</u>	
Capital lease obligations:		
2017	\$	94
2018		91
2019		70
2020		46
2021		43
2022 and thereafter		170
Total minimum payments		<u>514</u>
Less: amount representing interest and executory costs		(123)
Present value of minimum payments		<u>391</u>
Less: current portion		(69)
Long-term portion	\$	<u><u>322</u></u>

If, as anticipated, we sell our colocation business and data centers in the manner discussed in Note 3—Pending Sale of Colocation Business and Data Centers, \$305 million of the capital lease obligations as of December 31, 2016 will be assumed by the Purchaser. The future annual minimum payments under capital lease arrangements for the colocation operations as of December 31, 2016 were as follows:

	<b>Future Minimum Payments</b>	
	<u>(Dollars in millions)</u>	
Capital lease obligations:		
2017	\$	60
2018		62
2019		52
2020		39
2021		40
2022 and thereafter		145
Total minimum payments		<u>398</u>
Less: amount representing interest and executory costs		(93)
Present value of minimum payments	\$	<u><u>305</u></u>

The present value of the minimum payments under capital lease arrangements for the colocation operations is included in "Current liabilities associated with assets held for sale" on our consolidated balance sheets. See Note 3—Pending Sale of Colocation Business and Data Centers for additional information.

### *Operating Leases*

CenturyLink leases various equipment, office facilities, retail outlets, switching facilities and other network sites. These leases, with few exceptions, provide for renewal options and escalations that are either fixed or based on the consumer price index. Any rent abatements, along with rent escalations, are included in the computation of rent expense calculated on a straight-line basis over the lease term. The lease term for most leases includes the initial non-cancelable term plus any term under renewal options that are reasonably assured. For the years ended December 31, 2016, 2015 and 2014, our gross rental expense was \$482 million, \$467 million and \$446 million, respectively. We also received sublease rental income for the years ended December 31, 2016, 2015 and 2014 of \$12 million, \$12 million and \$14 million, respectively.



At December 31, 2016, our future rental commitments for operating leases were as follows:

	<b>Future Minimum Payments</b>	
	<b>(Dollars in millions)</b>	
2017	\$	295
2018		276
2019		249
2020		226
2021		162
2022 and thereafter		1,049
Total future minimum payments <sup>(1)</sup>	<b>\$</b>	<b>2,257</b>

(1) Minimum payments have not been reduced by minimum sublease rentals of \$77 million due in the future under non-cancelable subleases.

If, as anticipated, we sell our colocation business and data centers in the manner discussed in Note 3—Pending Sale of Colocation Business and Data Centers, \$750 million of the operating leases future rental commitments as of December 31, 2016 will be assumed by the Purchaser. The future rental commitments under operating leases for the colocation operations as of December 31, 2016 were as follows:

	<b>Future Minimum Payments</b>	
	<b>(Dollars in millions)</b>	
2017	\$	89
2018		84
2019		71
2020		68
2021		68
2022 and thereafter		370
Total future minimum payments	<b>\$</b>	<b>750</b>

#### *Purchase Commitments*

We have several commitments primarily for marketing activities and support services from a variety of vendors to be used in the ordinary course of business totaling \$427 million at December 31, 2016. Of this amount, we expect to purchase \$166 million in 2017, \$153 million in 2018 through 2019, \$41 million in 2020 through 2021 and \$67 million in 2022 and thereafter. These amounts do not represent our entire anticipated purchases in the future, but represent only those items for which we were contractually committed as of December 31, 2016.

If, as anticipated, we sell our colocation business and data centers in the manner discussed in Note 3—Pending Sale of Colocation Business and Data Centers, \$80 million of the purchase commitments as of December 31, 2016 will be assumed by the Purchaser.

**(17) Other Financial Information****Other Current Assets**

The following table presents details of other current assets in our consolidated balance sheets:

	As of December 31,	
	2016	2015
	(Dollars in millions)	
Prepaid expenses	\$ 206	238
Materials, supplies and inventory	134	144
Deferred activation and installation charges	101	105
Other	106	86
Total other current assets	<u>\$ 547</u>	<u>573</u>

**Selected Current Liabilities**

Current liabilities reflected in our consolidated balance sheets include accounts payable and other current liabilities as follows:

	As of December 31,	
	2016	2015
	(Dollars in millions)	
Accounts payable	\$ 1,179	968
Other current liabilities:		
Accrued rent	\$ 31	32
Legal reserves	30	20
Other	152	168
Total other current liabilities	<u>\$ 213</u>	<u>220</u>

Included in accounts payable at December 31, 2016 and 2015, were (i) \$56 million and \$68 million, respectively, representing book overdrafts and (ii) \$196 million and \$94 million, respectively, associated with capital expenditures.

**(18) Labor Union Contracts**

Approximately 38% of our employees are members of various bargaining units represented by the Communication Workers of America and the International Brotherhood of Electrical Workers. We believe that relations with our employees continue to be generally good. Approximately 12,000, or 30%, of our employees are subject to collective bargaining agreements that are scheduled to expire in 2017, including approximately 11,000, or 28%, of our employees that are subject to collective bargaining agreements that are scheduled to expire October 7, 2017.

**(19) Accumulated Other Comprehensive Loss**

The table below summarizes changes in accumulated other comprehensive loss recorded on our consolidated balance sheet by component for the year ended December 31, 2016:

	Pension Plans	Post-Retirement Benefit Plans	Foreign Currency Translation Adjustment and Other	Total
Balance at December 31, 2015	\$ (1,715)	(180)	(39)	(1,934)
Other comprehensive income (loss) before reclassifications	(280)	6	(22)	(296)
Amounts reclassified from accumulated other	100	12	1	113

7/20/2017

Document

comprehensive income

Net current-period other comprehensive income (loss)

Balance at December 31, 2016

	<u>(180)</u>	<u>18</u>	<u>(21)</u>	<u>(183)</u>
	<u>\$ (1,895)</u>	<u>(162)</u>	<u>(60)</u>	<u>(2,117)</u>

131

The table below presents further information about our reclassifications out of accumulated other comprehensive loss by component for the year ended December 31, 2016:

Year Ended December 31, 2016	Decrease (Increase) in Net Income	Affected Line Item in Consolidated Statement of Operations or Footnote Where Additional Information is Presented If The Amount is not Recognized in Net Income in Total
(Dollars in millions)		
Amortization of pension & post-retirement plans		
Net actuarial loss	\$ 175	See Note 9—Employee Benefits
Prior service cost	12	See Note 9—Employee Benefits
Total before tax	187	
Income tax expense (benefit)	(75)	Income tax expense
Insignificant items	1	
Net of tax	\$ 113	

The table below summarizes changes in accumulated other comprehensive loss recorded on our consolidated balance sheet by component for the year ended December 31, 2015:

	Pension Plans	Post-Retirement Benefit Plans	Foreign Currency Translation Adjustment and Other	Total
(Dollars in millions)				
Balance at December 31, 2014	\$ (1,720)	(272)	(25)	(2,017)
Other comprehensive income (loss) before reclassifications	(98)	80	(14)	(32)
Amounts reclassified from accumulated other comprehensive income	103	12	—	115
Net current-period other comprehensive income (loss)	5	92	(14)	83
Balance at December 31, 2015	\$ (1,715)	(180)	(39)	(1,934)

The table below presents further information about our reclassifications out of accumulated other comprehensive loss by component for the year ended December 31, 2015:

Year Ended December 31, 2015	Decrease (Increase) in Net Loss	Affected Line Item in Consolidated Statement of Operations or Footnote Where Additional Information is Presented If The Amount is not Recognized in Net Income in Total
(Dollars in millions)		
Amortization of pension & post-retirement plans		
Net actuarial loss	\$ 161	See Note 9—Employee Benefits
Prior service cost	24	See Note 9—Employee Benefits
Total before tax	185	
Income tax expense (benefit)	(70)	Income tax expense
Net of tax	\$ 115	

**(20) Dividends**

Our Board of Directors declared the following dividends payable in 2016 and 2015:

<b>Date Declared</b>	<b>Record Date</b>	<b>Dividend Per Share</b>	<b>Total Amount</b>	<b>Payment Date</b>
			(in millions)	
November 15, 2016	11/28/2016	\$ 0.540	\$ 294	12/12/2016
August 23, 2016	9/2/2016	0.540	295	9/16/2016
May 18, 2016	5/31/2016	0.540	294	6/14/2016
February 23, 2016	3/4/2016	0.540	295	3/18/2016
November 10, 2015	11/24/2015	0.540	293	12/8/2015
August 25, 2015	9/8/2015	0.540	300	9/22/2015
May 20, 2015	6/2/2015	0.540	303	6/16/2015
February 23, 2015	3/6/2015	0.540	303	3/20/2015

The declaration of dividends is solely at the discretion of our Board of Directors, which may change or terminate our dividend practice at any time for any reason without prior notice.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

**ITEM 9A. CONTROLS AND PROCEDURES****Disclosure Controls and Procedures**

The Company maintains disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act (the "Exchange Act")) designed to provide reasonable assurance that the information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms. These include controls and procedures designed to ensure that this information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Management, with the participation of our Chief Executive Officer, Glen F. Post, III, and our Chief Financial Officer, R. Stewart Ewing, Jr., evaluated the effectiveness of the Company's disclosure controls and procedures as of December 31, 2016. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of December 31, 2016, at the reasonable assurance level.

The effectiveness of our or any system of disclosure controls and procedures is subject to certain limitations, including the exercise of judgment in designing, implementing and evaluating the controls and procedures, the assumptions used in identifying the likelihood of future events and the inability to eliminate misconduct completely. As a result, there can be no assurance that our disclosure controls and procedures will detect all errors or fraud. By their nature, our or any system of disclosure controls and procedures can provide only reasonable assurance regarding management's control objectives.

**Changes in Internal Control Over Financial Reporting**

There were no changes in our internal control over financial reporting during the quarter ended December 31, 2016 that materially affected, or that we believe are reasonably likely to materially affect, our internal control over financial reporting.

## Internal Control Over Financial Reporting

### *Management's Report on Internal Control Over Financial Reporting*

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act), a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles in the United States. Under the supervision and with the participation of management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control-Integrated Framework (2013) issued by the COSO. Based on our evaluation under the framework of COSO, management concluded that our internal control over financial reporting was effective at December 31, 2016. The effectiveness of our internal control over financial reporting at December 31, 2016 has been audited by KPMG LLP, as stated in their report. See the Report of Independent Registered Public Accounting Firm on our internal control over financial reporting in Item 8, which is incorporated herein by reference.

### *Management's Report on the Consolidated Financial Statements*

Management has prepared and is responsible for the integrity and objectivity of our consolidated financial statements for the year ended December 31, 2016. The consolidated financial statements included in this annual report have been prepared in accordance with accounting principles generally accepted in the United States and necessarily include amounts determined using our best judgments and estimates.

Our consolidated financial statements have been audited by KPMG LLP, an independent registered public accounting firm, who have expressed their opinion with respect to the fairness of the consolidated financial statements. Their audit was conducted in accordance with standards of the Public Company Accounting Oversight Board (United States).

/s/ Glen F. Post, III

Glen F. Post, III

Chief Executive Officer, President and Director

/s/ R. Stewart Ewing, Jr.

R. Stewart Ewing, Jr.

Executive Vice President, Chief Financial Officer and Assistant Secretary

February 22, 2017

## ITEM 9B. OTHER INFORMATION

None.

## PART III

### ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by Item 10 is incorporated by reference to the Proxy Statement.

### ITEM 11. EXECUTIVE COMPENSATION

The information required by Item 11 is incorporated by reference to the Proxy Statement.

## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

### Equity Compensation Plan Information

The following table provides information as of December 31, 2016 about our equity compensation plans under which Common Shares are authorized for issuance:

	Number of securities to be issued upon exercise of outstanding options and rights (a)	Weighted-average exercise price of outstanding options and rights (b)	Number of securities remaining available for future issuance under plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by shareholders	2,000,623 <sup>(1)</sup>	\$ 45.75 <sup>(2)</sup>	17,904,466
Equity compensation plans not approved by shareholders <sup>(3)</sup>	2,282,277	38.28	—
<b>Totals</b>	<b>4,282,900 <sup>(1)</sup></b>	<b>\$ 40.08 <sup>(2)</sup></b>	<b>17,904,466</b>

(1) These amounts include restricted stock units, which represent the difference between the number of shares of restricted stock subject to market conditions granted at target and the maximum possible payout for these awards. Depending on performance, the actual share payout of these awards may range between 0-200% of target.

(2) The amounts in column (a) include restricted stock units, which do not have an exercise price. Consequently, those awards were excluded from the calculation of this exercise price.

(3) These amounts represent common shares to be issued upon exercise of options that were assumed in connection with certain acquisitions.

The balance of the information required by Item 12 is incorporated by reference to the Proxy Statement.

## ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

The information required by Item 13 is incorporated by reference to the Proxy Statement.

## ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by Item 14 is incorporated by reference to the Proxy Statement.

## PART IV

## ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

Exhibits identified in parentheses below are on file with the SEC and are incorporated herein by reference. All other exhibits are provided as part of this electronic submission.

Exhibit Number	Description
2.1	Agreement and Plan of Merger, dated as of October 31, 2016, by and among CenturyLink, Inc., Level 3 Communications, Inc., Wildcat Merger Sub 1 LLC and WWG Merger Sub LLC (incorporated by reference to Exhibit 2.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on November 3, 2016).
3.1	Amended and Restated Articles of Incorporation of CenturyLink, Inc., as amended through May 23, 2012 (incorporated by reference to Exhibit 3.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on May 30, 2012).
3.2	Bylaws of CenturyLink, Inc., as amended and restated through February 4, 2016 (incorporated by reference to Exhibit 3.2 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on February 29, 2016).
4.1	Form of common stock certificate (incorporated by reference to Exhibit 4.10 of CenturyLink, Inc.'s Registration Statement on Form S-3 filed with the Securities and Exchange Commission on March 2, 2012 (Registration No. 333-179888)).
4.2	Instruments relating to CenturyLink, Inc.'s Revolving Credit Facility, <ol style="list-style-type: none"> <li>a. Amended and Restated Credit Agreement, dated as of April 6, 2012, by and among CenturyLink, Inc. and the lenders and agents named therein (incorporated by reference to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on April 11, 2012, as amended by the First Amendment to Amended and Restated Credit Agreement, dated as of December 3, 2014, among CenturyLink, Inc. and the lenders and agents named therein (incorporated by reference to Exhibit 4.3 of CenturyLink's Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on December 5, 2014).</li> <li>b. Guarantee Agreement, dated as of April 6, 2012, by and among the original guarantors named therein (incorporated by reference to Exhibit 4.2 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on April 11, 2012), as assumed by two additional guarantors under an assumption agreement, dated as of May 23, 2013 (incorporated by reference to Exhibit 4.2(b) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2013 (File No. 001-07784) filed with the Securities and Exchange Commission on August 8, 2013), as amended by the Amendment to Guarantee Agreement and Reaffirmation Agreement, dated as of December 3, 2014, among CenturyLink, Inc. and the affiliated guarantors named therein (incorporated by reference to Exhibit 4.4 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on December 5, 2014).</li> </ol>
4.3	Instruments relating to CenturyLink, Inc.'s Term Loan, <ol style="list-style-type: none"> <li>a. Credit Agreement, dated as of April 18, 2012, by and among CenturyLink, Inc., the several banks and other financial institutions or entities from time to time parties thereto, and CoBank, ACB, as administrative agent (incorporated by reference to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on April 20, 2012), as amended by the amendment dated as of March 13, 2015.</li> <li>b. Guarantee Agreement, dated as of April 18, 2012, by and among the original guarantors named therein (incorporated by reference to Exhibit 4.2 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on April 20, 2012), as assumed by two additional guarantors under an assumption agreement, dated as of May 23, 2013 (incorporated by reference to Exhibit 4.3(b) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2013 (File No. 001-07784) filed with the Securities and Exchange Commission on August 8, 2013), as amended by the amendment dated as of March 13, 2015 (incorporated by reference to Exhibit 4.3(b) of CenturyLink's Quarterly Report on Form 10-Q for the period ended March 31, 2015 (File No. 001-07784) filed with the Securities and Exchange Commission on May 6, 2015).</li> </ol>



Exhibit Number	Description
----------------	-------------

- |     |   |
|-----|---|
| 4.4 | Instruments relating to CenturyLink, Inc.'s public senior debt. <sup>(1)</sup>  |
| a.  | <p>Indenture, dated as of March 31, 1994, by and between Century Telephone Enterprises, Inc. (currently named CenturyLink, Inc.) and Regions Bank (successor-in-interest to First American Bank &amp; Trust of Louisiana), as Trustee.</p> <p>(i). Form of 7.2% Senior Notes, Series D, due 2025 (incorporated by reference to Exhibit 4.27 of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 1995 (File No. 001-07784) filed with the Securities and Exchange Commission on March 18, 1996).</p> <p>(ii). Form of 6.875% Debentures, Series G, due 2028, (incorporated by reference to Exhibit 4.9 of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 1997 (File No. 001-07784) filed with the Securities and Exchange Commission on March 16, 1998).</p>             |
| b.  | <p>Fourth Supplemental Indenture, dated as of March 26, 2007, by and between CenturyTel, Inc. (currently named CenturyLink, Inc.) and Regions Bank, as Trustee, designating and outlining the terms and conditions of CenturyLink's 6.0% Senior Notes, Series N, due 2017 and 5.5% Senior Notes, Series O, due 2013 (incorporated by reference to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on March 29, 2007).</p> <p>(i). Form of 6.0% Senior Notes, Series N, due 2017 and 5.5% Senior Notes, Series O, due 2013 (incorporated by reference to Exhibit A to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on March 29, 2007).</p>                |
| c.  | <p>Fifth Supplemental Indenture, dated as of September 21, 2009, by and between CenturyTel, Inc. (currently named CenturyLink, Inc.) and Regions Bank, as Trustee, designating and outlining the terms and conditions of CenturyLink's 7.60% Senior Notes, Series P, due 2039 and 6.15% Senior Notes, Series Q, due 2019 (incorporated by reference to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on September 22, 2009).</p> <p>(i). Form of 7.60% Senior Notes, Series P, due 2039 and 6.15% Senior Notes, Series Q, due 2019 (incorporated by reference to Exhibit A to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on September 22, 2009).</p> |
| d.  | <p>Sixth Supplemental Indenture, dated as of June 16, 2011, by and between CenturyLink, Inc. and Regions Bank, as Trustee, designating and outlining the terms and conditions of CenturyLink's 5.15% Senior Notes, Series R, due 2017 and 6.45% Senior Notes, Series S, due 2021 (incorporated by reference to Exhibit 4.2 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on June 16, 2011).</p> <p>(i). Form of 5.15% Senior Notes, Series R, due 2017 and 6.45% Senior Notes, Series S, due 2021 (incorporated by reference to Exhibit A to Exhibit 4.2 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on June 16, 2011).</p>   |
| e.  | <p>Seventh Supplemental Indenture, dated as of March 12, 2012, by and between CenturyLink, Inc. and Regions Bank, as Trustee, designating and outlining the terms and conditions of CenturyLink's 5.80% Senior Notes, Series T, due 2022 and 7.65% Senior Notes, Series U, due 2042 (incorporated by reference to Exhibit 4.1 of CenturyLink's Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on March 12, 2012).</p> <p>(i). Form of 5.80% Senior Notes, Series T, due 2022 and 7.65% Senior Notes, Series U, due 2042 (incorporated by reference to Exhibit A to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on March 12, 2012).</p>  |
| f.  | <p>Eighth Supplemental Indenture, dated as of March 21, 2013, by and between CenturyLink, Inc. and Regions Bank, as Trustee, designating and outlining the terms and conditions of CenturyLink's 5.625% Senior Notes, Series V, due 2020 (incorporated by reference to Exhibit 4.1 of CenturyLink's Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on March 21, 2013).</p> <p>(i). Form of 5.625% Senior Notes, Series V, due 2020 (incorporated by reference to Exhibit A to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the</p>  |

Securities and Exchange Commission on March 21, 2013).

Exhibit Number	Description
----------------	-------------

- |      |   |
|------|---|
| g.   | Ninth Supplemental Indenture, dated as of November 27, 2013, by and between CenturyLink, Inc. and Regions Bank, as Trustee, designating and outlining the terms and conditions of CenturyLink's 6.75% Senior Notes, Series W, due 2023 (incorporated by reference to Exhibit 4.1 of CenturyLink's Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on November 27, 2013).  |
| (i). | Form of 6.75% Senior Notes, Series W, due 2023 (incorporated by reference to Exhibit A to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on November 27, 2013).   |
| h.   | Tenth Supplemental Indenture, dated as of March 19, 2015, by and between CenturyLink, Inc. and Regions Bank, as Trustee, designating and outlining the terms and conditions of CenturyLink's 5.625% Senior Notes, Series X, due 2025 (incorporated by reference to Exhibit 4.1 of CenturyLink's Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on March 19, 2015).   |
| (i). | Form of 5.625% Senior Notes, Series X, due 2025 (incorporated by reference to Exhibit A to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on March 19, 2015).   |
| i.   | Eleventh Supplemental Indenture, dated as of April 6, 2016, by and between CenturyLink, Inc. and Regions Bank, as Trustee, designating and outlining the terms and conditions of CenturyLink's 7.5% Senior Notes, Series Y, due 2024 (incorporated by reference to Exhibit 4.1 of CenturyLink's Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on April 6, 2016).  |
| (i). | Form of 7.5% Senior Notes, Series Y, due 2024 (incorporated by reference to Exhibit A to Exhibit 4.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on April 6, 2016).  |
| 4.5  | Instruments relating to indebtedness of Qwest Communications International, Inc. and its subsidiaries. <sup>(1)</sup>   |
| a.   | Indenture, dated as of April 15, 1990, by and between The Mountain States Telephone and Telegraph Company (currently named Qwest Corporation) and The First National Bank of Chicago (incorporated by reference to Exhibit 4.2 of Qwest Corporation's annual report on Form 10-K for the year ended December 31, 2002 (File No. 001-03040) filed with the Securities and Exchange Commission on January 13, 2004).  |
| (i). | First Supplemental Indenture, dated as of April 16, 1991, by and between U S WEST Communications, Inc. (currently named Qwest Corporation) and The First National Bank of Chicago (incorporated by reference to Exhibit 4.3 of Qwest Corporation's annual report on Form 10-K for the year ended December 31, 2002 (File No. 001-03040) filed with the Securities and Exchange Commission on January 13, 2004).   |
| b.   | Indenture, dated as of April 15, 1990, by and between Northwestern Bell Telephone Company (predecessor to Qwest Corporation) and The First National Bank of Chicago (incorporated by reference to Exhibit 4.5(b) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2012 (File No. 001-07784) filed with the Securities and Exchange Commission on May 10, 2012).  |
| (i). | First Supplemental Indenture, dated as of April 16, 1991, by and between U S WEST Communications, Inc. (currently named Qwest Corporation) and The First National Bank of Chicago (incorporated by reference to Exhibit 4.3 of Qwest Corporation's annual report on Form 10-K for the year ended December 31, 2002 (File No. 001-03040) filed with the Securities and Exchange Commission on January 13, 2004).   |
| c.   | Indenture, dated as of June 29, 1998, by and among U S WEST Capital Funding, Inc. (currently named Qwest Capital Funding, Inc.), U S WEST, Inc. (predecessor to Qwest Communications International Inc.) and The First National Bank of Chicago, as trustee (incorporated by reference to Exhibit 4(a) of U S WEST, Inc.'s Current Report on Form 8-K (File No. 001-14087) filed with the Securities and Exchange Commission on November 18, 1998).   |
| (i). | First Supplemental Indenture, dated as of June 30, 2000, by and among U S WEST Capital Funding, Inc. (currently named Qwest Capital Funding, Inc.), U S WEST, Inc. (predecessor to Qwest Communications International Inc.) and Bank One Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.10 of Qwest Communications International Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2000 (File No. 001-15577) filed with the Securities and Exchange Commission on August 11, 2000). |

- d. Indenture, dated as of October 15, 1999, by and between US West Communications, Inc. (currently named Qwest Corporation) and Bank One Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4(b) of Qwest Corporation's annual report on Form 10-K for the year ended December 31, 1999 (File No. 001-03040) filed with the Securities and Exchange Commission on March 3, 2000).

Exhibit Number	Description
----------------	-------------

- |     |   |
|-----|---|
|     | (i). Fifth Supplemental Indenture, dated as of May 16, 2007, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.1 of Qwest Communications International Inc.'s Current Report on Form 8-K (File No. 001-15577) filed with the Securities and Exchange Commission on May 18, 2007).                     |
|     | (ii). Eighth Supplemental Indenture, dated as of September 21, 2011, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.9 of Qwest Corporation's Form 8-A (File No. 001-03040) filed with the Securities and Exchange Commission on September 20, 2011).   |
|     | (iii). Ninth Supplemental Indenture, dated as of October 4, 2011, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.1 of Qwest Corporation's Current Report on Form 8-K (File No. 001-03040) filed with the Securities and Exchange Commission on October 4, 2011).                                   |
|     | (iv). Tenth Supplemental Indenture, dated as of April 2, 2012, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.11 of Qwest Corporation's Form 8-A (File No. 001-03040) filed with the Securities and Exchange Commission on March 30, 2012).  |
|     | (v). Eleventh Supplemental Indenture, dated as of June 25, 2012, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.12 of Qwest Corporation's Form 8-A (File No. 001-03040) filed with the Securities and Exchange Commission on June 22, 2012).   |
|     | (vi). Twelfth Supplemental Indenture, dated as of May 23, 2013, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.13 of Qwest Corporation's Form 8-A (File No. 001-03040) filed with the Securities and Exchange Commission on May 22, 2013).   |
|     | (vii). Thirteenth Supplemental Indenture, dated as of September 29, 2014, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.14 of Qwest Corporation's Form 8-A (File No. 001-03040) filed with the Securities and Exchange Commission on September 26, 2014).   |
|     | (viii). Fourteenth Supplemental Indenture, dated as of September 21, 2015, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.15 of Qwest Corporation's Form 8-A (File No. 001-03040) filed with the Securities and Exchange Commission on September 21, 2015).  |
|     | (ix). Fifteenth Supplemental Indenture, dated as of January 29, 2016, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.16 of Qwest Corporation's Form 8-A (File No. 001-03040) filed with the Securities and Exchange Commission on January 29, 2016).   |
|     | (x). Sixteenth Supplemental Indenture, dated as of August 22, 2016, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Exhibit 4.17 of Qwest Corporation's Form 8-A (File No. 001-03040) filed with Securities and Exchange Commission on August 22, 2016).  |
|     | e. Credit Agreement, dated as of February 20, 2015, by and among Qwest Corporation, the several lenders from time to time parties thereto, and CoBank, ACB, as administrative agent.  |
| 4.6 | Instruments relating to indebtedness of Embarq Corporation. <sup>(1)</sup>  |
|     | a. Indenture, dated as of May 17, 2006, by and between Embarq Corporation and J.P. Morgan Trust Company, National Association, a national banking association, as trustee (incorporated by reference to Exhibit 4.1 of Embarq Corporation's Current Report on Form 8-K (File No. 001-32732) filed with the Securities and Exchange Commission on May 18, 2006). |
|     | b. 7.995% Global Note due 2036 of Embarq Corporation (incorporated by reference to Exhibit 4.4 to Embarq Corporation's annual report on Form 10-K for the year ended December 31, 2006 (File No. 001-32372) filed with the Securities and Exchange Commission on March 9, 2007).  |
| 4.7 | Intercompany debt instruments.  |
|     | a. Revolving Promissory Note, dated as of April 2, 2012 pursuant to which Embarq Corporation may borrow from an affiliate of CenturyLink, Inc. up to \$2.5 billion on a revolving basis (incorporated by reference to   |

Exhibit 4.7(a) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended September 30, 2012 (File No. 001-07784) filed with the Securities and Exchange Commission on November 8, 2012).

Exhibit Number	Description
----------------	-------------

- |    |   |
|----|---|
| b. | Revolving Promissory Note, dated as of April 18, 2012, pursuant to which Qwest Corporation may borrow from an affiliate of CenturyLink, Inc. up to \$1.0 billion on a revolving basis (incorporated by reference to Exhibit 4.7(b) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended September 30, 2012 (File No. 001-07784) filed with the Securities and Exchange Commission on November 8, 2012).                  |
| c. | Revolving Promissory Note, dated as of September 27, 2012, pursuant to which Qwest Communications International, Inc. may borrow from an affiliate of CenturyLink, Inc. up to \$3.0 billion on a revolving basis (incorporated by reference to Exhibit 4.7(c) of CenturyLink Inc.'s annual report on Form 10-K for the year ended December 31, 2012 (File No. 001-07844) filed with the Securities and Exchange Commission on March 1, 2013). |

## 10.2 Stock-based Incentive Plans and Agreements of CenturyLink

- |         |   |
|---------|---|
| a.      | Amended and Restated 2005 Directors Stock Plan, as amended and restated through February 23, 2010 (incorporated by reference to Exhibit 10.2(f) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2009 (File No. 001-07784) filed with the Securities and Exchange Commission on March 1, 2010).  |
| (i).    | Form of Restricted Stock Agreement, pursuant to the foregoing plan, entered into between CenturyLink, Inc. and each of its outside directors as of May 12, 2006 (incorporated by reference to Exhibit 10.1 of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2006 (File No. 001-07784) filed with the Securities and Exchange Commission on August 3, 2006).   |
| (ii).   | Form of Restricted Stock Agreement, pursuant to the foregoing plan, entered into between CenturyLink, Inc. and each of its outside directors as of May 11, 2007 (incorporated by reference to Exhibit 10.2(f) (iii) of CenturyLink, Inc.'s annual report on Form 10-K for the period ended December 31, 2008 (File No. 001-07784) filed with the Securities and Exchange Commission on February 27, 2009).  |
| (iii).  | Form of Restricted Stock Agreement, pursuant to the foregoing plan, entered into between CenturyLink, Inc. and each of its outside directors as of May 9, 2008 (incorporated by reference to Exhibit 10.2 (f) (iv) of CenturyLink, Inc.'s annual report on Form 10-K for the period ended December 31, 2008 (File No. 001-07784) filed with the Securities and Exchange Commission on February 27, 2009).   |
| (iv).   | Form of Restricted Stock Agreement, pursuant to the foregoing plan and dated as of May 8, 2009, entered into between CenturyLink, Inc. and each of its outside directors on such date who remained on the Board following July 1, 2009 (incorporated by reference to Exhibit 10.2(b) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (File No. 001-07784) filed with the Securities and Exchange Commission on August 7, 2009). |
| (v).    | Form of Restricted Stock Agreement, pursuant to the foregoing plan and dated as of May 8, 2009, entered into between CenturyLink, Inc. and each of its outside directors who retired on July 1, 2009 (incorporated by reference to Exhibit 10.2(c) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (File No. 001-07784) filed with the Securities and Exchange Commission on August 7, 2009).                                   |
| (vi).   | Form of Restricted Stock Agreement, pursuant to the foregoing plan and dated as of July 2, 2009, entered into between CenturyLink, Inc. and each of its outside directors named to the Board on July 1, 2009 (incorporated by reference to Exhibit 10.1(d) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (File No. 001-07784) filed with the Securities and Exchange Commission on August 7, 2009).                           |
| (vii).  | Restricted Stock Agreement, pursuant to the foregoing plan and dated as of July 2, 2009, entered into between CenturyLink, Inc. and William A. Owens in payment of Mr. Owens' 2009 supplemental chairman's fees (incorporated by reference to Exhibit 10.2(e) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2009 (File No. 001-07784) filed with the Securities and Exchange Commission on August 7, 2009).                        |
| (viii). | Form of Restricted Stock Agreement, pursuant to the foregoing plan and dated as of May 21, 2010, entered into between CenturyLink, Inc. and seven of its outside directors on such date (incorporated by reference to Exhibit 10.1 of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2010 (File No. 001-07784) filed with the Securities and Exchange Commission on August 6, 2010).   |
| b.      | Amended and Restated 2005 Management Incentive Compensation Plan, as amended and restated through   |

February 23, 2010 (incorporated by reference to Exhibit 10.2(g) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2009 (File No. 001-07784) filed with the Securities and Exchange Commission on March 1, 2010).

Exhibit Number	Description
----------------	-------------

- |      |   |
|------|---|
|      | <ul style="list-style-type: none"> <li>(i). Form of Stock Option Agreement, pursuant to the foregoing plan and dated as of February 21, 2006, entered into between CenturyLink, Inc. and its executive officers (incorporated by reference to Exhibit 10.2(g) (iii) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2005 (File No. 001-07784) filed with the Securities and Exchange Commission on March 16, 2006).</li> <li>(ii). Form of Stock Option Agreement, pursuant to the foregoing plan and dated as of February 26, 2007, entered into between CenturyLink, Inc. and its executive officers (incorporated by reference to Exhibit 10.1 of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2007 (File No. 001-07784) filed with the Securities and Exchange Commission on May 9, 2007).</li> </ul>   |
|      | <ul style="list-style-type: none"> <li>c. CenturyLink 2011 Equity Incentive Plan, as amended through May 18, 2016 (incorporated by reference to Appendix A of CenturyLink, Inc.'s Proxy Statement for its 2016 Annual Meeting of Shareholders (File No. 001-07784) filed with the Securities and Exchange Commission on April 5, 2016).           <ul style="list-style-type: none"> <li>(i). Form of Restricted Stock Agreement for non-management directors used since 2011 (incorporated by reference to Exhibit 10.2(a) (ii) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2011 (File No. 001-07784) filed with the Securities and Exchange Commission on August 9, 2011).</li> <li>(ii). Form of Restricted Stock Agreement for executive officers used since May 2013 (incorporated by reference to Exhibit 10.2(i) (iii) of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2013 (File No. 001-07784) filed with the Securities and Exchange Commission on August 8, 2013).</li> </ul> </li> </ul>  |
| 10.3 | Key Employee Incentive Compensation Plan, dated as of January 1, 1984, as amended and restated as of November 16, 1995 (incorporated by reference to Exhibit 10.1(f) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 1995 (File No. 001-07784) filed with the Securities and Exchange Commission on March 18, 1996) and amendment thereto dated as of November 21, 1996 (incorporated by reference to Exhibit 10.1(f) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 1996 (File No. 001-07784) filed with the Securities and Exchange Commission on March 17, 1997), amendment thereto dated as of February 25, 1997 (incorporated by reference to Exhibit 10.2 of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 1997 (File No. 001-07784) filed with the Securities and Exchange Commission on May 8, 1997), amendment thereto dated as of April 25, 2001 (incorporated by reference to Exhibit 10.2 of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2001 (File No. 001-07784) filed with the Securities and Exchange Commission on May 15, 2001), amendment thereto dated as of April 17, 2000 (incorporated by reference to Exhibit 10.3(a) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2001 (File No. 001-07784) filed with the Securities and Exchange Commission on March 15, 2002) and amendment thereto dated as of February 27, 2007 (incorporated by reference to Exhibit 10.1 of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2007 (File No. 001-07784) filed with the Securities and Exchange Commission on August 8, 2007). |
| 10.4 | Supplemental Dollars & Sense Plan, 2008 Restatement, effective January 1, 2008, (incorporated by reference to Exhibit 10.3(c) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2007 (File No. 001-07784) filed with the Securities and Exchange Commission on February 29, 2009) and amendment thereto dated as of October 24, 2008 (incorporated by reference to Exhibit 10.3(c) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2008 (File No. 001-07784) filed with the Securities and Exchange Commission on March 27, 2009) and amendment thereto dated as of December 27, 2010 (incorporated by reference to Exhibit 10.4 of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2010 (File No. 001-07784) filed with the Securities and Exchange Commission on March 1, 2011).   |
| 10.5 | Supplemental Defined Benefit Pension Plan, effective as of January 1, 2012 (incorporated by reference to Exhibit 10.5 of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2011 (File No. 001-07784) filed with the Securities and Exchange Commission on February 28, 2012).  |
| 10.6 | Amended and Restated Salary Continuation (Disability) Plan for Officers, dated as of November 26, 1991 (incorporated by reference to Exhibit 10.16 of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 1991).   |
| 10.7 | 2015 Executive Officer Short-Term Incentive Program (incorporated by reference to Exhibit A of CenturyLink's 2015 Proxy Statement on Form 14A (File No. 001-07784) filed with the Securities and Exchange Commission on April 8, 2015).   |

- 10.8 Form of Indemnification Agreement entered into between CenturyLink, Inc. and each of its directors as of February 24, 2016 (incorporated by reference to Exhibit 10.1 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on February 29, 2016).

Exhibit Number	Description
10.9	Form of Indemnification Agreement entered into between CenturyLink, Inc. and each of its officers as of February 24, 2016 (incorporated by reference to Exhibit 10.2 of CenturyLink, Inc.'s Current Report on Form 8-K (File No. 001-07784) filed with the Securities and Exchange Commission on February 29, 2016).
10.10	Change of Control Agreement, effective January 1, 2011, by and between Glen F. Post, III and CenturyLink, Inc. (incorporated by reference to Exhibit 10.11 of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2010 (File No. 001-07784) filed with the Securities and Exchange Commission on March 1, 2011).
10.11	Form of Change of Control Agreement, effective January 1, 2011 between CenturyLink, Inc. and each of its other executive officers (incorporated by reference to Exhibit 10.12 of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2010 (File No. 001-07784) filed with the Securities and Exchange Commission on March 1, 2011).
10.12	CenturyLink Executive Severance Plan (incorporated by reference to Exhibit 10.13 of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2014 (File No. 001-07784) filed with the Securities and Exchange Commission on February 24, 2015.)
10.13	Amended and Restated CenturyLink, Inc. Bonus Life Insurance Plan for Executive Officers, dated as of April 3, 2008 (incorporated by reference to Exhibit 10.4 of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2008 (File No. 001-07784) filed with the Securities and Exchange Commission on May 7, 2008) and First Amendment thereto (incorporated by reference to Exhibit 10.13 of CenturyLink, Inc.'s Quarterly Report on Form 10-Q for the period ended September 30, 2010 (File No. 001-07784) filed with the Securities and Exchange Commission on November 5, 2010).
10.14	<p data-bbox="245 842 899 861">Certain Material Agreements and Plans of Embarq Corporation.</p> <p data-bbox="245 877 1427 961">a. Embarq Corporation 2006 Equity Incentive Plan, as amended and restated (incorporated by reference to Exhibit 99.1 of the Registration Statement on Form S-8 filed by CenturyLink, Inc. (File No. 001-07784) filed with the Securities and Exchange Commission on July 1, 2009).</p> <p data-bbox="245 978 1427 1062">b. Form of 2007 Award Agreement for executive officers of Embarq Corporation (incorporated by reference to Exhibit 10.1 of Embarq Corporation's Current Report on Form 8-K (File No. 001-32372) filed with the Securities and Exchange Commission on February 27, 2007).</p> <p data-bbox="245 1079 1427 1163">c. Form of Stock Option Award Agreement (incorporated by reference to Exhibit 10.3 of Embarq Corporation's Current Report on Form 8-K (File No. 001-32372) filed with the Securities and Exchange Commission on March 4, 2008).</p> <p data-bbox="245 1180 1427 1444">d. Embarq Supplemental Executive Retirement Plan, as amended and restated as of January 1, 2009 (incorporated by reference to Exhibit 10.27 of Embarq Corporation's annual report on Form 10-K for the year ended December 31, 2008 (File No. 001-32372) filed with the Securities and Exchange Commission on February 13, 2009), amendment thereto dated as of December 27, 2010 (incorporated by reference to Exhibit 10.14(o) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2010 (File No. 001-07784) filed with the Securities and Exchange Commission on March 1, 2011) and second amendment thereto as of dated as of November 15, 2011 (incorporated by reference to Exhibit 10.14(k) of CenturyLink, Inc.'s annual report on Form 10-K for the year ended December 31, 2011 (File No. 001-07784) filed with the Securities and Exchange Commission on February 28, 2012).</p>
10.15	<p data-bbox="245 1461 1263 1480">Certain Material Agreements and Plans of Qwest Communications International Inc. or Savvis, Inc.</p> <p data-bbox="245 1497 1427 1581">a. Equity Incentive Plan, as amended and restated (incorporated by reference to Annex A of Qwest Communications International Inc.'s Proxy Statement for the 2007 Annual Meeting of Stockholders (File No. 001-15577) filed with the Securities and Exchange Commission on March 29, 2007).</p> <p data-bbox="245 1598 1427 1961">b. Forms of restricted stock, performance share and option agreements used under Equity Incentive Plan, as amended and restated (incorporated by reference to Exhibit 10.2 of Qwest Communications International Inc.'s Current Report on Form 8-K (File No. 001-15577) filed with the Securities and Exchange Commission on October 24, 2005; Exhibit 10.2 of Qwest Communication International Inc.'s annual report on Form 10-K for the year ended December 31, 2005 (File No. 001-15577) filed with the Securities and Exchange Commission on February 16, 2006; Exhibit 10.2 of Qwest Communication International Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2006 (File No. 001-15577) filed with the Securities and Exchange Commission on May 3, 2006; Exhibit 10.2 of Qwest Communication International Inc.'s annual report on Form 10-K for the year ended December 31, 2006 (File No. 001-15577) filed with the Securities and Exchange Commission on February 8, 2007; Exhibit 10.3 of Qwest Communication International Inc.'s Current Report on Form 8-K (File No. 001-15577) filed with the Securities and Exchange Commission on September 15, 2008; Exhibit 10.2 of Qwest</p>

Communication International Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2009 (File No. 001-15577) filed with the Securities and Exchange Commission on April 30, 2009; and Exhibit 10.2 of Qwest Communication International Inc.'s annual report on Form 10-K for the year ended December 31, 2010 (File No. 001-15577) filed with the Securities and Exchange Commission on February 15, 2011).

Exhibit Number	Description
----------------	-------------

- |       |  |
|-------|--|
| c.    | Deferred Compensation Plan for Nonemployee Directors, as amended and restated, Amendment to Deferred Compensation Plan for Nonemployee Directors (incorporated by reference to Exhibit 10.2 of Qwest Communications International Inc.'s Current Report on Form 8-K (File No. 001-15577) filed with the Securities and Exchange Commission on December 16, 2005 and Exhibit 10.8 to Qwest Communication International Inc.'s Quarterly Report on Form 10-Q for the period ended September 30, 2008 (File No. 001-15577) filed with the Securities and Exchange Commission on October 29, 2008) and Amendment No. 2011-1 to Deferred Compensation Plan for Nonemployee Directors (incorporated by reference to Exhibit 10.15(c) of CenturyLink, Inc.'s annual report for the year ended December 31, 2011 (File No. 001-07784) filed with the Securities and Exchange Commission on February 28, 2012).   |
| d.    | Qwest Nonqualified Pension Plan (incorporated by reference to Exhibit 10.9 of Qwest Communications International Inc.'s annual report on Form 10-K for the year ended December 31, 2009 (File No. 001-15577) filed with the Securities and Exchange Commission on February 16, 2010).  |
| e.    | SAVVIS, Inc. Amended and Restated 2003 Incentive Compensation Plan (incorporated by reference to Exhibit 10.4 of SAVVIS, Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2006 (File No. 000-29375) filed with the Securities and Exchange Commission on May 5, 2006), as amended by Amendment No. 1 (incorporated by reference to Exhibit 10.6 of SAVVIS, Inc.'s annual report on Form 10-K for the year ended December 31, 2006 (File No. 000-29375) filed with the Securities and Exchange Commission on February 26, 2007); Amendment No. 2 (incorporated by reference to Exhibit 10.1 of SAVVIS, Inc.'s Current Report on Form 8-K (File No. 000-29375) filed with the Securities and Exchange Commission on May 15, 2007); Amendment No. 3 (incorporated by reference to Exhibit 10.3 of SAVVIS, Inc.'s Quarterly Report on Form 10-Q for the period ended June 30, 2007 (File No. 000-29375) filed with the Securities and Exchange Commission on July 31, 2007; Amendment No. 4 (incorporated by reference to Exhibit 10.2 of SAVVIS, Inc.'s Current Report on Form 8-K (file No. 000-29375) filed with the Securities and Exchange Commission on May 22, 2009); and Amendment No. 5 (incorporated by reference to Exhibit 10.2 of SAVVIS, Inc.'s Current Report on Form 8-K (File No. 000-29375) filed with the Securities and Exchange Commission on May 22, 2009). |
| 12*   | Ratio of Earnings to Fixed Charges   |
| 21*   | Subsidiaries of CenturyLink, Inc.  |
| 23*   | Independent Registered Public Accounting Firm Consent  |
| 31.1* | Certification of the Chief Executive Officer of CenturyLink, Inc. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.   |
| 31.2* | Certification of the Chief Financial Officer of CenturyLink, Inc. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.   |
| 32*   | Certification of the Chief Executive Officer and Chief Financial Officer of CenturyLink, Inc. pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 101*  | Financial statements from the annual report on Form 10-K of CenturyLink, Inc. for the period ended December 31, 2016, formatted in XBRL: (i) the Consolidated Statements of Operations, (ii) the Consolidated Statements of Comprehensive Income (Loss), (iii) the Consolidated Balance Sheets, (iv) the Consolidated Statements of Cash Flows, (v) the Consolidated Statements of Stockholders' Equity and (vi) the Notes to Consolidated Financial Statements.   |

\* Exhibit filed herewith.

(1) Certain of the items in Sections 4.4, 4.5 and 4.6 (i) omit supplemental indentures or other instruments governing debt that has been retired, or (ii) refer to trustees who may have been replaced, acquired or affected by similar changes. In accordance with Item 601(b) (4) (iii) (A) of Regulation S-K, copies of certain instruments defining the rights of holders of certain of our long-term debt are not filed herewith. Pursuant to this regulation, we hereby agree to furnish a copy of any such instrument to the SEC upon request

**ITEM 16. SUMMARY OF BUSINESS AND FINANCIAL INFORMATION**

Not applicable.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this annual report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: February 22, 2017

By: CenturyLink, Inc.  
/s/ David D. Cole  
 David D. Cole  
 Executive Vice President, Controller and Operations  
 Support  
 (Chief Accounting Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this annual report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated.

/s/ Glen F. Post, III	Chief Executive Officer, President and Director	February 22, 2017
Glen F. Post, III		
/s/ William A. Owens	Chairman of the Board	February 22, 2017
William A. Owens		
/s/ Harvey P. Perry	Vice Chairman of the Board	February 22, 2017
Harvey P. Perry		
/s/ R. Stewart Ewing, Jr.	Executive Vice President, Chief Financial Officer and Assistant Secretary	February 22, 2017
R. Stewart Ewing, Jr.		
/s/ David D. Cole	Executive Vice President, Controller and Operations Support	February 22, 2017
David D. Cole		
/s/ Martha H. Bejar	Director	February 22, 2017
Martha H. Bejar		
/s/ Virginia Boulet	Director	February 22, 2017
Virginia Boulet		
/s/ Peter C. Brown	Director	February 22, 2017
Peter C. Brown		
/s/ W. Bruce Hanks	Director	February 22, 2017
W. Bruce Hanks		
/s/ Mary L. Landrieu	Director	February 22, 2017
Mary L. Landrieu		

<u>/s/ Gregory J. McCray</u> Gregory J. McCray	Director	February 22, 2017
<u>/s/ Michael J. Roberts</u> Michael J. Roberts	Director	February 22, 2017
<u>/s/ Laurie A. Siegel</u> Laurie A. Siegel	Director	February 22, 2017

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 10-K**

(Mark One)

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

For the fiscal year ended December 31, 2016

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: 001-33664

**Charter**  
COMMUNICATIONS  
**Charter Communications, Inc.**  
*(Exact name of registrant as specified in its charter)*

Delaware

84-1496755

*(State or other jurisdiction of incorporation or organization)*

*(I.R.S. Employer Identification Number)*

400 Atlantic Street  
Stamford, Connecticut 06901

(203) 905-7800

*(Address of principal executive offices including zip code)*

*(Registrant's telephone number, including area code)*

**Securities registered pursuant to section 12(b) of the Act:**

Title of each class	Name of Exchange which registered
Class A Common Stock, \$.001 Par Value	NASDAQ Global Select Market

**Securities registered pursuant to section 12(g) of the Act: None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act Yes  No

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

Indicate by check mark whether the registrants have submitted electronically and posted on their corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrants were required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

The aggregate market value of the registrant of outstanding Class A common stock held by non-affiliates of the registrant at June 30, 2016 was approximately \$49.1 billion, computed based on the closing sale price as quoted on the NASDAQ Global Select Market on that date. For purposes of this calculation only, directors, executive officers and the principal controlling shareholders or entities controlled by such controlling shareholders of the registrant are deemed to be affiliates of the registrant.

There were 268,897,792 shares of Class A common stock outstanding as of December 31, 2016. There was 1 share of Class B common stock outstanding as of the same date.

#### Documents Incorporated By Reference

Information required by Part III is incorporated by reference from Registrant's proxy statement or an amendment to this Annual Report on Form 10-K to be filed by April 30, 2017.

# Charter

COMMUNICATIONS

CHARTER COMMUNICATIONS, INC.  
FORM 10-K — FOR THE YEAR ENDED DECEMBER 31, 2016

## TABLE OF CONTENTS

	Page No.
<u>PART I</u>	
<u>Item 1</u>	<u>1</u>
<u>Item 1A</u>	<u>18</u>
<u>Item 1B</u>	<u>32</u>
<u>Item 2</u>	<u>32</u>
<u>Item 3</u>	<u>32</u>
<u>Item 4</u>	<u>32</u>
<u>PART II</u>	
<u>Item 5</u>	<u>33</u>
<u>Item 6</u>	<u>37</u>
<u>Item 7</u>	<u>37</u>
<u>Item 7A</u>	<u>57</u>
<u>Item 8</u>	<u>58</u>
<u>Item 9</u>	<u>58</u>
<u>Item 9A</u>	<u>58</u>
<u>Item 9B</u>	<u>59</u>
<u>PART III</u>	
<u>Item 10</u>	<u>60</u>
<u>Item 11</u>	<u>60</u>
<u>Item 12</u>	<u>60</u>
<u>Item 13</u>	<u>60</u>
<u>Item 14</u>	<u>60</u>
<u>PART IV</u>	
<u>Item 15</u>	<u>61</u>
<u>Signatures</u>	<u>S- 1</u>
<u>Exhibit Index</u>	<u>E- 1</u>

This annual report on Form 10-K is for the year ended December 31, 2016. The United States Securities and Exchange Commission ("SEC") allows us to "incorporate by reference" information that we file with the SEC, which means that we can disclose important information to you by referring you directly to those documents. Information incorporated by reference is considered to be part of this annual report. In addition, information that we file with the SEC in the future will automatically update and supersede information

contained in this annual report. In this annual report, "Charter," "we," "us" and "our" refer to Charter Communications, Inc. and its subsidiaries.

### Explanatory Note

On May 18, 2016, Charter Communications, Inc. (formerly known as CCH I, LLC, the "Company" or "Charter") completed its previously reported merger transactions among Charter, Time Warner Cable Inc. ("Legacy TWC"), Charter Communications, Inc. ("Legacy Charter"), and certain other subsidiaries of Charter (the "TWC Transaction"). Also on May 18, 2016, Charter completed its previously reported acquisition of Bright House Networks, LLC ("Legacy Bright House") from Advance/Newhouse Partnership (the "Bright House Transaction," and, together with the TWC Transaction, the "Transactions"). As a result of the Transactions, Charter became the new public parent company that holds the combined operations of Legacy Charter, Legacy TWC and Legacy Bright House and was renamed Charter Communications, Inc. The financial statements presented in this annual report reflect the operations of Legacy Charter through May 17, 2016 and the Company on and after May 18, 2016. See Part II, Item 8. Financial Statements and Supplementary Data, Notes to Consolidated Financial Statements, Note 2, "Mergers and Acquisitions - Selected Pro Forma Financial Information" for certain financial information presented as if the Transactions had closed on January 1, 2015. Also see Exhibit 99.1 in Charter's Quarterly Report on Form 10-Q for the three and nine months ended September 30, 2016 filed with the SEC on November 3, 2016 for pro forma financial information for each quarter of 2015 and the first and second quarter of 2016. Throughout this report references to the "Company" or to "Charter" refer to the combined company following the completion of the Transactions.

As a result of the Transactions and by operation of Rule 12g-3(c) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), Charter is the successor issuer to Legacy Charter and succeeds to the attributes of Legacy Charter as the registrant. Charter's Class A common stock is deemed to be registered under Section 12(b) of the Exchange Act, and Charter is subject to the Exchange Act to the same extent as Legacy Charter.

## CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS:

This annual report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), regarding, among other things, our plans, strategies and prospects, both business and financial including, without limitation, the forward-looking statements set forth in Part I. Item 1. under the heading "Business" and in Part II. Item 7. under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this annual report. Although we believe that our plans, intentions and expectations reflected in or suggested by these forward-looking statements are reasonable, we cannot assure you that we will achieve or realize these plans, intentions or expectations. Forward-looking statements are inherently subject to risks, uncertainties and assumptions, including, without limitation, the factors described in Part I. Item 1A. under "Risk Factors" and in Part II. Item 7. under the heading, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this annual report. Many of the forward-looking statements contained in this annual report may be identified by the use of forward-looking words such as "believe," "expect," "anticipate," "should," "planned," "will," "may," "intend," "estimated," "aim," "on track," "target," "opportunity," "tentative," "positioning," "designed," "create," "predict," "project," "initiatives," "seek," "would," "could," "continue," "ongoing," "upside," "increases" and "potential," among others. Important factors that could cause actual results to differ materially from the forward-looking statements we make in this annual report are set forth in this annual report and in other reports or documents that we file from time to time with the SEC, and include, but are not limited to:

### *Risks Related to the Recently Completed Transactions:*

- our ability to promptly, efficiently and effectively integrate acquired operations;
- managing a significantly larger company than before the completion of the Transactions;
- our ability to achieve the synergies and value creation contemplated by the Transactions;
- changes in Legacy Charter, Legacy TWC or Legacy Bright House operations' businesses, future cash requirements, capital requirements, results of operations, revenues, financial condition and/or cash flows;
- disruption in our business relationships as a result of the Transactions;
- the increase in indebtedness as a result of the Transactions, which will increase interest expense and may decrease our operating flexibility;
- operating costs and business disruption that may be greater than expected;
- the ability to retain and hire key personnel; and
- costs, disruptions and possible limitations on operating flexibility related to, and our ability to comply with, regulatory conditions applicable to us as a result of the Transactions.

### *Risks Related to Our Business*

- our ability to sustain and grow revenues and cash flow from operations by offering video, Internet, voice, advertising and other services to residential and commercial customers, to adequately meet the customer experience demands in our markets and to maintain and grow our customer base, particularly in the face of increasingly aggressive competition, the need for innovation and the related capital expenditures;
- the impact of competition from other market participants, including but not limited to incumbent telephone companies, direct broadcast satellite operators, wireless broadband and telephone providers, digital subscriber line ("DSL") providers, fiber to the home providers, video provided over the Internet by (i) market participants that have not historically competed in the multichannel video business, (ii) traditional multichannel video distributors, and (iii) content providers that have historically licensed cable networks to multichannel video distributors, and providers of advertising over the Internet;
- general business conditions, economic uncertainty or downturn, unemployment levels and the level of activity in the housing sector;
- our ability to obtain programming at reasonable prices or to raise prices to offset, in whole or in part, the effects of higher programming costs (including retransmission consents);
- our ability to develop and deploy new products and technologies including our cloud-based user interface, Spectrum Guide®, and downloadable security for set-top boxes, and any other cloud-based consumer services and service platforms;
- the effects of governmental regulation on our business or potential business combination transactions;
- any events that disrupt our networks, information systems or properties and impair our operating activities or our reputation;
- the availability and access, in general, of funds to meet our debt obligations prior to or when they become due and to fund our operations and necessary capital expenditures, either through (i) cash on hand, (ii) free cash flow, or (iii) access to the capital or credit markets; and

- our ability to comply with all covenants in our indentures and credit facilities, any violation of which, if not cured in a timely manner, could trigger a default of our other obligations under cross-default provisions.

All forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by this cautionary statement. We are under no duty or obligation to update any of the forward-looking statements after the date of this annual report.

## PART I

### Item 1. *Business.*

#### Introduction

We are the second largest cable operator in the United States and a leading broadband communications services company providing video, Internet and voice services to approximately 26.2 million residential and business customers at December 31, 2016. In addition, we sell video and online advertising inventory to local, regional and national advertising customers and fiber-delivered communications and managed information technology ("IT") solutions to larger enterprise customers. We also own and operate regional sports networks and local sports, news and lifestyle channels and sell security and home management services to the residential marketplace.

Our core strategy is to deliver high quality products at competitive prices, combined with outstanding service. This strategy, combined with simple, easy to understand pricing and packaging, is central to our goal of growing our customer base while also selling more individual services to each customer. We expect to execute this strategy by managing our operations in a consumer-friendly, efficient and cost effective manner. Our operating strategy includes insourcing much of our customer care and field operations workforce which results in higher quality service transactions. While an insourced operating model can increase field operations and customer care costs associated with each service transaction, the higher quality nature of each service transaction significantly reduces the volume of service transactions per customer, more than offsetting the higher investment made in each service transaction. As we reduce the number of service transactions and recurring costs per customer relationship, we effectively pass those savings on to customers in the form of products and prices, that we believe are more cost effective than what our competitors offer. The combination of offering competitively priced products and high quality service, allows us to increase the number of customer relationships over a fixed network and products sold per relationship, while at the same time reducing the number of service transactions per relationship, improving customer satisfaction and reducing churn, which results in lower costs to acquire and serve customers. Ultimately, this operating strategy enables us to offer high quality, competitively priced services profitably, while continuing to invest in new products and services.

Our principal executive offices are located at 400 Atlantic Street, Stamford, Connecticut 06901. Our telephone number is (203) 905-7800, and we have a website accessible at [www.charter.com](http://www.charter.com). Our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, and all amendments thereto, are available on our website free of charge as soon as reasonably practicable after they have been filed. The information posted on our website is not incorporated into this annual report.

#### TWC Transaction

On May 18, 2016, the transactions contemplated by the Agreement and Plan of Mergers dated as of May 23, 2015 (the "Merger Agreement"), by and among Legacy TWC, Legacy Charter, CCH I, LLC, previously a wholly owned subsidiary of Legacy Charter ("New Charter") and certain other subsidiaries of New Charter were completed. As a result of the TWC Transaction, New Charter became the new public parent company that holds the operations of the combined companies and was renamed Charter Communications, Inc.

Pursuant to the terms of the Merger Agreement, upon consummation of the TWC Transaction, 285 million outstanding shares of Legacy TWC common stock were converted into 143 million shares of Charter Class A common stock valued at approximately \$32 billion as of the date of acquisition. In addition, Legacy TWC shareholders (excluding Liberty Broadband Corporation ("Liberty Broadband") and Liberty Interactive Corporation ("Liberty Interactive")) received approximately \$28 billion in cash.

As of the date of completion of the Transactions, the total value of the TWC Transaction was approximately \$85 billion, including cash, equity and Legacy TWC assumed debt. The purchase price also includes an estimated pre-combination vesting period fair value of \$514 million for Legacy TWC equity awards converted into Charter awards upon closing of the TWC Transaction ("Converted TWC Awards") and \$69 million of cash paid to former Legacy TWC employees and non-employee directors who held equity awards, whether vested or not vested.

#### Bright House Transaction

Also, on May 18, 2016, Legacy Charter and Advance/Newhouse Partnership ("A/N"), the former parent of Legacy Bright House, completed their previously announced transaction, pursuant to a definitive Contribution Agreement (the "Contribution Agreement"), under which Charter acquired Bright House. Pursuant to the Bright House Transaction, Charter became the owner



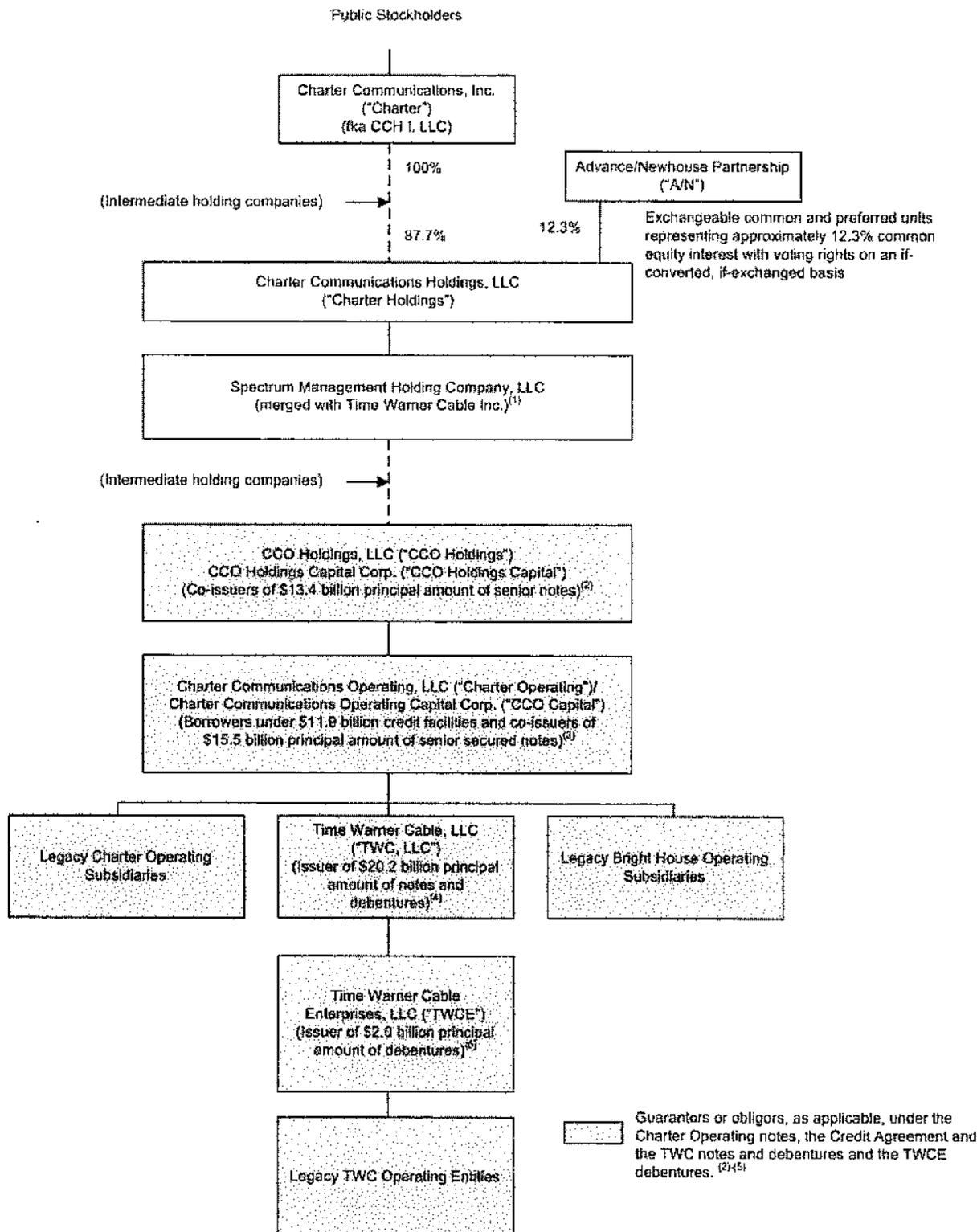
of the membership interests in Bright House and the other assets primarily related to Bright House (other than certain excluded assets and liabilities and non-operating cash). As of the date of acquisition, the purchase price totaled approximately \$12.2 billion consisting of (a) \$2 billion in cash, (b) 25 million convertible preferred units of Charter Communications Holdings, LLC ("Charter Holdings") with a face amount of \$2.5 billion that pay a 6% annual preferential dividend, (c) approximately 31.0 million common units of Charter Holdings that are exchangeable into Charter Class A common stock on a one-for-one basis and (d) one share of Charter Class B common stock.

### **Liberty Transaction**

In connection with the TWC Transaction, Legacy Charter and Liberty Broadband completed their previously announced transactions pursuant to their investment agreement, in which Liberty Broadband purchased for cash approximately 22.0 million shares of Charter Class A common stock valued at \$4.3 billion at the closing of the TWC Transaction to partially finance the cash portion of the TWC Transaction consideration. In connection with the Bright House Transaction, Liberty Broadband purchased approximately 3.7 million shares of Charter Class A common stock valued at \$700 million at the closing of the Bright House Transaction. See Note 2 to the accompanying consolidated financial statements contained in "Item 8. Financial Statements and Supplementary Data," for more information on the Transactions.

**Corporate Entity Structure**

The chart below sets forth our entity structure and that of our direct and indirect subsidiaries. The chart does not include all of our affiliates and subsidiaries and, in some cases, we have combined separate entities for presentation purposes. The equity ownership percentages shown below are approximations. Indebtedness amounts shown below are principal amounts as of December 31, 2016. See Note 9 to the accompanying consolidated financial statements contained in "Item 8. Financial Statements and Supplementary Data," which also includes the accreted values of the indebtedness described below.





- (1) In connection with the Transactions, Legacy TWC transferred substantially all of its assets to TWC, LLC and merged with and into Spectrum Management Holding Company, LLC (formerly named Nina Company II, LLC) ("Spectrum Management") with Spectrum Management as the surviving entity. Spectrum Management was the successor to the SEC reporting obligations of Legacy TWC (which have since been terminated).
- (2) In connection with the Transactions, on May 18, 2016, the proceeds of \$2.5 billion principal amount of senior notes previously issued by CCOH Safari, LLC ("CCOH Safari") and held in escrow were released from escrow, and CCOH Safari merged with and into CCO Holdings, LLC ("CCO Holdings"), which, among other things, assumed the obligations under these debt securities and agreed to guarantee, along with Time Warner Cable, LLC ("TWC, LLC"), Time Warner Cable Enterprises LLC ("TWCE") and substantially all of the operating subsidiaries of Charter Communications Operating, LLC ("Charter Operating") (collectively, the "Subsidiary Guarantors"), the Charter Operating notes, the TWC, LLC and TWCE debt securities and the Charter Operating credit facilities.
- (3) In connection with the Transactions, on May 18, 2016, (a) the proceeds of \$15.5 billion principal amount of senior notes previously issued by CCO Safari II, LLC ("CCO Safari") and held in escrow were released from escrow, and CCO Safari II merged with and into Charter Operating, which, among other things, assumed these debt obligations, (b) the \$3.8 billion credit facility of CCO Safari III, LLC ("CCO Safari III") was issued, and CCO Safari III merged with and into Charter Operating, which, among other things, assumed the obligations under this credit facility and (c) Charter Operating agreed to guarantee, along with the Subsidiary Guarantors, the TWC, LLC senior notes and debentures and the TWCE senior debentures. As of December 31, 2016, the Charter Operating credit facilities were comprised of \$2.5 billion aggregate principal amount term loan A facility, \$1.4 billion aggregate principal amount term loan E facility, \$1.2 billion aggregate principal amount term loan F facility, \$993 million aggregate principal amount term loan H facility and \$2.8 billion aggregate principal amount term loan I facility. Charter Operating also has availability under its revolving credit facility of approximately \$2.8 billion as of December 31, 2016.
- (4) In connection with the Transactions, Legacy TWC transferred substantially all of its assets to TWC, LLC (f/k/a TWC NewCo LLC), and, among other things, TWC, LLC assumed all the obligations under \$20.2 billion principal amount of notes and debentures previously issued by Legacy TWC, and agreed to guarantee the Charter Operating and TWCE notes and debentures and the Charter Operating credit facilities.
- (5) In connection with the Transactions, TWCE assumed all the obligations under \$2.0 billion principal amount of debentures previously issued by Legacy TWC, and agreed to guarantee the Charter Operating and TWC, LLC notes and debentures and the Charter Operating credit facilities.

### Products and Services

We offer our customers subscription-based video services, including video on demand ("VOD"), high definition ("HD") television, and digital video recorder ("DVR") service), Internet services and voice services. As of December 31, 2016, 70% of our footprint was all-digital enabling us to offer more HD channels, faster Internet speeds and better video picture quality and we intend to transition the remaining portions of our Legacy TWC and Legacy Bright House footprints. Our video, Internet, and voice services are offered to residential and commercial customers on a subscription basis, with prices and related charges based on the types of service selected, whether the services are sold as a "bundle" or on an individual basis, and the equipment necessary to receive our services. Bundled services are available to approximately 99% of our passings, and approximately 61% of our customers subscribe to a bundle of services.

All customer statistics as of December 31, 2016 include the operations of Legacy TWC, Legacy Bright House and Legacy Charter, each of which is based on individual legacy company reporting methodology. These methodologies differ and their differences may be material and statistical reporting will be conformed over time to a single reporting methodology. The following table summarizes our customer statistics for video, Internet and voice as of December 31, 2016 and 2015 (in thousands except per customer data and footnotes).

	Approximate as of	
	December 31,	
	2016 (a)	2015 (a)
<b><u>Customer Relationships (b)</u></b>		
Residential	24,801	6,284
Small and Medium Business	1,404	390
Total Customer Relationships	26,205	6,674
<b><u>Residential Primary Service Units ("PSUs")</u></b>		
Video	16,836	4,322
Internet	21,374	5,227
Voice	10,327	2,598
	48,537	12,147
Monthly Residential Revenue per Residential Customer (c)	\$ 109.77	\$ 111.19
<b><u>Small and Medium Business PSUs</u></b>		
Video	400	108
Internet	1,219	345
Voice	778	218
	2,397	671
Monthly Small and Medium Business Revenue per Customer (d)	\$ 214.25	\$ 172.88
<b><u>Enterprise PSUs (e)</u></b>	97	30

After giving effect to the Transactions, December 31, 2015 residential and small and medium business customer relationships would have been 23,795,000 and 1,256,000, respectively, residential video, Internet and voice PSUs would have been 17,062,000, 19,911,000 and 9,959,000, respectively and small and medium business PSUs would have been 361,000, 1,078,000 and 667,000, respectively; Enterprise PSUs would have been 81,000.

- We calculate the aging of customer accounts based on the monthly billing cycle for each account. On that basis, as of December 31, 2016 and 2015, customers include approximately 208,400 and 38,100 customers, respectively, whose accounts were over 60 days past due, approximately 15,500 and 1,700 customers, respectively, whose accounts were over 90 days past due, and approximately 8,000 and 900 customers, respectively, whose accounts were over 120 days past due.
- Customer relationships include the number of customers that receive one or more levels of service, encompassing video, Internet and voice services, without regard to which service(s) such customers receive. Customers who reside in residential multiple dwelling units ("MDUs") and that are billed under bulk contracts are counted based on the number of billed units within each bulk MDU. Total customer relationships excludes enterprise customer relationships.
- Monthly residential revenue per residential customer is calculated as total residential video, Internet and voice quarterly revenue divided by three divided by average residential customer relationships during the respective quarter.
- Monthly small and medium business revenue per customer is calculated as total small and medium business quarterly revenue divided by three divided by average small and medium business customer relationships during the respective quarter.
- Enterprise PSUs represent the aggregate number of fiber service offerings counting each separate service offering as an individual PSU.



## Residential Services

### *Video Services*

Our video customers receive a package of basic programming which, in our all-digital markets, includes a digital set-top box that provides an interactive electronic programming guide with parental controls, access to pay-per-view services, including VOD (available to nearly all of our passings), digital music channels and the option to view certain video services on third party devices. Customers have the option to purchase additional tiers of services including premium channels which provide original programming, commercial-free movies, sports, and other special event entertainment programming. Substantially all of our video programming is available in HD.

In most areas, we offer VOD service which allows customers to select from approximately 30,000 titles at any time. VOD includes standard definition, HD and three dimensional ("3D") content. VOD programming options may be accessed for free if the content is associated with a customer's linear subscription, or for a fee on a transactional basis. VOD services are also offered on a subscription basis included in a digital tier premium channel subscription or for a monthly fee. Pay-per-view channels allow customers to pay on a per-event basis to view a single showing of a one-time special sporting event, music concert, or similar event on a commercial-free basis.

Our goal is to provide our video customers with the programming they want, when they want it, on any device. DVR service enables customers to digitally record programming and to pause and rewind live programming. Customers can also use the Charter TV applications available on portable devices, streaming devices and on our websites to watch up to 300 channels of cable TV, view VOD programming, remotely control digital set-top boxes while in the home and to program DVRs remotely. We intend to consolidate the various legacy entity TV applications into a single Spectrum TV Application in 2017. Customers also have access to programmer authenticated applications and websites such as HBO Go<sup>®</sup>, Fox Now<sup>®</sup>, Discovery Go<sup>®</sup> and WatchESPN<sup>®</sup>.

In certain markets, we have launched Spectrum Guide<sup>®</sup>, a network or "cloud-based" user interface that runs on traditional set-top boxes, with a look and feel that is similar to that of the Spectrum TV App. Spectrum Guide<sup>®</sup> is designed to enable our customers to enjoy a state-of-the-art video experience on set-top boxes, regardless of the age of the set-top box. The guide enables customers to find video content more easily across cable TV channels and VOD options. We plan to continue to deploy across our footprint and enhance this technology in 2017 and beyond.

### *Internet Services*

Approximately 99% of our estimated passings are enabled for DOCSIS 3.0 wideband technology, allowing us to offer our residential customers multiple tiers of Internet services with currently marketed download speeds of up to 300 megabits per second ("Mbps"). In nearly every market where we have launched Spectrum pricing and packaging ("SPP"), our entry level Internet download speed offering is 60 or 100 Mbps which, among other things, allows several people within a single household to stream HD video content online while simultaneously using our Internet service for non-video purposes. As we roll out SPP in Legacy TWC and Legacy Bright House markets, we will bring base speed offerings to a standard minimum of 60 or 100 Mbps at uniform pricing without any usage-based pricing data caps, modem fees or early termination fees. Finally, we offer a security suite with our Internet services which, upon installation by customers, provides protection against computer viruses and spyware and includes parental control features.

We offer an in-home WiFi product that permits customers to lease high performance wireless routers to maximize their in-home wireless Internet experience. Additionally, we offer an out-of-home WiFi service ("Spectrum WiFi") in most of our footprint to our Internet customers at designated "hot spots." In 2017, we expect to expand WiFi accessibility to our customers both inside and outside of their legacy entity footprints.

### *Voice Services*

We provide voice communications services using VoIP technology to transmit digital voice signals over our network. Our voice services include unlimited local and long distance calling to the United States, Canada, Mexico and Puerto Rico, voicemail, call waiting, caller ID, call forwarding and other features and offers international calling either by the minute, or through packages of minutes per month. For customers that subscribe to both our voice and video offerings, caller ID on TV is also available in most areas.

### *Other Residential Services*

We are continually engaging in product research and development and other opportunities to expand our services including the activation of our Mobile Virtual Network Operator ("MVNO") agreement with Verizon which would enable us to offer mobile services. The activation of the MVNO with Verizon does not, however, represent an obligation for us to offer mobile services.

### **Commercial Services**

We offer scalable broadband communications solutions for businesses and carrier organizations of all sizes, selling Internet access, data networking, fiber connectivity to cellular towers and office buildings, video entertainment services and business telephone services.

### *Small and Medium Business*

As Spectrum Business, we offer video, Internet and voice services to small and medium businesses over our coaxial network that are similar to those that we provide to our residential customers. Spectrum Business includes a full range of video programming and music services and Internet speeds of up to 100 Mbps downstream, 300 Mbps in certain markets, and up to 20 Mbps upstream in its DOCSIS 3.0 markets. Spectrum Business also includes a set of business services including web hosting, e-mail and security, and multi-line telephone services with more than 30 business features including web-based service management.

### *Enterprise Solutions*

As Spectrum Enterprise, we offer fiber-delivered communications and managed IT solutions to larger businesses, as well as high-capacity last-mile data connectivity services to wireless and wireline carriers, Internet Service Providers ("ISPs") and other competitive carriers on a wholesale basis. More specifically, Spectrum Enterprise's portfolio includes fiber Internet access with symmetrical speeds up to 10 gigabits per second ("Gbps"), voice trunking services such as Primary Rate Interface ("PRI") and Session Initiation Protocol ("SIP") Trunks, Ethernet services that privately and securely connect geographically dispersed client locations with speeds up to 10 Gbps, and video solutions designed to meet the needs of the hospitality, education, and health care clients. Our managed IT portfolio includes Cloud Infrastructure as a Service ("IaaS") and Cloud Desktop as a Service ("DaaS"), and managed hosting, application, and messaging solutions, along with other related IT and professional services. The Transactions have provided us with a larger footprint which allows us to more effectively serve business customers with multiple sites across given geographic regions. These customers can benefit from obtaining these advanced services from a single provider simplifying procurement and potentially reducing their costs.

### **Advertising Services**

Our advertising sales division, Spectrum Reach<sup>®</sup>, offers local, regional and national businesses with the opportunity to advertise in individual and multiple markets on cable television networks. We receive revenues from the sale of local advertising on digital advertising networks and satellite-delivered networks such as MTV<sup>®</sup>, CNN<sup>®</sup> and ESPN<sup>®</sup>. In any particular market, we typically insert local advertising on over 50 channels. Since completion of the Transactions, our larger footprint has increased opportunities for advertising customers to address broader regional audiences from a single provider and thus reach more customers with a single transaction. Our increased size provides scale to invest in new technology to create more targeted and interactive advertising capabilities.

Available advertising time is generally sold by our advertising sales force. In some markets, we have formed advertising interconnects or entered into representation agreements with other video distributors, including, among others, Verizon Communications Inc.'s ("Verizon") fiber optic service ("FiOS") and AT&T Inc.'s ("AT&T") U-verse, under which we sell advertising on behalf of those operators. In some markets, we enter into representation agreements under which another operator in the area will sell advertising on our behalf. These arrangements enable us and our partners to deliver linear commercials across wider geographic areas, replicating the reach of local broadcast television stations to the extent possible. In addition, we, together with Comcast Corporation ("Comcast") and Cox Communications, Inc., own National Cable Communications LLC, which, on behalf of a number of video operators, sells advertising time to national and regional advertisers.

We also sell the advertising inventory of our owned and operated local sports, news and lifestyle channels, and advertising inventory on our regional sports networks that carry Los Angeles Lakers' basketball games and other sports programming and on SportsNet LA, a regional sports network that carries Los Angeles Dodgers' baseball games and other sports programming.

We have deployed advanced advertising products such as interactivity, household addressability, dynamic ad insertion into VOD and data infused advertising campaigns within various parts of our footprint. These new products will be distributed across more of our footprint in 2017.

## **Other Services**

### ***Regional Sports and News Networks***

We have an agreement with the Los Angeles Lakers for rights to distribute all locally available pre-season, regular season and post-season Los Angeles Lakers' games through 2033. We broadcast those games on our regional sports network, Spectrum SportsNet. As of December 31, 2016, Spectrum SportsNet was distributed to approximately 4.7 million multichannel video customers via the majority of major multichannel video distributors in our Southern California, Las Vegas, NV and Hawaii regions. We also manage 36 local news channels, including Spectrum News NY1, a 24-hour news channel focused on New York City, 20 local sports channels and three local lifestyle community channels, and we own 26.8% of Sterling Entertainment Enterprises, LLC (doing business as SportsNet New York), a New York City-based regional sports network that carries New York Mets' baseball games as well as other regional sports programming.

American Media Productions, LLC ("American Media Productions"), an unaffiliated third party, owns SportsNet LA, a regional sports network carrying the Los Angeles Dodgers' baseball games and other sports programming. In accordance with agreements with American Media Productions, we act as the network's exclusive affiliate and advertising sales representative and have certain branding and programming rights with respect to the network. In addition, we provide certain production and technical services to American Media Productions. The affiliate, advertising, production and programming agreements continue through 2038. We continue to seek distribution agreements for the carriage of SportsNet LA by other major distributors.

### ***Security and Home Management***

We also provide security and home management services to our residential customers in certain markets. Our broadband cable system connects the customer's in-home system to our emergency response center. In addition to providing traditional security, fire and medical emergency monitoring and dispatch, the service allows customers to remotely arm or disarm their security system, monitor their home via indoor and outdoor cameras, and remotely operate key home functions, including setting and controlling lights, thermostats and door locks.

## **Pricing of Our Products and Services**

Our revenues are principally derived from the monthly fees customers pay for the services we provide. We typically charge a one-time installation fee which is sometimes waived or discounted in certain sales channels during certain promotional periods.

Our SPP offers a standardized price for each tier of service, bundle of services, and add-on service, regardless of market and emphasizes triple play bundles of video, Internet and voice services. Our most popular and competitive services are combined in core packages at what we believe are attractive prices. We began launching SPP in the Legacy TWC and Legacy Bright House footprints in the third quarter of 2016, and we expect to offer SPP in all markets by the middle of 2017. We believe our approach:

- offers simplicity for customers to understand our offers, and for our employees in service delivery;
- offers the ability to package more services at the time of sale, thus increasing revenue per customer;
- offers a higher quality and more value-based set of services, including faster Internet speeds, more HD channels, lower equipment fees and a more transparent pricing structure;
- drives higher customer satisfaction, lower service calls and churn; and
- allows for gradual price increases at the end of promotional periods.

## **Our Network Technology and Customer Premise Equipment**

Our network includes three key components: a national backbone, regional/metro networks and the "last-mile" network. Both our national backbone and regional/metro network components utilize a redundant Internet Protocol ("IP") ring/mesh architecture. The national backbone component provides connectivity from the regional demarcation points to nationally centralized content, connectivity and services. The regional/metro network components provide connectivity between the regional demarcation points and headends within a specific geographic area and enable the delivery of content and services between these network components.

Our last-mile network utilizes a hybrid fiber coaxial cable ("HFC") architecture, which combines the use of fiber optic cable with coaxial cable. In most systems, we deliver our signals via fiber optic cable from the headend to a group of nodes, and use coaxial



cable to deliver the signal from individual nodes to the homes served by that node. For our fiber Internet, Ethernet, carrier wholesale, SIP and PRI Spectrum Enterprise customers, fiber optic cable is extended from the individual nodes to the customer's site. For certain new build and MDU sites, we increasingly bring fiber to the customer site. Our design standard is six strands of fiber to each node, with two strands activated and four strands reserved for spares and future services. This design standard allows these strands to be utilized for additional residential traffic capacity, and enterprise customer needs as they arise. We believe that this hybrid network design provides high capacity and signal quality. The design also provides two-way signal capabilities for the support of interactive services.

HFC architecture benefits include:

- bandwidth capacity to enable traditional and two-way video and broadband services;
- dedicated bandwidth for two-way services; and
- signal quality and high service reliability.

Approximately 98% of our estimated passings are served by systems that have bandwidth of 750 megahertz or greater as of December 31, 2016. This bandwidth capacity enables us to offer HD television, DOCSIS-based Internet services and voice services.

An all-digital platform enables us to offer a larger selection of HD channels, faster Internet speeds and better picture quality while providing greater plant security and enabling lower installation and disconnect service truck rolls. We are currently all-digital in 70% of our footprint and intend to transition the remaining portions of our Legacy TWC and Legacy Bright House footprints.

We have been introducing our new set-top box, WorldBox, to consumers in certain markets. The WorldBox design has opened the set-top box market to new vendors and reduced our set-top box costs. The WorldBox also includes more advanced features and functionality than older set-top boxes, including faster processing times, IP capabilities with increased speed, additional simultaneous recordings, increased DVR storage capacity, and a greater degree of flexibility for consumers to take Charter-provisioned set-top boxes with them, if and when, they move residences. We have also been introducing our new cloud-based user interface, Spectrum Guide<sup>®</sup>, to our video customers in certain markets. Spectrum Guide<sup>®</sup> improves video content search and discovery, and fully enables our on-demand offering. In addition, Spectrum Guide<sup>®</sup> can function on nearly all of Legacy Charter's deployed set-tops, reducing costs and customer disruption to swap equipment for new functionality.

### **Management, Customer Care and Marketing**

Our operations are centralized, with senior executives located at several key corporate offices, responsible for coordinating and overseeing operations including establishing company-wide strategies, policies and procedures. Sales and marketing, network operations, field operations, customer operations, engineering, advertising sales, human resources, legal, government relations, information technology and finance are all directed at the corporate level. Regional and local field operations are responsible for on-site service transactions with customers and maintaining and constructing that portion of our network which is located outdoors. In 2017, our field operations group will focus on standardizing practices, processes, procedures and metrics, including those used to assure the quality of work performed when servicing customers.

We continue to focus on improving the customer experience through enhanced product offerings, reliability of services, and delivery of quality customer service. As part of our operating strategy, we are committed to investments and hiring plans that will insource most of our customer service workload over the next few years. We intend to bring the Legacy TWC and Legacy Bright House customer operations workload, much of which is outsourced offshore, back to the United States. Most of these repatriated jobs will be fully insourced and will increase our full time labor force. We are currently constructing a new call center in McAllen, TX which will solely serve customers who prefer to engage with us in Spanish, resulting in the creation of new jobs. This new facility will be operational and taking calls in 2017.

Legacy Charter's in-house domestic call centers currently handle approximately 90% of calls, managed centrally to ensure a consistent, high quality customer experience. On a consolidated basis, in-house domestic call centers handle just over 60% of customer service calls. Over a multi-year period, however, we plan to migrate Legacy TWC and Legacy Bright House customer service centers to Legacy Charter's model of using segmented, virtualized, U.S.-based in-house call centers. Segmented, virtualized call centers allow calls to be routed to agents across our footprint based on call type, enabling agents to be experts in addressing specific customer needs, thus creating a better customer experience. Legacy Charter's inbound sales, billing, service and retention call centers are also virtualized and segmented by call-type. A new call center agent desktop interface tool, already used at Legacy Charter, is being developed for the acquired systems. This new desktop interface tool will enable virtualization of all call centers, regardless of the legacy billing platform, to better serve our customers.



We also provide customers with the opportunity to interact with us through a variety of forums in addition to telephonic communications, including through our customer website, mobile device applications, online chat, and via social media. Our customer websites and mobile applications enable customers to pay their bills, manage their accounts, order new services and utilize self-service help and support.

We sell our residential and commercial services using a national brand platform known as Spectrum®, Spectrum Business® and Spectrum Enterprise®. These brands reflect our comprehensive approach to industry-leading products, driven by speed, performance and innovation. Our marketing strategy emphasizes the sale of our bundled services through targeted direct response marketing programs to existing and potential customers and increases awareness and the value of the Spectrum brand. Our marketing organization creates and executes marketing programs intended to grow customer relationships, increase services per relationship, retain existing customers and cross-sell additional products to current customers. We monitor the effectiveness of our marketing efforts, customer perception, competition, pricing, and service preferences, among other factors, in order to increase our responsiveness to our customers and to improve our sales and customer retention. Our marketing organization also manages and directs several sales channels including direct sales, on-line, outbound telemarketing and stores.

### **Programming**

We believe that offering a wide variety of video programming choices influences a customer's decision to subscribe and retain our cable video services. We obtain basic and premium programming, usually pursuant to written contracts, from a number of suppliers although media consolidation has resulted in fewer suppliers and additional selling power on the part of programmer suppliers. Our programming contracts generally continue for a fixed period of time, usually for multiple years, and are subject to negotiated renewal.

Programming is usually made available to us for a license fee, which is generally paid based on the number of customers to whom we make that programming available. Programming license fees may include "volume" discounts and financial incentives to support the launch of a channel and/or ongoing marketing support, as well as discounts for channel placement or service penetration. For home shopping channels, we typically receive a percentage of the revenue attributable to our customers' purchases. We also offer VOD and pay per view channels of movies and events that are subject to a revenue split with the content provider.

Our programming costs have increased in excess of customary inflationary and cost-of-living type increases. We expect programming costs to continue to increase due to a variety of factors including, annual increases pursuant to our programming contracts, contract renewals with programmers and the carriage of incremental programming, including new services and VOD programming. Increases in the cost of sports programming and the amounts paid for broadcast station retransmission consent have been the largest contributors to the growth in our programming costs over the last few years. Additionally, the demands of large media companies who link carriage of their most popular networks to carriage and cost increases of their less popular networks, has limited our flexibility in creating more tailored and cost-sensitive programming packages for consumers. Finally, programmers have experienced declines in demand for advertising as advertisers shift more of their marketing spend online. We believe that this is resulting in programmers demanding higher programming fees from us, as they seek to recover revenue they are losing to online advertising.

Federal law allows commercial television broadcast stations to make an election between "must-carry" rights and an alternative "retransmission-consent" regime. When a station opts for the retransmission-consent regime, we are not allowed to carry the station's signal without that station's permission. Continuing demands by owners of broadcast stations for cash payments at substantial increases over amounts paid in prior years in exchange for retransmission consent will increase our programming costs or require us to cease carriage of popular programming, potentially leading to a loss of customers in affected markets.

Over the past several years, increases in our video service rates have not fully offset increasing programming costs, and with the impact of increasing competition and other marketplace factors, we do not expect them to do so in the foreseeable future. Although we pass along a portion of amounts paid for retransmission consent to the majority of our customers, our inability to fully pass programming cost increases on to our video customers has had, and is expected in the future to have, an adverse impact on our cash flow and operating margins associated with our video product. In order to mitigate reductions of our operating margins due to rapidly increasing programming costs, we continue to review our pricing and programming packaging strategies.

We have programming contracts that have expired and others that will expire at or before the end of 2017. We will seek to renegotiate the terms of these agreements. There can be no assurance that these agreements will be renewed on favorable or comparable terms. To the extent that we are unable to reach agreements with certain programmers on terms that we believe are reasonable, we have been, and may in the future be, forced to remove such programming channels from our line-up, which may result in a loss of customers.



## Regions

We operate in geographically diverse areas which are organized in regional clusters. These regions are managed centrally on a consolidated level. Our eleven regions and the customer relationships within each region as of December 31, 2016 are as follows (in thousands):

Regions	Total Customer Relationships
Carolinas	2,609
Central	2,800
Florida	2,251
Great Lakes	2,143
Northeast	2,909
Northwest	1,410
NYC	1,317
South	2,030
Southern Ohio	2,039
Texas	2,561
West	4,136

## Competition

### Residential Services

We face intense competition for residential customers, both from existing competitors and, as a result of the rapid development of new technologies, services and products, from new entrants.

#### *Video competition*

Our residential video service faces competition from direct broadcast satellite (“DBS”) services, which have a national footprint and compete in all of our operating areas. DBS providers offer satellite-delivered pre-packaged programming services that can be received by relatively small and inexpensive receiving dishes. They offer aggressive promotional pricing, exclusive programming (e.g., NFL Sunday Ticket) and video services that are comparable in many respects to our residential video service. Our residential video service also faces competition from phone companies with fiber-based networks, primarily AT&T U-verse, Frontier Communications Corporation (“Frontier”) FiOs and Verizon FiOs, which offer wireline video services in approximately 23%, 8% and 4%, respectively, of our operating areas. In July 2015, AT&T acquired DIRECTV Group Inc. (“DIRECTV”), the nation’s largest DBS provider, with the combined company able to offer bundles of video, Internet, wireline phone service and wireless service. As a condition to the Federal Communications Commission (“FCC”) approval of the transaction, AT&T is required to deploy fiber to the home (“FTTH”) to 12.5 million locations within four years from the close of its transaction. AT&T also announced the acquisition of Time Warner Inc. in October 2016 which is subject to regulatory approval. If approved, it is not yet clear how AT&T will use the various programming and studio assets to benefit its own video on its various platforms or potential program access conditions as part of such regulatory approval.

Our residential video service also faces growing competition from a number of other sources, including companies that deliver linear network programming, movies and television shows on demand and other video content over broadband Internet connections to televisions, computers, tablets and mobile devices. These newer categories of competitors include virtual multichannel video programming distributors (“V-MVPD”) such as AT&T’s “DirecTV NOW,” DISH Network Corporation’s “Sling TV,” and Sony Corporation’s “Playstation Vue,” and direct to consumer products offered by programmers that have not traditionally sold programming directly to consumers, such as HBO’s “HBO Now,” CBS’ “CBS All Access” and Showtime’s “Showtime Anytime.” Other online video business models have also developed, including, (i) subscription video on demand (“SVOD”) services such as Netflix, Amazon.com Inc.’s (“Amazon”) “Prime,” and “Hulu Plus,” (ii) ad-supported free online video products, including Google Inc.’s (“Google”), “YouTube” and “Hulu,” some of which offer programming for free to consumers that we currently purchase for a fee, (iii) pay-per-view products, such as Apple’s “iTunes” and Amazon’s, “Amazon Instant,” and (iv) additional ad-supported free

offerings from wireless providers such as Verizon's "go90" and T-Mobile's "Binge On" that exempt certain video content traffic from counting towards monthly data caps. We have viewed online video services as complementary to our

own video offering, and we have developed a cloud-based guide that is capable of incorporating video from many on-line video services currently offered in the marketplace. As the proliferation of online video services grows, however, services such as DirecTV Now and potential forthcoming services such as Hulu Live, and new direct to consumer offerings, could negatively impact the growth of our video business.

#### ***Internet competition***

Our residential Internet service faces competition from the phone companies' DSL, FTTH and wireless broadband offerings as well as from a variety of companies that offer other forms of online services, including wireless and satellite-based broadband services. Verizon's FiOs and Frontier in certain markets acquired from Verizon, are our primary fiber-to-the-home competitor, although AT&T has also begun fiber-to-the-home builds as well, including the required buildout per the FCC condition as a result of AT&T's acquisition of DIRECTV noted above. Given the FTTH deployments of our competitors, launches of broadband services offering 1 Gbps speed are becoming more common. Several competitors, including AT&T and Google, deliver 1 Gbps broadband speed in at least a portion of their footprints which overlap our footprint. DSL service is often offered at prices lower than our Internet services, although typically at speeds lower than the speeds we offer. Various wireless phone companies are now offering third and fourth generation (3G and 4G) wireless Internet services with fifth generation (5G) and faster services on the horizon, some of which offer unlimited data packages to customers. In addition, a growing number of commercial areas, such as retail malls, restaurants and airports, offer WiFi Internet service. Numerous local governments are also considering or actively pursuing publicly subsidized WiFi Internet access networks. These options offer alternatives to cable-based Internet access.

#### ***Voice competition***

Our residential voice service competes with wireless and wireline phone providers, as well as other forms of communication, such as text messaging on cellular phones, instant messaging, social networking services, video conferencing and email. We also compete with "over-the-top" phone providers, such as Vonage, Skype, magicJack, Google Voice and Ooma, Inc., as well as companies that sell phone cards at a cost per minute for both national and international service. The increase in the number of different technologies capable of carrying voice services and the number of alternative communication options available to customers as well as the replacement of wireline services by wireless have intensified the competitive environment in which we operate our residential voice service.

#### ***Regional Competitors***

In some of our operating areas, other competitors have built networks that offer video, Internet and voice services that compete with our services. For example, in Kansas City and Austin, Texas, our residential video, Internet and voice services compete with Google Fiber services. In addition to Google Fiber, Cincinnati Bell Inc., Hawaiian Telcom, RCN Telecom Services, LLC and WideOpenWest Finance, LLC ("WOW"), each compete with us in parts of our operating area.

#### ***Additional competition***

In addition to multi-channel video providers, cable systems compete with other sources of news, information and entertainment, including over-the-air television broadcast reception, live events, movie theaters and the Internet. Competition is also posed by satellite master antenna television systems, or SMATV systems, serving MDUs, such as condominiums, apartment complexes, and private residential communities.

#### ***Business Services***

We face intense competition as to each of our business services offerings. Our small and medium business video, Internet, networking and voice services face competition from a variety of providers as described above. Our enterprise solutions also face competition from the competitors described above as well as other telecommunications carriers, such as metro and regional fiber-based carriers. We also compete with cloud, hosting and related service providers and application-service providers.

#### ***Advertising***

We face intense competition for advertising revenue across many different platforms and from a wide range of local and national competitors. Advertising competition has increased and will likely continue to increase as new formats seek to attract the same advertisers. We compete for advertising revenue against, among others, local broadcast stations, national cable and broadcast networks, radio stations, print media and online advertising companies and content providers.



## Security and Home Management

Our IntelligentHome service faces competition from traditional security companies, such as The ADT Corporation, service providers such as Verizon and AT&T, as well as new entrants, such as Vivint, Inc., Alarm.com, Inc. and NEST Labs, Inc. (which Google acquired in 2014).

## Seasonality and Cyclicity

Our business is subject to seasonal and cyclical variations. Our results are impacted by the seasonal nature of customers receiving our cable services in college and vacation markets. Our revenue is subject to cyclical advertising patterns and changes in viewership levels. Our advertising revenue is generally higher in the second and fourth calendar quarters of each year, due in part to increases in consumer advertising in the spring and in the period leading up to and including the holiday season. U.S. advertising revenue is also cyclical, benefiting in even-numbered years from advertising related to candidates running for political office and issue-oriented advertising. Our capital expenditures and trade working capital are also subject to significant seasonality based on the timing of subscriber growth, network programs, specific projects and construction.

## Regulation and Legislation

The following summary addresses the key regulatory and legislative developments affecting the cable industry and our three primary services for both residential and commercial customers: video, Internet, and voice services. Cable system operations are extensively regulated by the federal government (primarily the FCC), certain state governments, and many local governments. A failure to comply with these regulations could subject us to substantial penalties. Our business can be dramatically impacted by changes to the existing regulatory framework, whether triggered by legislative, administrative, or judicial rulings. Congress and the FCC have frequently revisited the subject of communications regulation and they are likely to do so again in the future. We could be materially disadvantaged in the future if we are subject to new regulations or regulatory actions that do not equally impact our key competitors. We cannot provide assurance that the already extensive regulation of our business will not be expanded in the future. In addition, we are already subject to Charter-specific conditions regarding certain business practices as a result of the FCC's approval of the Transactions.

## Video Service

### *Must Carry/Retransmission Consent*

There are two alternative legal methods for carriage of local broadcast television stations on cable systems. Federal "must carry" regulations require cable systems to carry local broadcast television stations upon the request of the local broadcaster. Alternatively, federal law includes "retransmission consent" regulations, by which popular commercial television stations can prohibit cable carriage unless the cable operator first negotiates for "retransmission consent," which may be conditioned on significant payments or other concessions. Popular stations invoking "retransmission consent" have been demanding substantial compensation increases in their recent negotiations with cable operators, thereby significantly increasing our operating costs.

Additional government-mandated broadcast carriage obligations could disrupt existing programming commitments, interfere with our preferred use of limited channel capacity, and limit our ability to offer services that appeal to our customers and generate revenues.

### *Cable Equipment*

In 1996, Congress enacted a statute requiring the FCC to adopt regulations designed to assure the development of an independent retail market for "navigation devices," such as cable set-top boxes. As a result, the FCC required cable operators to make a separate offering of security modules (*i.e.*, a "CableCARD") that can be used with retail navigation devices. Some of the FCC's rules requiring support for CableCARDS were vacated by the United States Court of Appeals for the District of Columbia in 2013, and another of these rules was repealed by Congress in 2014, but the basic obligation to provide separable security for retail devices remains in place. In 2016, the FCC proposed to replace its CableCARD regime with burdensome new rules that would have required us to make disaggregated "information flows" available to set-top boxes and apps supplied by third parties. That proposal was not adopted, but various parties may continue to advocate alternative regulatory approaches to reduce consumer dependency on traditional operator provided set-top boxes. It remains uncertain whether the FCC or Congress will change the legal requirements related to our set-top boxes and what the impact of any such changes might be.



### ***Privacy and Information Security Regulation***

The Communications Act limits our ability to collect, use, and disclose subscribers' personally identifiable information for our video, voice, and Internet services, as well as provides requirements to safeguard such information. We are subject to additional federal, state, and local laws and regulations that impose additional restrictions on the collection, use and disclosure of consumer, subscriber and employee information. Further, the FCC, Federal Trade Commission ("FTC"), and many states regulate and restrict the marketing practices of communications service providers, including telemarketing and online marketing efforts. The FCC recently adopted privacy rules that contain new restrictions affecting the use of broadband and voice customer data, and various other federal agencies, including the FTC, continue to provide updated guidance on the use and protection of consumer data.

Our operations are also subject to federal and state laws governing information security, including new "reasonable" data security requirements set forth in the FCC's recently adopted privacy rules, which will become effective on March 3, 2017. In the event of an information security breach, such rules may require consumer and government agency notification and may result in regulatory enforcement actions with the potential of monetary forfeitures. The FCC has recently used the existing authority under its privacy and security requirements for telecommunications services to bring enforcement actions against several companies for failing to protect customer data from unauthorized access by and disclosure to third parties, resulting in substantial monetary settlements. Similarly, the FTC and state attorneys general regularly bring enforcement actions against companies related to information security breaches and privacy violations. Several state legislatures are considering the adoption of new data security and cybersecurity legislation that could result in additional network and information security requirements for our business.

Various security standards provide guidance to telecommunications companies in order to help identify and mitigate cybersecurity risk. One such standard is the voluntary framework released by the National Institute for Standards and Technologies ("NIST") in February 2014, in cooperation with other federal agencies and owners and operators of U.S. critical infrastructure. The NIST cybersecurity framework provides a prioritized and flexible model for organizations to identify and manage cyber risks inherent to their business. It was designed to supplement, not supersede, existing cybersecurity regulations and requirements. Several government agencies have encouraged compliance with the NIST cybersecurity framework, including the FCC, which is also considering expansion of its cybersecurity guidelines or the adoption of cybersecurity requirements. We cannot predict what proposals may be adopted or how new legislation and regulations, if any, would affect our business.

### ***MDUs / Inside Wiring***

The FCC has adopted a series of regulations designed to spur competition to established cable operators in MDU complexes. These regulations allow our competitors to access certain existing cable wiring inside MDUs. The FCC also adopted regulations limiting the ability of established cable operators, like us, to enter into exclusive service contracts for MDU complexes. In their current form, the FCC's regulations in this area favor our competitors.

### ***Pole Attachments***

The Communications Act requires most utilities owning utility poles to provide cable systems with access to poles and conduits and simultaneously subjects the rates charged for this access to either federal or state regulation. In 2011 and again in 2015, the FCC amended its existing pole attachment rules to promote broadband deployment. The 2011 order allows for new penalties in certain cases involving unauthorized attachments, but generally strengthens the cable industry's ability to access investor-owned utility poles on reasonable rates, terms, and conditions. Additionally, the 2011 order reduces the federal rate formula previously applicable to "telecommunications" attachments to closely approximate the rate formula applicable to "cable" attachments. The 2015 order continues the reconciliation of rates, effectively closing the remaining "loophole" that potentially allowed for significantly higher rates for telecommunications than for "cable" attachments in certain scenarios. Utility pole owners have appealed the 2015 order. Neither the 2011 order nor the 2015 order directly affect the rate in states that self-regulate (rather than allow the FCC to regulate pole rates), but many of those states have substantially the same rate for cable and telecommunications attachments.

Although the 2011 and 2015 orders do not impact the status quo treatment of cable-provided VoIP service as an unclassified service eligible for the favorable cable rate, the issue has not been fully resolved by the FCC, and a potential change in classification in a pending proceeding could adversely impact our pole attachment rates in states or for periods of time in which the cable rate is or was lower than the telecommunications rate. Additionally, although the FCC's 2015 reclassification of broadband Internet access as a telecommunications service also set forth the FCC's intention that pole rates not increase as result. That reclassification ruling could adversely impact our pole attachment rates in states or for periods of time in which the cable rate is or was lower than the telecommunications rate.



### ***Cable Rate Regulation***

Federal law strictly limits the potential scope of cable rate regulation. Pursuant to federal law, all video offerings are universally exempt from rate regulation, except for a cable system's minimum level of video programming service, referred to as "basic service," and associated equipment. Rate regulation of basic service and associated equipment operates pursuant to a federal formula, with local governments, commonly referred to as local franchising authorities, primarily responsible for administering this regulation. The majority of our local franchising authorities have never certified to regulate basic service cable rates. In 2015, the FCC adopted an order (which is now under appeal) reversing its historic approach to rate regulation certifications and requiring a local franchise authority interested in regulating cable rates to first make an affirmative showing that there is no "effective competition" (as defined under federal law) in the community. Very few local franchise authorities have filed the necessary rate regulation certification, and the FCC's 2015 order should make it more difficult for such entities to assert rate regulation in the future.

There have been calls to impose expanded rate regulation on the cable industry. Confronted with rapidly increasing cable programming costs, it is possible that Congress may adopt new constraints on the retail pricing or packaging of cable programming. Any such constraints could adversely affect our operations.

### ***Ownership Restrictions***

Federal regulation of the communications field traditionally included a host of ownership restrictions, which limited the size of certain media entities and restricted their ability to enter into competing enterprises. Through a series of legislative, regulatory, and judicial actions, most of these restrictions have been either eliminated or substantially relaxed. Changes in this regulatory area could alter the business environment in which we operate.

### ***Access Channels***

Local franchise agreements often require cable operators to set aside certain channels for public, educational, and governmental access programming. Federal law also requires cable systems to designate up to 15% of their channel capacity for commercial leased access by unaffiliated third parties, who may offer programming that our customers do not particularly desire. The FCC adopted revised rules in 2007 mandating a significant reduction in the rates that operators can charge commercial leased access users and imposing additional administrative requirements that would be burdensome on the cable industry. The effect of the FCC's revised rules was stayed by a federal court, pending a cable industry appeal and an adverse finding by the Office of Management and Budget. Although commercial leased access activity historically has been relatively limited, increased activity in this area could further burden the channel capacity of our cable systems.

### ***Other FCC Regulatory Matters***

FCC regulations cover a variety of additional areas, including, among other things: (1) equal employment opportunity obligations; (2) customer service standards; (3) technical service standards; (4) mandatory blackouts of certain network and syndicated programming; (5) restrictions on political advertising; (6) restrictions on advertising in children's programming; (7) licensing of systems and facilities; (8) maintenance of public files; (9) emergency alert systems; and (10) disability access, including new requirements governing video-description and closed-captioning. Each of these regulations restricts our business practices to varying degrees and may impose additional costs on our operations.

It is possible that Congress or the FCC will expand or modify its regulation of cable systems in the future, and we cannot predict at this time how that might impact our business.

### ***Copyright***

Cable systems are subject to a federal copyright compulsory license covering carriage of television and radio broadcast signals. The possible modification or elimination of this compulsory copyright license is the subject of continuing legislative proposals and administrative review and could adversely affect our ability to obtain desired broadcast programming.

Copyright clearances for non-broadcast programming services are arranged through private negotiations. Cable operators also must obtain music rights for locally originated programming and advertising from the major music performing rights organizations. These licensing fees have been the source of litigation in the past, and we cannot predict with certainty whether license fee disputes may arise in the future.



### ***Franchise Matters***

Our cable systems generally are operated pursuant to nonexclusive franchises, permits, and similar authorizations granted by a municipality or other state or local government entity in order to utilize and cross public rights-of-way. Cable franchises generally are granted for fixed terms and in many cases include monetary penalties for noncompliance and may be terminable if the franchisee fails to comply with material provisions. The specific terms and conditions of cable franchises vary significantly between jurisdictions. Cable franchises generally contain provisions governing cable operations, franchise fees, system construction, maintenance, technical performance, customer service standards, supporting and carrying public access channels, and changes in the ownership of the franchisee. A number of states subject cable systems to the jurisdiction of centralized state government agencies, such as public utility commissions. Although local franchising authorities have considerable discretion in establishing franchise terms, certain federal protections benefit cable operators. For example, federal law caps local franchise fees.

Prior to the scheduled expiration of our franchises, we generally initiate renewal proceedings with the granting authorities. The Communications Act of 1934, as amended (the "Communications Act"), which is the primary federal statute regulating interstate communications, provides for an orderly franchise renewal process in which granting authorities may not unreasonably withhold renewals. In connection with the franchise renewal process, however, many governmental authorities require the cable operator to make additional costly commitments. Historically, we have been able to renew our franchises without incurring significant costs, although any particular franchise may not be renewed on commercially favorable terms or otherwise. If we fail to obtain renewals of franchises representing a significant number of our customers, it could have a material adverse effect on our consolidated financial condition, results of operations, or our liquidity, including our ability to comply with our debt covenants. Similarly, if a local franchising authority's consent is required for the purchase or sale of a cable system, the local franchising authority may attempt to impose more burdensome requirements as a condition for providing its consent.

The traditional cable franchising regime has undergone significant change as a result of various federal and state actions. The FCC has adopted rules that streamline entry for new competitors (particularly those affiliated with telephone companies) and reduce certain franchising burdens for these new entrants. The FCC adopted more modest relief for existing cable operators.

At the same time, a substantial number of states have adopted new franchising laws. Again, these laws were principally designed to streamline entry for new competitors, and they often provide advantages for these new entrants that are not immediately available to existing cable operators. In many instances, these franchising regimes do not apply to established cable operators until the existing franchise expires or a competitor directly enters the franchise territory. The exact nature of these state franchising laws, and their varying application to new and existing video providers, will impact our franchising obligations and our competitive position.

### **Internet Service**

FCC regulations subject broadband Internet access services to certain regulations intended to ensure that end users can send and receive lawful Internet content without discrimination by Internet service providers such as us. Under these rules, providers of broadband Internet access service are not permitted to block access to, or restrict data rates for downloading, lawful content or ban the attachment of non-harmful devices to our service except to the extent required by reasonable network management practices. Internet service providers are also not permitted to give special priority to the transmission of content from our affiliates or accept payment from third parties to give special priority their content. Furthermore, Internet service providers are subject to a general obligation not to take actions that unreasonably interfere with the ability of end users (such as our subscribers) and edge providers (such as web sites) to exchange data with each other. The FCC has also stated that it will investigate problems that may arise regarding interconnection of the networks of retail broadband Internet access providers with "upstream" providers of Internet connectivity. In addition, the FCC rules require that we meet certain "transparency" obligations, i.e., that we disclose material technical and other terms and conditions applicable to our Internet service. These FCC regulations were upheld by the D.C. Circuit in June 2016, but remain subject to additional appeals. We cannot predict how those ongoing appeals will be resolved. Moreover, it is possible that Congress or the FCC will modify or repeal the existing regulations.

We cannot predict how the FCC will enforce its regulations in particular cases or whether in the future the FCC may seek to expand the scope of its regulatory obligations on Internet access service providers. In addition to the regulatory obligations noted above, providers of broadband Internet access service are obliged by the Communications Assistance for Law Enforcement Act (CALEA) to configure their networks in a manner that facilitates the ability of law enforcement, with proper legal authorization, to obtain information about our customers, including the content of their Internet communications. The FCC and Congress also are considering subjecting Internet access services to the Universal Service funding requirements. These funding requirements could impose significant new costs on our Internet service. Also, the FCC and some state regulatory commissions direct certain subsidies to telephone companies deploying broadband to areas deemed to be "unserved" or "underserved." We have opposed such subsidies when directed to areas that we serve. Despite our efforts, future subsidies may be directed to areas served by us, which could



result in subsidized competitors operating in our service territories. State and local governmental organizations have also adopted Internet-related regulations. These various governmental jurisdictions are also considering additional regulations in these and other areas, such as privacy, pricing, service and product quality, and taxation. The adoption of new Internet regulations or the adaptation of existing laws to the Internet could adversely affect our business.

Aside from the FCC's generally applicable regulations, we have made certain commitments to comply with the FCC's order in connection with the FCC's approval of the TWC Transaction and the Bright House Transaction (discussed above).

The FCC is considering whether online video distributors ("OVDs") that offer programming to customers with a broadband Internet connection should be classified as multichannel video programming distributors ("MVPDs"), and thereby subject to the program access protections available to MVPDs, as well as some of the regulatory requirements applicable to MVPDs. The outcome of this proceeding, which could impact how OVDs compete in the future with traditional cable service, cannot be determined at the current time.

### **Voice Service**

The Telecommunications Act of 1996 created a more favorable regulatory environment for us to provide telecommunications and/or competitive voice services than had previously existed. In particular, it established requirements ensuring that competitive telephone companies could interconnect their networks with those providers of traditional telecommunications services to open the market to competition. The FCC has subsequently ruled that competitive telephone companies that support VoIP services, such as those we offer our customers, are entitled to interconnection with incumbent providers of traditional telecommunications services, which ensures that our VoIP services can compete in the market. Since that time, the FCC has initiated a proceeding to determine whether such interconnection rights should extend to traditional and competitive networks utilizing IP technology, and how to encourage the transition to IP networks throughout the industry. New rules or obligations arising from these proceedings may affect our ability to compete in the provision of voice services.

The FCC has collected extensive data from providers of point to point transport ("special access") services, such as us, and the FCC may use that data to evaluate whether the market for such services is competitive, or whether the market should be subject to further regulation, which may increase our costs or constrain our ability to compete in this market. The FCC also recently selected a new national local number portability administrator, and the change to that new administrator may adversely impact our ability to manage number porting and related tasks.

Further regulatory changes are being considered that could impact our voice business and that of our primary telecommunications competitors. The FCC and state regulatory authorities are considering, for example, whether certain common carrier regulations traditionally applied to incumbent local exchange carriers should be modified or reduced, and the extent to which common carrier requirements should be extended to VoIP providers. The FCC has already determined that certain providers of voice services using Internet Protocol technology must comply with requirements relating to 911 emergency services ("E911"), the CALEA (the statute governing law enforcement access to and surveillance of communications), Universal Service Fund contributions, customer privacy and Customer Proprietary Network Information issues, number portability, network outage reporting, rural call completion, disability access, regulatory fees, and discontinuance of service. In November 2014, the FCC adopted an order imposing limited back-up power obligations on providers of facilities-based fixed, residential voice services that are not otherwise line-powered, including our VoIP services. This order became effective in February 2016 and requires us to disclose certain information to customers and to make back-up power available at the point of sale. In March 2007, a federal appeals court affirmed the FCC's decision concerning federal regulation of certain VoIP services, but declined to specifically find that VoIP service provided by cable companies, such as we provide, should be regulated only at the federal level. As a result, some states have begun proceedings to subject cable VoIP services to state level regulation, and at least one state has asserted jurisdiction over our VoIP services. We have filed a legal challenge to that state's assertion of jurisdiction, which is now pending before a federal district court in Minnesota. Although we have registered with, or obtained certificates or authorizations from the FCC and the state regulatory authorities in those states in which we offer competitive voice services in order to ensure the continuity of our services and to maintain needed network interconnection arrangements, it is unclear whether and how these and other ongoing regulatory matters ultimately will be resolved.

## Transaction-Related Commitments

In connection with approval of the Transactions, federal and state regulators imposed a number of post-merger conditions on us including but not limited to the following.

### *FCC Conditions*

- Offer settlement-free Internet interconnection to any party that meets the requirements of our Interconnection Policy (available on Charter's website) on terms generally consistent with the policy for seven years (with a possible reduction to five);
- Deploy and offer high-speed broadband Internet access service to an additional two million locations over five years, at least one million of which must be in areas outside our footprint that face competition from another high-speed Internet provider;
- Refrain from charging usage-based prices or imposing data caps on any fixed mass market broadband Internet access service plans for seven years (with a possible reduction to five);
- Offer 30/4 Mbps discounted broadband where technically feasible to eligible customers throughout our service area for four years from the offer's commencement; and
- Continue to provide CableCARDS to any new or existing customer upon request for use in third-party retail devices for four years-and continue to support such CableCARDS for seven years (in each case, unless the FCC changes the relevant rules).

The FCC conditions also contain a number of compliance reporting requirements.

### *DOJ Conditions*

The Department of Justice ("DOJ") Order prohibits us from entering into or enforcing any agreement with a video programmer that forbids, limits or creates incentives to limit the video programmer's provision of content to OVDs. We will not be able to avail ourselves of other distributors' most favored nation ("MFN") provisions if they are inconsistent with this prohibition. The DOJ's conditions are effective for seven years, although we may petition the DOJ to eliminate the conditions after five years.

### *State Conditions*

Certain state regulators, including California, New York, Hawaii and New Jersey also imposed conditions in connection with the approval of the Transactions. These conditions include requirements related to:

- Upgrading networks within the designated state, including upgrades to broadband speeds and conversion of all households served within California and New York to an all-digital platform;
- Building out our network to households and business locations that are not currently served by cable within the designated states;
- Offering LifeLine service discounts and low-income broadband to eligible households served within the applicable states;
- Investing in service improvement programs and customer service enhancements and maintaining customer-facing jobs within the designated state;
- Continuing to make legacy service offerings available, including allowing Legacy TWC and Legacy Bright House customers to maintain their existing service offerings for a period of three years; and
- Complying with reporting requirements.

## Employees

As of December 31, 2016, we had approximately 91,500 active full-time equivalent employees. At December 31, 2016, approximately 2,500 of our employees were represented by collective bargaining agreements. We believe we have good relations with our employees including those represented by collective bargaining agreements.

## Item 1A. Risk Factors.

### Risks Related to the Integration of the Transactions

*If we are not able to successfully integrate our business with that of Legacy TWC and Legacy Bright House within the anticipated time frame, or at all, the anticipated cost savings and other benefits of the Transactions may not be realized fully, or at all, or*



*may take longer to realize than expected. In such circumstance, we may not perform as expected and the value of Charter's Class A common stock may be adversely affected.*

Until the closing of the Transactions, Legacy Charter, Legacy TWC and Legacy Bright House operated independently, and there can be no assurances that their businesses can be integrated successfully. We now have significantly more systems, assets, investments, businesses, customers and employees than each company did prior to the Transactions. It is possible that the integration process could result in the loss of key Charter employees, the loss of customers, the disruption of our ongoing businesses or in unexpected integration issues, higher than expected integration costs and an overall post-completion integration process that takes longer than originally anticipated. The process of integrating Legacy TWC and Legacy Bright House with the Legacy Charter operations will require significant capital expenditures and the expansion of certain operations and operating and financial systems. Management will be required to devote a significant amount of time and attention to the integration process and there is a significant degree of difficulty and management involvement inherent in that process. These difficulties include:

- integrating the companies' operations and corporate functions;
- integrating the companies' technologies, networks and customer service platforms;
- integrating and unifying the product offerings and services available to customers, including customer premise equipment and video user interfaces;
- harmonizing the companies' operating practices, employee development and compensation programs, internal controls and other policies, procedures and processes;
- maintaining existing relationships and agreements with customers, providers, programmers and other vendors and avoiding delays in entering into new agreements with prospective customers, providers and vendors;
- addressing possible differences in business backgrounds, corporate cultures and management philosophies;
- consolidating the companies' administrative and information technology infrastructure;
- coordinating programming and marketing efforts;
- coordinating geographically dispersed organizations;
- integrating information, purchasing, provisioning, accounting, finance, sales, billing, payroll, reporting and regulatory compliance systems;
- completing the conversion of analog systems to all-digital for the Legacy TWC and Legacy Bright House systems; and
- attracting and retaining the necessary personnel associated with the acquired assets.

Even if the new businesses are successfully integrated, it may not be possible to realize the benefits that are expected to result from the Transactions, or realize these benefits within the time frame that is expected. For example, the elimination of duplicative costs may not be possible or may take longer than anticipated, or the benefits from the Transactions may be offset by costs incurred or delays in integrating the businesses and increased operating costs. If the combined company fails to realize the anticipated benefits from the transactions, our liquidity, results of operations, financial condition and/or share price may be adversely affected. In addition, at times, the attention of certain members of our management and resources may be focused on the integration of the businesses and diverted from day-to-day business operations, which may disrupt the business of the combined company.

*If the operating results of Legacy TWC and/or Legacy Bright House are less than our expectations, or an increase in the capital expenditures to upgrade and maintain those assets as well as to keep pace with technological developments are greater than expected, we may not achieve the expected level of financial results from the Transactions.*

We will derive a portion of our continuing revenues and earnings per share from the operations of Legacy TWC and Legacy Bright House. Therefore, any negative impact on these companies or the operating results derived from such companies could harm the combined company's operating results.

Our business and the businesses of Legacy TWC and Legacy Bright House are characterized by rapid technological change and the introduction of new products and services. We intend to make investments in the combined business and transition toward only using two-way all-digital set-top boxes. The increase in capital expenditures necessary for the transition toward two-way set-top boxes in the business may negatively impact the expected financial results from the Transactions. The combined company may not be able to fund the capital expenditures necessary to keep pace with technological developments, execute the plans to do so, or anticipate the demand of its customers for products and services requiring new technology or bandwidth. Our inability to maintain, expand and upgrade our existing or combined businesses could materially adversely affect our financial condition and results of operations.

The Transactions were accounted for as an acquisition in accordance with accounting principles generally accepted in the United States. Under the acquisition method of accounting, the assets and liabilities of Legacy TWC and Legacy Bright House have been recorded, as of the date of completion of the Transactions, at their respective fair values and added to our assets and liabilities.



The excess of the purchase price over those fair values has been recorded as goodwill. To the extent the value of goodwill or intangibles becomes impaired, we may be required to incur material charges relating to such impairment. Such a potential impairment charge could have a material impact on our operating results.

*As a result of the closing of the Transactions, our businesses are subject to the conditions set forth in the FCC Order and the DOJ Consent Decree and those imposed by state utility commissions and local franchise authorities, and there can be no assurance that these conditions will not have an adverse effect on our businesses and results of operations.*

In connection with the Transactions, the FCC Order, the DOJ Consent Decree, and the approvals from state utility commissions and local franchise authorities incorporated numerous commitments and voluntary conditions made by the parties and imposed numerous conditions on our businesses relating to the operation of our business and other matters. Among other things, (i) we will not be permitted to charge usage-based prices or impose data caps and will be prohibited from charging interconnection fees for qualifying parties; (ii) we will be prohibited from entering into or enforcing any agreement with a programmer that forbids, limits or creates incentives to limit the programmer's provision of content to OVD and cannot retaliate against programmers for licensing to OVDs; (iii) we will not be able to avail ourselves of other distributors' most favored nation ("MFN") provisions if they are inconsistent with this prohibition; (iv) we must undertake a number of actions designed to promote diversity; (v) we must appoint an independent compliance monitor and comply with a broad array of reporting requirements; and (v) we must satisfy various other conditions relating to our Internet services, including building out an additional two million locations with access to a high-speed connection of at least 60 megabits per second with at least one million of those connections in competition with another high-speed broadband provider in the market served, and implementing a reduced price high-speed Internet program for low income families. These and other conditions and commitments relating to the Transactions are of varying duration, ranging from three to seven years. In light of the breadth and duration of the conditions and potential changes in market conditions during the time the conditions and commitments are in effect, there can be no assurance that our compliance, and ability to comply, with the conditions will not have a material adverse effect on our business or results of operations.

#### **Risks Related to Our Indebtedness**

*We have a significant amount of debt and may incur significant additional debt, including secured debt, in the future, which could adversely affect our financial health and our ability to react to changes in our business.*

We have a significant amount of debt and may (subject to applicable restrictions in our debt instruments) incur additional debt in the future. As of December 31, 2016, our total principal amount of debt was approximately \$60.0 billion.

Our significant amount of debt could have consequences, such as:

- impact our ability to raise additional capital at reasonable rates, or at all;
- make us vulnerable to interest rate increases, in part because approximately 13% of our borrowings as of December 31, 2016 were, and may continue to be, subject to variable rates of interest;
- expose us to increased interest expense to the extent we refinance existing debt with higher cost debt;
- require us to dedicate a significant portion of our cash flow from operating activities to make payments on our debt, reducing our funds available for working capital, capital expenditures, and other general corporate expenses;
- limit our flexibility in planning for, or reacting to, changes in our business, the cable and telecommunications industries, and the economy at large;
- place us at a disadvantage compared to our competitors that have proportionately less debt; and
- adversely affect our relationship with customers and suppliers.

If current debt amounts increase, our business results are lower than expected, or credit rating agencies downgrade our debt limiting our access to investment grade markets, the related risks that we now face will intensify.

*The agreements and instruments governing our debt contain restrictions and limitations that could significantly affect our ability to operate our business, as well as significantly affect our liquidity.*

Our credit facilities and the indentures governing our debt contain a number of significant covenants that could adversely affect our ability to operate our business, our liquidity, and our results of operations. These covenants restrict, among other things, our and our subsidiaries' ability to:

- incur additional debt;
- repurchase or redeem equity interests and debt;
- issue equity;



- make certain investments or acquisitions;
- pay dividends or make other distributions;
- dispose of assets or merge;
- enter into related party transactions; and
- grant liens and pledge assets.

Additionally, the Charter Operating credit facilities require Charter Operating to comply with a maximum total leverage covenant and a maximum first lien leverage covenant. The breach of any covenants or obligations in our indentures or credit facilities, not otherwise waived or amended, could result in a default under the applicable debt obligations and could trigger acceleration of those obligations, which in turn could trigger cross defaults under other agreements governing our long-term indebtedness. In addition, the secured lenders under our notes and the Charter Operating credit facilities could foreclose on their collateral, which includes equity interests in our subsidiaries, and exercise other rights of secured creditors.

***We depend on generating sufficient cash flow to fund our debt obligations, capital expenditures, and ongoing operations.***

We are dependent on our cash on hand and cash flow from operations to fund our debt obligations, capital expenditures and ongoing operations. Our ability to service our debt and to fund our planned capital expenditures and ongoing operations will depend on our ability to continue to generate cash flow and our access (by dividend or otherwise) to additional liquidity sources at the applicable obligor. Our ability to continue to generate cash flow is dependent on many factors, including:

- our ability to sustain and grow revenues and cash flow from operations by offering video, Internet, voice, advertising and other services to residential and commercial customers, to adequately meet the customer experience demands in our markets and to maintain and grow our customer base, particularly in the face of increasingly aggressive competition, the need for innovation and the related capital expenditures;
- the impact of competition from other market participants, including but not limited to incumbent telephone companies, direct broadcast satellite operators, wireless broadband and telephone providers, DSL providers, video provided over the Internet and providers of advertising over the Internet;
- general business conditions, economic uncertainty or downturn, high unemployment levels and the level of activity in the housing sector;
- our ability to obtain programming at reasonable prices or to raise prices to offset, in whole or in part, the effects of higher programming costs (including retransmission consents);
- the development and deployment of new products and technologies including our cloud-based user interface, Spectrum Guide®;
- the effects of governmental regulation on our business or potential business combination transactions; and
- any events that disrupt our networks, information systems or properties and impair our operating activities and negatively impact our reputation.

Some of these factors are beyond our control. If we are unable to generate sufficient cash flow or we are unable to access additional liquidity sources, we may not be able to service and repay our debt, operate our business, respond to competitive challenges, or fund our other liquidity and capital needs.

***Restrictions in our subsidiaries' debt instruments and under applicable law limit their ability to provide funds to us and our subsidiaries that are debt issuers.***

Our primary assets are our equity interests in our subsidiaries. Our operating subsidiaries are separate and distinct legal entities and are not obligated to make funds available to their debt issuer holding companies for payments on our notes or other obligations in the form of loans, distributions, or otherwise. Charter Operating's ability to make distributions to Charter or CCO Holdings, our other primary debt issuers other than TWC, LLC and TWCE, to service debt obligations is subject to its compliance with the terms of its credit facilities, and restrictions under applicable law. TWC, LLC's and TWCE's ability to make distributions to Charter, CCO Holdings or Charter Operating to service debt obligations is subject to restrictions under applicable law. See Note 9 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data." Under the Delaware Limited Liability Company Act (the "Act"), our subsidiaries may only make distributions if the relevant entity has "surplus" as defined in the Act. Under fraudulent transfer laws, our subsidiaries may not pay dividends if the relevant entity is insolvent or is rendered insolvent thereby. The measures of insolvency for purposes of these fraudulent transfer laws vary depending upon the law applied in any proceeding to determine whether a fraudulent transfer has occurred. Generally, however, an entity would be considered insolvent if:

- the sum of its debts, including contingent liabilities, was greater than the fair saleable value of all its assets;



- the present fair saleable value of its assets was less than the amount that would be required to pay its probable liability on its existing debts, including contingent liabilities, as they become absolute and mature: or
- it could not pay its debts as they became due.

We believe that our relevant subsidiaries currently have surplus and are not insolvent, however, these subsidiaries may become insolvent in the future. Our direct or indirect subsidiaries include the borrowers and guarantors under the Charter Operating credit facilities and notes, under the CCO Holdings notes and under the TWC, LLC and TWCE notes. As of December 31, 2016, our total principal amount of debt was approximately \$60.0 billion.

In the event of bankruptcy, liquidation, or dissolution of one or more of our subsidiaries, that subsidiary's assets would first be applied to satisfy its own obligations, and following such payments, such subsidiary may not have sufficient assets remaining to make payments to its parent company as an equity holder or otherwise. In that event, the lenders under Charter Operating's credit facilities and notes and any other indebtedness of our subsidiaries whose interests are secured by substantially all of our operating assets, and all holders of other debt of Charter Operating, CCO Holdings, TWC, LLC and TWCE will have the right to be paid in full before us from any of our subsidiaries' assets.

*Some of our outstanding debt is subject to change of control provisions. We may not have the ability to raise the funds necessary to fulfill our obligations under our indebtedness following a change of control, which would place us in default under the applicable debt instruments.*

We may not have the ability to raise the funds necessary to fulfill our obligations under our notes and our credit facilities following a change of control. Under the indentures governing the CCO Holdings' notes, upon the occurrence of specified change of control events, the debt issuer is required to offer to repurchase all of its outstanding notes. However, we may not have sufficient access to funds at the time of the change of control event to make the required repurchase of the applicable notes, and Charter Operating is limited in its ability to make distributions or other payments to any debt issuer to fund any required repurchase. In addition, a change of control under the Charter Operating credit facilities would result in a default under those credit facilities, which would trigger a default under the indentures governing the CCO Holdings' notes, the Charter Operating notes and the TWC, LLC and TWCE notes. Because such credit facilities and notes are obligations of Charter Operating and its subsidiaries, the credit facilities would have to be repaid before Charter Operating's assets could be available to CCO Holdings to repurchase their notes. Any failure to make or complete a change of control offer would place CCO Holdings in default under their notes. The failure of our subsidiaries to make a change of control offer or repay the amounts accelerated under their notes and credit facilities would place them in default under such agreements.

## **Risks Related to Our Business**

*We operate in a very competitive business environment, which affects our ability to attract and retain customers and can adversely affect our business, operations and financial results.*

The industry in which we operate is highly competitive and has become more so in recent years. In some instances, we compete against companies with fewer regulatory burdens, better access to financing, greater personnel resources, greater resources for marketing, greater and more favorable brand name recognition, and long-established relationships with regulatory authorities and customers. Increasing consolidation in the cable industry and the repeal of certain ownership rules have provided additional benefits to certain of our competitors, either through access to financing, resources, or efficiencies of scale.

Our residential video service faces competition from a number of sources, including direct broadcast satellite services, as well as other companies that deliver movies, television shows and other video programming over broadband Internet connections to TVs, computers, tablets and mobile devices. Our residential Internet service faces competition from the phone companies' DSL, FTTH and wireless broadband offerings as well as from a variety of companies that offer other forms of online services, including wireless and satellite-based broadband services. Our residential voice service competes with wireless and wireline phone providers, as well as other forms of communication, such as text messaging on cellular phones, instant messaging, social networking services, video conferencing and email. Competition from these companies, including intensive marketing efforts with aggressive pricing, exclusive programming and increased HD broadcasting may have an adverse impact on our ability to attract and retain customers.

Overbuilds could also adversely affect our growth, financial condition, and results of operations, by creating or increasing competition. We are aware of traditional overbuild situations impacting certain of our markets, however, we are unable to predict the extent to which additional overbuild situations may occur.

Our services may not allow us to compete effectively. Competition may reduce our expected growth of future cash flows which may contribute to future impairments of our franchises and goodwill and our ability to meet cash flow requirements, including



debt service requirements. For additional information regarding the competition we face, see “Business —Competition” and “—Regulation and Legislation.”

*We face risks relating to competition for the leisure time and discretionary spending of audiences, which has intensified in part due to advances in technology and changes in consumer expectations and behavior.*

In addition to the various competitive factors discussed above, we are subject to risks relating to increasing competition for the leisure time, shifting consumer needs and discretionary spending of consumers. We compete with all other sources of entertainment, news and information delivery, as well as a broad range of communications products and services. Technological advancements, such as new video formats and Internet streaming and downloading of programming that can be viewed on televisions, computers, smartphones and tablets, many of which have been beneficial to us, have nonetheless increased the number of entertainment and information delivery choices available to consumers and intensified the challenges posed by audience fragmentation.

Newer products and services, particularly alternative methods for the distribution, sale and viewing of content will likely continue to be developed, further increasing the number of competitors that we face. The increasing number of choices available to audiences, including low-cost or free choices, could negatively impact not only consumer demand for our products and services, but also advertisers’ willingness to purchase advertising from us. We compete for the sale of advertising revenue with television networks and stations, as well as other advertising platforms, such as radio, print and, increasingly, online media. Our failure to effectively anticipate or adapt to new technologies and changes in consumer expectations and behavior could significantly adversely affect our competitive position and our business and results of operations.

*Our exposure to the economic conditions of our current and potential customers, vendors and third parties could adversely affect our cash flow, results of operations and financial condition.*

We are exposed to risks associated with the economic conditions of our current and potential customers, the potential financial instability of our customers and their financial ability to purchase our products. If there were a general economic downturn, we may experience increased cancellations by our customers or unfavorable changes in the mix of products purchased, including an increase in the number of homes that replace their video service with Internet-delivered and/or over-air content, which would negatively impact our ability to attract customers, increase rates and maintain or increase revenue. In addition, providing video services is an established and highly penetrated business. Our ability to gain new video subscribers is dependent to a large extent on growth in occupied housing in our service areas, which is influenced by both national and local economic conditions. Weak economic conditions may also have a negative impact on our advertising revenue. These events have adversely affected us in the past, and may adversely affect our cash flow, results of operations and financial condition if a downturn were to occur.

In addition, we are susceptible to risks associated with the potential financial instability of the vendors and third parties on which we rely to provide products and services or to which we outsource certain functions. The same economic conditions that may affect our customers, as well as volatility and disruption in the capital and credit markets, also could adversely affect vendors and third parties and lead to significant increases in prices, reduction in output or the bankruptcy of our vendors or third parties upon which we rely. Any interruption in the services provided by our vendors or by third parties could adversely affect our cash flow, results of operation and financial condition.

*We face risks inherent in our commercial business.*

We may encounter unforeseen difficulties as we increase the scale of our service offerings to businesses. We sell Internet access, data networking and fiber connectivity to cellular towers and office buildings, video and business voice services to businesses and have increased our focus on growing this business. In order to grow our commercial business, we expect to continue investment in technology, equipment and personnel focused on the commercial business. Commercial business customers often require service level agreements and generally have heightened customer expectations for reliability of services. If our efforts to build the infrastructure to scale the commercial business are not successful, the growth of our commercial services business would be limited. We depend on interconnection and related services provided by certain third parties for the growth of our commercial business. As a result, our ability to implement changes as the services grow may be limited. If we are unable to meet these service level requirements or expectations, our commercial business could be adversely affected. Finally, we expect advances in communications technology, as well as changes in the marketplace and the regulatory and legislative environment. Consequently, we are unable to predict the effect that ongoing or future developments in these areas might have on our voice and commercial businesses and operations.

*Programming costs are rising at a much faster rate than wages or inflation, and we may not have the ability to reduce or moderate the growth rates of, or pass on to our customers, our increasing programming costs, which would adversely affect our cash flow and operating margins.*

Video programming has been, and is expected to continue to be, our largest operating expense item. In recent years, the cable industry has experienced a rapid escalation in the cost of programming. We expect programming costs to continue to increase because of a variety of factors including amounts paid for broadcast station retransmission consent, annual increases imposed by programmers and carriage of incremental programming, including new services and VOD programming. The inability to fully pass programming cost increases on to our customers has had, and is expected in the future to have, an adverse impact on our cash flow and operating margins associated with the video product. We have programming contracts that have expired and others that will expire at or before the end of 2017. There can be no assurance that these agreements will be renewed on favorable or comparable terms. Three programmers have filed lawsuits against us regarding which legacy programming arrangements apply after the closing of the Transactions, and there can be no assurance that other programmers will not bring similar suits in the future. In addition, a number of programmers have begun to sell their services through alternative distribution channels which may cause those programmers to seek even higher programming fees from us as this may degrade security of their product, increase their operating costs or reduce their advertising revenue. To the extent that we are unable to reach agreement with certain programmers on terms that we believe are reasonable, we have been, and may be in the future, forced to remove such programming channels from our line-up, which may result in a loss of customers. Our failure to carry programming that is attractive to our subscribers could adversely impact our customer levels, operations and financial results. In addition, if our Internet customers are unable to access desirable content online because content providers block or limit access by our subscribers as a class, our ability to gain and retain customers, especially Internet customers, may be negatively impacted.

Increased demands by owners of some broadcast stations for carriage of other services or payments to those broadcasters for retransmission consent are likely to further increase our programming costs. Federal law allows commercial television broadcast stations to make an election between "must-carry" rights and an alternative "retransmission-consent" regime. When a station opts for the retransmission consent regime, we are not allowed to carry the station's signal without the station's permission. In some cases, we carry stations under short-term arrangements while we attempt to negotiate new long-term retransmission agreements. If negotiations with these programmers prove unsuccessful, they could require us to cease carrying their signals, possibly for an indefinite period. Any loss of stations could make our video service less attractive to customers, which could result in less subscription and advertising revenue. In retransmission-consent negotiations, broadcasters often condition consent with respect to one station on carriage of one or more other stations or programming services in which they or their affiliates have an interest. Carriage of these other services, as well as increased fees for retransmission rights, may increase our programming expenses and diminish the amount of capacity we have available to introduce new services, which could have an adverse effect on our business and financial results.

*Our inability to respond to technological developments and meet customer demand for new products and services could adversely affect our ability to compete effectively.*

We operate in a highly competitive, consumer-driven and rapidly changing environment. Our success is, to a large extent, dependent on our ability to acquire, develop, adopt, upgrade and exploit new and existing technologies to address consumers' changing demands and distinguish our services from those of our competitors. We may not be able to accurately predict technological trends or the success of new products and services. If we choose technologies or equipment that are less effective, cost-efficient or attractive to customers than those chosen by our competitors, if we offer services that fail to appeal to consumers, are not available at competitive prices or that do not function as expected, or we are not able to fund the expenditures necessary to keep pace with technological developments, our competitive position could deteriorate, and our business and financial results could suffer.

The ability of some of our competitors to introduce new technologies, products and services more quickly than we do may adversely affect our competitive position. Furthermore, advances in technology, decreases in the cost of existing technologies or changes in competitors' product and service offerings may require us in the future to make additional research and development expenditures or to offer at no additional charge or at a lower price certain products and services that we currently offer to customers separately or at a premium. In addition, the uncertainty of our ability, and the costs, to obtain intellectual property rights from third parties could impact our ability to respond to technological advances in a timely and effective manner.

The implementation of our network-based user interface, Spectrum Guide may ultimately be unsuccessful or more expensive than anticipated. Our inability to maintain and expand our upgraded systems and provide advanced services such as a state of the art user interface in a timely manner, or to anticipate the demands of the marketplace, could materially adversely affect our ability to attract and retain customers. Consequently, our growth, financial condition and results of operations could suffer materially.



*We depend on third party service providers, suppliers and licensors; thus, if we are unable to procure the necessary services, equipment, software or licenses on reasonable terms and on a timely basis, our ability to offer services could be impaired, and our growth, operations, business, financial results and financial condition could be materially adversely affected.*

We depend on a limited number of third party service providers, suppliers and licensors to supply some of the services, hardware, software and operational support necessary to provide some of our services. Some of our hardware, software and operational support vendors, and service providers represent our sole source of supply or have, either through contract or as a result of intellectual property rights, a position of some exclusivity. If any of these parties breaches or terminates its agreement with us or otherwise fails to perform its obligations in a timely manner, demand exceeds these vendors' capacity, they experience operating or financial difficulties, they significantly increase the amount we pay for necessary products or services, or they cease production of any necessary product due to lack of demand, profitability or a change in ownership or are otherwise unable to provide the equipment or services we need in a timely manner, at our specifications and at reasonable prices, our ability to provide some services might be materially adversely affected, or the need to procure or develop alternative sources of the affected materials or services might delay our ability to serve our customers. In addition, the existence of only a limited number of vendors of key technologies can lead to less product innovation and higher costs. These events could materially and adversely affect our ability to retain and attract customers and our operations, business, financial results and financial condition.

Our cable systems have historically been restricted to using one of two proprietary conditional access security systems, which we believe has limited the number of manufacturers producing set-top boxes for such systems. As an alternative, we developed a new conditional access security system which can be downloaded into set-top boxes with features we specify that could be provided by a variety of manufacturers. We refer to our specified set-top box as our Worldbox. Additionally, we are developing technology to allow our two current proprietary conditional access security systems to be software downloadable into our Worldbox. In order to realize the broadest benefits of our Worldbox technology, we must now complete the support for the downloadable proprietary conditional access security systems within the Worldbox. We cannot provide assurances that this implementation will ultimately be successful or completed in the expected timeframe or at the expected budget.

*Our business may be adversely affected if we cannot continue to license or enforce the intellectual property rights on which our business depends.*

We rely on patent, copyright, trademark and trade secret laws and licenses and other agreements with our employees, customers, suppliers and other parties to establish and maintain our intellectual property rights in technology and the products and services used in our operations. Also, because of the rapid pace of technological change, we both develop our own technologies, products and services and rely on technologies developed or licensed by third parties. However, any of our intellectual property rights could be challenged or invalidated, or such intellectual property rights may not be sufficient to permit us to take advantage of current industry trends or otherwise to provide competitive advantages, which could result in costly redesign efforts, discontinuance of certain product or service offerings or other competitive harm. We may not be able to obtain or continue to obtain licenses from these third parties on reasonable terms, if at all. In addition, claims of intellectual property infringement could require us to enter into royalty or licensing agreements on unfavorable terms, incur substantial monetary liability or be enjoined preliminarily or permanently from further use of the intellectual property in question, which could require us to change our business practices or offerings and limit our ability to compete effectively. Even unsuccessful claims can be time-consuming and costly to defend and may divert management's attention and resources away from our business. In recent years, the number of intellectual property infringement claims has been increasing in the communications and entertainment industries, and, with increasing frequency, we are party to litigation alleging that certain of our services or technologies infringe the intellectual property rights of others.

*Various events could disrupt our networks, information systems or properties and could impair our operating activities and negatively impact our reputation and financial results.*

Network and information systems technologies are critical to our operating activities, both for our internal uses, such as network management and supplying services to our customers, including customer service operations and programming delivery. Network or information system shutdowns or other service disruptions caused by events such as computer hacking, dissemination of computer viruses, worms and other destructive or disruptive software, "cyber attacks," process breakdowns, denial of service attacks and other malicious activity pose increasing risks. Both unsuccessful and successful "cyber attacks" on companies have continued to increase in frequency, scope and potential harm in recent years. While we develop and maintain systems seeking to prevent systems-related events and security breaches from occurring, the development and maintenance of these systems is costly and requires ongoing monitoring and updating as techniques used in such attacks become more sophisticated and change frequently. We, and the third parties on which we rely, may be unable to anticipate these techniques or implement adequate preventive measures. While from time to time attempts have been made to access our network, these attempts have not as yet resulted in any material release of information, degradation or disruption to our network and information systems.



Our network and information systems are also vulnerable to damage or interruption from power outages, telecommunications failures, accidents, natural disasters (including extreme weather arising from short-term or any long-term changes in weather patterns), terrorist attacks and similar events. Further, the impacts associated with extreme weather or long-term changes in weather patterns, such as rising sea levels or increased and intensified storm activity, may cause increased business interruptions or may require the relocation of some of our facilities. Our system redundancy may be ineffective or inadequate, and our disaster recovery planning may not be sufficient for all eventualities.

Any of these events, if directed at, or experienced by, us or technologies upon which we depend, could have adverse consequences on our network, our customers and our business, including degradation of service, service disruption, excessive call volume to call centers, and damage to our or our customers' equipment and data. Large expenditures may be necessary to repair or replace damaged property, networks or information systems or to protect them from similar events in the future. Moreover, the amount and scope of insurance that we maintain against losses resulting from any such events or security breaches may not be sufficient to cover our losses or otherwise adequately compensate us for any disruptions to our business that may result. Any such significant service disruption could result in damage to our reputation and credibility, customer dissatisfaction and ultimately a loss of customers or revenue. Any significant loss of customers or revenue, or significant increase in costs of serving those customers, could adversely affect our growth, financial condition and results of operations.

Furthermore, our operating activities could be subject to risks caused by misappropriation, misuse, leakage, falsification or accidental release or loss of information maintained in our information technology systems and networks and those of our third-party vendors, including customer, personnel and vendor data. We provide certain confidential, proprietary and personal information to third parties in connection with our business, and there is a risk that this information may be compromised.

As a result of the increasing awareness concerning the importance of safeguarding personal information, the potential misuse of such information and legislation that has been adopted or is being considered regarding the protection, privacy and security of personal information, information-related risks are increasing, particularly for businesses like ours that process, store and transmit large amount of data, including personal information for our customers. We could be exposed to significant costs if such risks were to materialize, and such events could damage our reputation, credibility and business and have a negative impact on our revenue. We could be subject to regulatory actions and claims made by consumers in private litigations involving privacy issues related to consumer data collection and use practices. We also could be required to expend significant capital and other resources to remedy any such security breach.

The risk described above may be increased during the period in which we are integrating our people, processes and systems as a result of the Transactions.

*For tax purposes, Charter could experience a deemed ownership change in the future that could limit its ability to use its tax loss carryforwards.*

Charter had approximately \$11.2 billion of federal tax net operating loss carryforwards resulting in a gross deferred tax asset of approximately \$3.9 billion as of December 31, 2016. These losses resulted from the operations of Charter Communications Holdings Company, LLC ("Charter Holdco") and its subsidiaries and from loss carryforwards received as a result of the TWC Transaction. Federal tax net operating loss carryforwards expire in the years 2018 through 2035. In addition, Charter had state tax net operating loss carryforwards resulting in a gross deferred tax asset (net of federal tax benefit) of approximately \$304 million as of December 31, 2016. State tax net operating loss carryforwards generally expire in the years 2017 through 2035.

In the past, Charter has experienced "ownership changes" as defined in Section 382 of the Internal Revenue Code of 1986, as amended (the "Code"). In general, an "ownership change" occurs whenever the percentage of the stock of a corporation owned, directly or indirectly, by "5-percent stockholders" (within the meaning of Section 382 of the Code) increases by more than 50 percentage points over the lowest percentage of the stock of such corporation owned, directly or indirectly, by such "5-percent stockholders" at any time over the preceding three years. As a result, Charter is subject to an annual limitation on the use of its loss carryforwards which existed at November 30, 2009 for the first "ownership change," those that existed at May 1, 2013 for the second "ownership change," and those created at May 18, 2016 for the third "ownership change." The limitation on Charter's ability to use its loss carryforwards, in conjunction with the loss carryforward expiration provisions, could reduce Charter's ability to use a portion of its loss carryforwards to offset future taxable income, which could result in Charter being required to make material cash tax payments. Charter's ability to make such income tax payments, if any, will depend at such time on its liquidity or its ability to raise additional capital, and/or on receipt of payments or distributions from Charter Holdco and its subsidiaries.

If Charter were to experience additional ownership changes in the future (as a result of purchases and sales of stock by its "5-percent stockholders," new issuances or redemptions of our stock, certain acquisitions of its stock and issuances, redemptions,



sales or other dispositions or acquisitions of interests in its "5-percent stockholders"), Charter's ability to use its loss carryforwards could become subject to further limitations.

*If Legacy TWC's Separation Transactions (as defined below), including the Distribution (as defined below), do not qualify as tax-free, either as a result of actions taken or not taken by Legacy TWC or as a result of the failure of certain representations by Legacy TWC to be true, Legacy TWC has agreed to indemnify Time Warner Inc. for its taxes resulting from such disqualification, which would be significant.*

As part of Legacy TWC's separation from Time Warner Inc. ("Time Warner") in March 2009 (the "Separation"), Time Warner received a private letter ruling from the IRS and Time Warner and TWC received opinions of tax counsel confirming that the transactions undertaken in connection with the Separation, including the transfer by a subsidiary of Time Warner of its 12.43% non-voting common stock interest in TW NY to TWC in exchange for 80 million newly issued shares of Legacy TWC's Class A common stock, Legacy TWC's payment of a special cash dividend to holders of Legacy TWC's outstanding Class A and Class B common stock, the conversion of each share of Legacy TWC's outstanding Class A and Class B common stock into one share of Legacy TWC common stock, and the pro-rata dividend of all shares of Legacy TWC common stock held by Time Warner to holders of record of Time Warner's common stock (the "Distribution" and, together with all of the transactions, the "Separation Transactions"), should generally qualify as tax-free to Time Warner and its stockholders for U.S. federal income tax purposes. The ruling and opinions rely on certain facts, assumptions, representations and undertakings from Time Warner and Legacy TWC regarding the past and future conduct of the companies' businesses and other matters. If any of these facts, assumptions, representations or undertakings are incorrect or not otherwise satisfied, Time Warner and its stockholders may not be able to rely on the ruling or the opinions and could be subject to significant tax liabilities. Notwithstanding the private letter ruling and opinions, the IRS could determine on audit that the Separation Transactions should be treated as taxable transactions if it determines that any of these facts, assumptions, representations or undertakings are not correct or have been violated, or for other reasons, including as a result of significant changes in the stock ownership of Time Warner or Legacy TWC after the Distribution.

Under the tax sharing agreement among Time Warner and Legacy TWC, Legacy TWC generally would be required to indemnify Time Warner against its taxes resulting from the failure of any of the Separation Transactions to qualify as tax-free as a result of (i) certain actions or failures to act by Legacy TWC or (ii) the failure of certain representations made by Legacy TWC to be true. In addition, even if Legacy TWC bears no contractual responsibility for taxes related to a failure of the Separation Transactions to qualify for their intended tax treatment, Treasury regulation section 1.1502-6 imposes on Legacy TWC several liability for all Time Warner federal income tax obligations relating to the period during which Legacy TWC was a member of the Time Warner federal consolidated tax group, including the date of the Separation Transactions. Similar provisions may apply under foreign, state or local law. Absent Legacy TWC causing the Separation Transactions to not qualify as tax-free, Time Warner has indemnified Legacy TWC against such several liability arising from a failure of the Separation Transactions to qualify for their intended tax treatment.

*If we are unable to retain key employees, our ability to manage our business could be adversely affected.*

Our operational results have depended, and our future results will depend, upon the retention and continued performance of our management team. Our ability to retain and hire new key employees for management positions could be impacted adversely by the competitive environment for management talent in the broadband communications industry. The loss of the services of key members of management and the inability or delay in hiring new key employees could adversely affect our ability to manage our business and our future operational and financial results.

*Our inability to successfully acquire and integrate other businesses, assets, products or technologies could harm our operating results.*

We continuously evaluate and pursue small and large acquisitions and strategic investments in businesses, products or technologies that we believe could complement or expand our business or otherwise offer growth or cost-saving opportunities. From time to time, we may enter into letters of intent with companies with which we are negotiating for potential acquisitions or investments, or as to which we are conducting due diligence. An investment in, or acquisition of, complementary businesses, products or technologies in the future could materially decrease the amount of our available cash or require us to seek additional equity or debt financing. We may not be successful in negotiating the terms of any potential acquisition, conducting thorough due diligence, financing the acquisition or effectively integrating the acquired business, product or technology into our existing business and operations. Our due diligence may fail to identify all of the problems, liabilities or other shortcomings or challenges of an acquired business, product or technology, including issues related to intellectual property, product quality or product architecture, regulatory compliance practices, revenue recognition or other accounting practices, or employee or customer issues.



Additionally, in connection with any acquisitions we complete, including the recently completed Transactions, we may not achieve the growth, synergies or other financial and operating benefits we expected to achieve, and we may incur write-downs, impairment charges or unforeseen liabilities that could negatively affect our operating results or financial position or could otherwise harm our business. Even if we are able to integrate the business operations obtained in such transactions successfully, it is not possible to predict with certainty if or when these cost synergies, growth opportunities and benefits will occur, or the extent to which they actually will be achieved. For example, the benefits from such transactions may be offset by costs incurred in integrating new business operations or in obtaining or attempting to obtain regulatory approvals, or increased operating costs that may be experienced as a result of the transactions. Realization of any benefits and cost synergies could be affected by the factors described in other risk factors and a number of factors beyond our control, as applicable, including, without limitation, general economic conditions, increased operating costs, the response of competitors and vendors and regulatory developments. Further, contemplating or completing an acquisition and integrating an acquired business, product or technology, individually or across multiple opportunities, could divert management and employee time and resources from other matters.

### **Risks Related to Ownership Position of Liberty Broadband Corporation and Advance/Newhouse Partnership**

#### ***Liberty Broadband and A/N have governance rights that give them influence over corporate transactions and other matters.***

Liberty Broadband currently owns a significant amount of Charter Class A common stock and is entitled to certain governance rights with respect to Charter. A/N currently owns Charter Class A common stock and a significant amount of membership interests in our subsidiary Charter Holdings that are convertible into our Charter Class A common stock and is entitled to certain governance rights with respect to Charter. Members of the Charter board of directors include directors who are also officers and directors of Liberty Broadband and directors who are current or former officers and directors of A/N. Dr. John Malone is the Chairman of Liberty Broadband, and Mr. Greg Maffei is the president and chief executive officer of Liberty Broadband. Steven Miron is the Chief Executive Officer of A/N and Michael Newhouse is an officer or director of several of A/N's affiliates. As of December 31, 2016, Liberty Broadband beneficially held approximately 19% of Charter's Class A common stock (including shares owned by Liberty Interactive over which Liberty Broadband holds an irrevocable voting proxy) and A/N beneficially held approximately 13% of Charter's Class A common stock, in each case assuming the conversion of the membership interests held by A/N. Pursuant to the stockholders agreement between Liberty Broadband, A/N and Charter, Liberty Broadband currently has the right to designate up to three directors as nominees for Charter's board of directors and A/N currently has the right to designate up to two directors as nominees for Charter's board of directors with one designated director to be appointed to each of the audit committee, the nominating and corporate governance committee, the compensation and benefits committee and the Finance Committee, in each case provided that each maintains certain specified voting or equity ownership thresholds and each nominee meets certain applicable requirements or qualifications.

In connection with the TWC Transaction, Liberty Broadband and Liberty Interactive entered into a proxy and right of first refusal agreement, pursuant to which Liberty Interactive granted Liberty Broadband an irrevocable proxy to vote all Charter Class A common stock owned beneficially or of record by Liberty Interactive, with certain exceptions. In addition, at the closing of the Bright House Transaction, A/N and Liberty Broadband entered into a proxy agreement pursuant to which A/N granted to Liberty Broadband a 5-year irrevocable proxy (which we refer to as the "A/N proxy") to vote, subject to certain exceptions, that number of shares of New Charter Class A common stock and New Charter Class B common stock, in each case held by A/N (such shares are referred to as the "proxy shares"), that will result in Liberty Broadband having voting power in Charter equal to 25.01% of the outstanding voting power of Charter, provided, that the voting power of the proxy shares is capped at 7.0% of the outstanding voting power of Charter. Therefore, giving effect to the Liberty Interactive proxy and the A/N proxy and the voting cap contained in the stockholders agreement, Liberty Broadband has 25.01% of the outstanding voting power in Charter. The stockholders agreement and Charter's amended and restated certificate of incorporation fixes the size of the board at 13 directors. Liberty Broadband and A/N are required to vote (subject to the applicable voting cap) their respective shares of Charter Class A common stock and Charter Class B common stock for the director nominees nominated by the nominating and corporate governance committee of the board of directors, including the respective designees of Liberty Broadband and A/N, and against any other nominees, except that, with respect to the unaffiliated directors, Liberty Broadband and A/N must instead vote in the same proportion as the voting securities are voted by stockholders other than A/N and Liberty Broadband or any group which includes any of them are voted, if doing so would cause a different outcome with respect to the unaffiliated directors. As a result of their rights under the stockholders agreement and their significant equity and voting stakes in Charter, Liberty Broadband and/or A/N, who may have interests different from those of other stockholders, will be able to exercise substantial influence over certain matters relating to the governance of Charter, including the approval of significant corporate actions, such as mergers and other business combination transactions.

*The stockholders agreement provides A/N and Liberty Broadband with preemptive rights with respect to issuances of Charter equity in connection with certain transactions, and in the event that A/N or Liberty Broadband exercises these rights, holders of Charter Class A common stock may experience further dilution.*

The stockholders agreement provides that A/N and Liberty Broadband will have certain contractual preemptive rights over issuances of Charter equity securities in connection with capital raising transactions, merger and acquisition transactions, and in certain other circumstances. Holders of Charter Class A common stock will not be entitled to similar preemptive rights with respect to such transactions. As a result, if Liberty Broadband and/or A/N elect to exercise their preemptive rights, (i) these parties would not experience the dilution experienced by the other holders of Charter Class A common stock, and (ii) such other holders of Charter Class A common stock may experience further dilution of their interest in Charter upon such exercise.

#### **Risks Related to Regulatory and Legislative Matters**

*Our business is subject to extensive governmental legislation and regulation, which could adversely affect our business.*

Regulation of the cable industry has increased cable operators' operational and administrative expenses and limited their revenues. Cable operators are subject to various laws and regulations including those covering the following:

- the provisioning and marketing of cable equipment and compatibility with new digital technologies;
- customer and employee privacy and data security;
- limited rate regulation of video service;
- copyright royalties for retransmitting broadcast signals;
- when a cable system must carry a particular broadcast station and when it must first obtain retransmission consent to carry a broadcast station;
- the provision of channel capacity to unaffiliated commercial leased access programmers;
- limitations on our ability to enter into exclusive agreements with multiple dwelling unit complexes and control our inside wiring;
- the provision of high-speed Internet service, including net neutrality or open Internet rules;
- the provision of voice communications;
- cable franchise renewals and transfers;
- equal employment opportunity, emergency alert systems, disability access, technical standards, marketing practices, customer service, and consumer protection; and
- approval for mergers and acquisitions often accompanied by the imposition of restrictions and requirements on an applicant's business in order to secure approval of the proposed transaction.

Legislators and regulators at all levels of government frequently consider changing, and sometimes do change, existing statutes, rules, regulations, or interpretations thereof, or prescribe new ones. Any future legislative, judicial, regulatory or administrative actions may increase our costs or impose additional restrictions on our businesses. For example, with respect to our retail broadband Internet access service, the FCC has (1) reclassified the service as a Title II service, (2) applied certain existing Title II provisions and associated regulations to it, (3) forbore from applying a range of other existing Title II provisions and associated regulations, but to varying degrees indicated that this forbearance may be only temporary, and (4) issued new rules expanding disclosure requirements and prohibiting blocking, throttling, paid prioritization, and unreasonable interference with the ability of end users and edge providers to reach each other. The order also subjected broadband providers' Internet traffic exchange rates and practices to potential FCC oversight for the first time and created a mechanism for third parties to file complaints regarding these matters. These FCC actions were upheld on appeal in June 2016, although additional appeals remain pending.

As a result of the reclassification of broadband Internet access service as a Title II communications service, the FCC adopted new privacy and data security rules for common carriers, interconnected VoIP providers, and broadband service providers on October 27, 2016. The new rules replace the prior rules and extend broader privacy protections to broadband customers, as well as voice service customers. The new rules place heightened restrictions on the use of customer information that Internet service providers obtain from the provision of broadband Internet access service (including increased notice, consumer choice, and security), and are more restrictive than other existing privacy and security frameworks. The new rules are subject to additional regulatory approval and legal challenges.

*Changes to existing statutes, rules, regulations, or interpretations thereof, or adoption of new ones, could have an adverse effect on our business.*

There are ongoing efforts to amend or expand the federal, state, and local regulation of some of the services offered over our cable systems, which may compound the regulatory risks we already face. For example, the FCC recently issued a proposal to impose



new regulations on our point to point transport service as well as other commercial data services ("business data services"). As a result, the FCC may price regulate business data services as common carriage services and impose additional restrictions on contracting terms. The FCC also has considered adopting new navigation device rules, pursuant to Section 629 of the Communications Act, which directs the FCC to assure the availability of navigation devices (such as set-top boxes) from third party providers. In 2016, the FCC proposed burdensome new rules that would have required us to make disaggregated "information flows" available to set-top boxes and apps supplied by third parties. That proposal has not been adopted, but various parties may continue to advocate alternative regulatory approaches to reduce consumer dependency on traditional operator provided set-top boxes. The FCC also is considering the appropriate regulatory framework for VoIP service, including whether that service should be regulated under Title II.

Congress is considering legislation that could increase costs on the company, including (1) the adoption of new data security and cybersecurity legislation that could result in additional network and information security requirements for our business, (2) a change in corporate tax laws that could eliminate some of our current deductions, and (3) broadband subsidies to rural areas that could result in subsidized overbuilding of our more rural facilities.

If any of these pending laws and regulations are enacted, they could affect our operations and require significant expenditures. We cannot predict future developments in these areas, and we are already subject to Charter-specific conditions regarding certain Internet practices as a result of the FCC's approval of the Transactions, but any changes to the regulatory framework for our Internet or VoIP services could have a negative impact on our business and results of operations.

It remains uncertain what rule changes, if any, will ultimately be adopted by Congress and the FCC and what operating or financial impact any such rules might have on us, including on our programming agreements, customer privacy and the user experience. In addition, the FCC's Enforcement Bureau has been actively investigating certain industry practices of various companies and imposing forfeitures for alleged regulatory violations.

***Our cable system franchises are subject to non-renewal or termination. The failure to renew a franchise in one or more key markets could adversely affect our business.***

Our cable systems generally operate pursuant to franchises, permits, and similar authorizations issued by a state or local governmental authority controlling the public rights-of-way. Many franchises establish comprehensive facilities and service requirements, as well as specific customer service standards and monetary penalties for non-compliance. In many cases, franchises are terminable if the franchisee fails to comply with significant provisions set forth in the franchise agreement governing system operations. Franchises are generally granted for fixed terms and must be periodically renewed. Franchising authorities may resist granting a renewal if either past performance or the prospective operating proposal is considered inadequate. Franchise authorities often demand concessions or other commitments as a condition to renewal. In some instances, local franchises have not been renewed at expiration, and we have operated and are operating under either temporary operating agreements or without a franchise while negotiating renewal terms with the local franchising authorities.

We cannot assure you that we will be able to comply with all significant provisions of our franchise agreements and certain of our franchisers have from time to time alleged that we have not complied with these agreements. Additionally, although historically we have renewed our franchises without incurring significant costs, we cannot assure you that we will be able to renew, or to renew as favorably, our franchises in the future. A termination of or a sustained failure to renew a franchise in one or more key markets could adversely affect our business in the affected geographic area.

***Our cable system franchises are non-exclusive. Accordingly, local and state franchising authorities can grant additional franchises and create additional competition for our products, resulting in overbuilds, which could adversely affect results of operations.***

Our cable system franchises are non-exclusive. Consequently, local and state franchising authorities can grant additional franchises to competitors in the same geographic area or operate their own cable systems. In some cases, local government entities and municipal utilities may legally compete with us on more favorable terms. Potential competitors (like Google) have recently pursued and obtained local franchises that are more favorable than the incumbent operator's franchise.

The FCC has adopted rules that streamline entry for new competitors (particularly those affiliated with telephone companies) and reduce franchising burdens for these new entrants. At the same time, a substantial number of states have adopted new franchising laws, principally designed to streamline entry for new competitors, and often provide advantages for these new entrants that are not immediately available to existing operators.



Broadband delivery of video content is not necessarily subject to the same franchising obligations applicable to our traditional cable systems. The FCC administers a program that collects Universal Service Fund contributions from telecommunications service providers and uses them to subsidize the provision of telecommunications services in high-cost areas and to low-income consumers and the provision of Internet and telecommunications services to schools, libraries and certain health care providers. A variety of regulatory changes may lead the FCC to expand the collection of Universal Service Fund contributions to encompass Internet service providers. The FCC already has begun to redirect the expenditure of some Universal Service Fund subsidies to broadband deployment in ways that could assist competitors.

*Local franchise authorities have the ability to impose additional regulatory constraints on our business, which could further increase our expenses.*

In addition to the franchise agreement, cable authorities in some jurisdictions have adopted cable regulatory ordinances that further regulate the operation of cable systems. This additional regulation increases the cost of operating our business. Local franchising authorities may impose new and more restrictive requirements. Local franchising authorities who are certified to regulate rates in the communities where they operate generally have the power to reduce rates and order refunds on the rates charged for basic service and equipment.

*Tax legislation and administrative initiatives or challenges to our tax positions could adversely affect our results of operations and financial condition.*

We operate cable systems in locations throughout the United States and, as a result, we are subject to the tax laws and regulations of federal, state and local governments. From time to time, various legislative and/or administrative initiatives may be proposed that could adversely affect our tax positions. There can be no assurance that our effective tax rate or tax payments will not be adversely affected by these initiatives. Certain states and localities have imposed or are considering imposing new or additional taxes or fees on our services or changing the methodologies or base on which certain fees and taxes are computed. Potential changes include additional taxes or fees on our services which could impact our customers, combined reporting and other changes to general business taxes, central/unit-level assessment of property taxes and other matters that could increase our income, franchise, sales, use and/or property tax liabilities. In addition, federal, state and local tax laws and regulations are extremely complex and subject to varying interpretations. There can be no assurance that our tax positions will not be challenged by relevant tax authorities or that we would be successful in any such challenge.

*Further regulation of the cable industry could impair our ability to raise rates to cover our increasing costs, resulting in increased losses.*

Currently, rate regulation of cable systems is strictly limited to the basic service tier and associated equipment and installation activities, and the FCC recently revised its rules, in response to changed market conditions, to make it more difficult for local franchising authorities to assert rate regulation authority. However, the FCC and Congress continue to be concerned that cable rate increases are exceeding inflation. It is possible that either the FCC or Congress will further restrict the ability of cable system operators to implement rate increases for our video services or even for our Internet and voice services. Should this occur, it would impede our ability to raise our rates. If we are unable to raise our rates in response to increasing costs, our financial results would be adversely impacted.

There has been legislative and regulatory interest in requiring companies that own multiple cable networks to make each of them available on a standalone, rather than a bundled basis to cable operators, and in requiring cable operators to offer historically bundled programming services on an à la carte basis to consumers. While any new regulation or legislation designed to enable cable operators to purchase programming on a standalone basis could be beneficial to us, any regulation or legislation that limits how we sell programming could adversely affect our business.

*Changes in channel carriage regulations could impose significant additional costs on us.*

Cable operators also face significant regulation of their video channel carriage. We can be required to devote substantial capacity to the carriage of programming that we might not carry voluntarily, including certain local broadcast signals; local public, educational and governmental access ("PEG") programming; and unaffiliated, commercial leased access programming (required channel capacity for use by persons unaffiliated with the cable operator who desire to distribute programming over a cable system). The FCC adopted revised commercial leased access rules which would dramatically reduce the rate we can charge for leasing this capacity and dramatically increase our administrative burdens, but these remain stayed while under appeal. Legislation has been introduced in Congress in the past that, if adopted, could impact our carriage of broadcast signals by eliminating the cable industry's compulsory copyright license. The FCC also continues to consider changes to the rules affecting the relationship between programmers (including broadcasters) and multichannel video distributors, including potential loosening of media ownership rules.



Future regulatory changes could disrupt existing programming commitments, interfere with our preferred use of limited channel capacity, increase our programming costs, and limit our ability to offer services that would maximize our revenue potential. It is possible that other legal restraints will be adopted limiting our discretion over programming decisions.

*Our voice service is subject to regulatory burdens which may increase, causing us to incur additional costs.*

We offer voice communications services over our broadband network using VoIP services. The FCC has ruled that competitive telephone companies that support VoIP services, such as those we offer our customers, are entitled to interconnect with incumbent providers of traditional telecommunications services, which ensures that our VoIP services can compete in the market. The scope of these interconnection rights are being reviewed in a current FCC proceeding, which may affect our ability to compete in the provision of voice services or result in additional costs. The FCC has also declared that certain VoIP services are not subject to traditional state public utility regulation. The full extent of the FCC preemption of state and local regulation of VoIP services is not yet clear, and at least one state (Minnesota) has asserted jurisdiction over the company's VoIP services. We have filed a legal challenge to that jurisdictional assertion, which is now pending before a federal district court in Minnesota. Telecommunications companies generally are subject to other significant regulation which could also be extended to VoIP providers. The FCC has already extended certain traditional telecommunications carrier requirements to many VoIP providers such as us. If additional telecommunications regulations are applied to our VoIP service, it could cause us to incur additional costs.

**Item 1B. Unresolved Staff Comments.**

None.

**Item 2. Properties.**

Our principal physical assets consist of cable distribution plant and equipment, including signal receiving, encoding and decoding devices, headend reception facilities, distribution systems, and customer premise equipment for each of our cable systems.

Our cable plant and related equipment are generally attached to utility poles under pole rental agreements with local public utilities and telephone companies, and in certain locations are buried in underground ducts or trenches. We own or lease real property for signal reception sites, and own our service vehicles.

Our subsidiaries generally lease space for business offices. Our headend and tower locations are located on owned or leased parcels of land, and we generally own the towers on which our equipment is located. We lease space for our corporate headquarters in Stamford, Connecticut.

The physical components of our cable systems require maintenance as well as periodic upgrades to support the new services and products we introduce. See "Item 1. Business – Our Network Technology." We believe that our properties are generally in good operating condition and are suitable for our business operations.

**Item 3. Legal Proceedings.**

The legal proceedings information set forth in Note 20 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data" in this Annual Report on Form 10-K is incorporated herein by reference.

**Item 4. Mine Safety Disclosures.**

Not applicable.

## PART II

**Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.****(A) Market Information**

Charter's Class A common stock is listed on the NASDAQ Global Select Market under the symbol "CHTR."

The following table sets forth, for the periods indicated, the range of high and low last reported sale price per share of Charter's Class A common stock on the NASDAQ Global Select Market.

**Class A Common Stock**

	<b>High</b>	<b>Low</b>
<b>2015</b>		
First quarter	\$ 193.46	\$ 150.60
Second quarter	\$ 193.19	\$ 167.84
Third quarter	\$ 194.50	\$ 167.36
Fourth quarter	\$ 193.33	\$ 174.81
<b>2016</b>		
First quarter	\$ 204.10	\$ 159.53
Second quarter	\$ 233.11	\$ 197.91
Third quarter	\$ 277.56	\$ 231.77
Fourth quarter	\$ 292.19	\$ 244.10

**(B) Holders**

As of December 31, 2016, there were approximately 15,035 holders of record of Charter's Class A common stock and one holder of Charter's Class B common stock.

**(C) Dividends**

Charter has not paid stock or cash dividends on any of its common stock.

Charter would be dependent on distributions from its subsidiaries if Charter were to make any dividends. Covenants in the indentures and Charter Operating credit facilities governing the debt obligations of our subsidiaries restrict their ability to make distributions to us, and accordingly, limit our ability to declare or pay cash dividends. Future cash dividends, if any, will be at the discretion of Charter's board of directors and will depend upon, among other things, our future operations and earnings, capital requirements, general financial condition, contractual restrictions and such other factors as Charter's board of directors may deem relevant.

**(D) Securities Authorized for Issuance Under Equity Compensation Plans**

The following information is provided as of December 31, 2016 with respect to equity compensation plans:

Plan Category	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted Average Exercise Price of Outstanding Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans
Equity compensation plans approved by security holders	12,905,216 (1)	\$ 184.22	3,155,002 (1)
Equity compensation plans not approved by security holders	—	\$ —	—
<b>TOTAL</b>	<b>12,905,216 (1)</b>		<b>3,155,002 (1)</b>

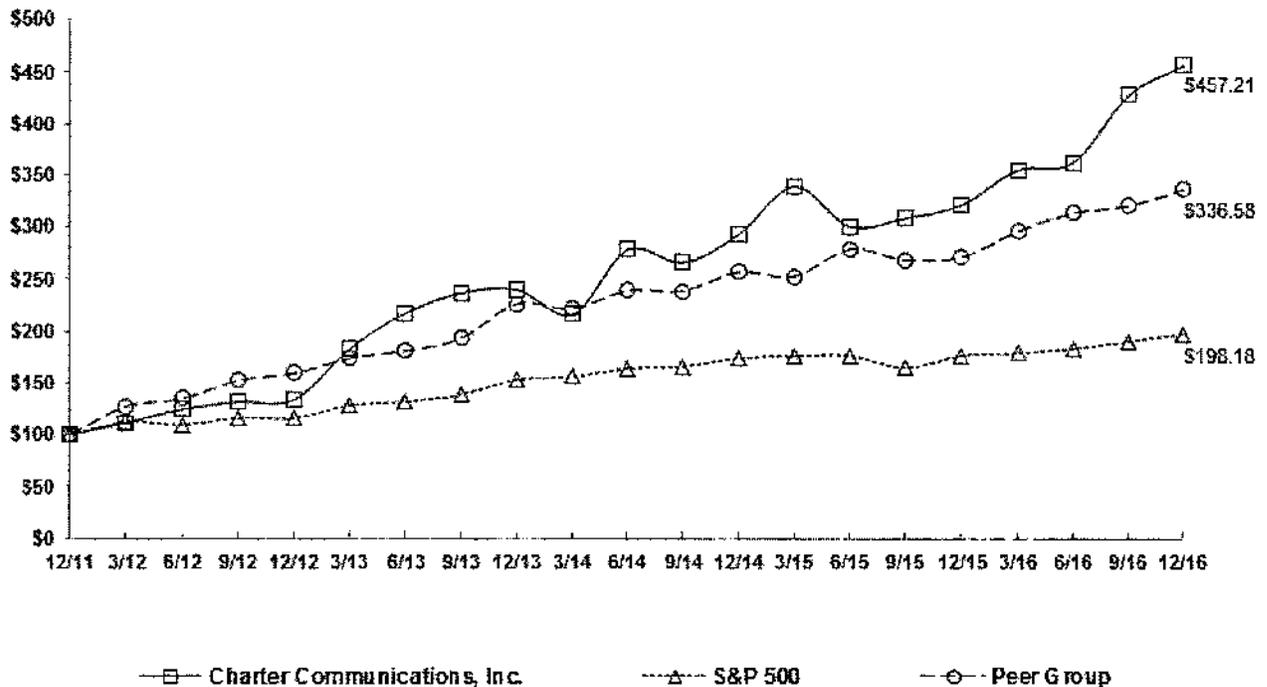
(1) This total does not include 9,811 shares issued pursuant to restricted stock grants made under our 2009 Stock Incentive Plan, which are subject to vesting based on continued employment and market conditions.

For information regarding securities issued under our equity compensation plans, see Note 16 to our accompanying consolidated financial statements contained in "Item 8. Financial Statements and Supplementary Data."

**(E) Performance Graph**

The graph below shows the cumulative total return on Charter’s Class A common stock for the period from December 31, 2011 through December 31, 2016, in comparison to the cumulative total return on Standard & Poor’s 500 Index and a peer group consisting of the national cable operators that are most comparable to us in terms of size and nature of operations. The Company’s peer group consists of Cablevision Systems Corporation (“Cablevision”), Comcast, and Legacy TWC (through May 18, 2016). The results shown assume that \$100 was invested on December 31, 2011 and that all dividends were reinvested. These indices are included for comparative purposes only and do not reflect whether it is management’s opinion that such indices are an appropriate measure of the relative performance of the stock involved, nor are they intended to forecast or be indicative of future performance of Charter’s Class A common stock.

**COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN\***  
Among Charter Communications, Inc., the S&P 500 Index,  
and a Peer Group



\*\$100 invested on 12/31/11 in stock or index, including reinvestment of dividends. Fiscal year ending December 31.  
Copyright© 2017 Standard & Poor’s, a division of S&P Global. All rights reserved.

**(F) Recent Sales of Unregistered Securities**

During 2016, there were no unregistered sales of securities of the registrant other than those previously reported on a Quarterly Report on Form 10-Q or Current Report on Form 8-K.

**(G) Purchases of Equity Securities by the Issuer**

The following table presents Charter's purchases of equity securities completed during the fourth quarter of 2016 (dollars in millions, except per share data).

Period	Total Number of Shares Purchased <sup>(1)</sup>	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>(2)</sup>	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs <sup>(2)</sup>
October 1 - 31, 2016	1,845,823	\$ 262.58	1,784,834	\$750
November 1 - 30, 2016	1,493,418	\$ 262.14	1,442,144	\$370
December 1 - 31, 2016	865,145	\$ 280.59	793,645	\$1,654

<sup>(1)</sup> Includes 60,989, 51,274 and 71,500 shares withheld from employees for the payment of taxes and exercise costs upon the exercise of stock options or vesting of other equity awards for the months of October, November and December 2016, respectively.

<sup>(2)</sup> In 2016, Charter purchased approximately 5.1 million shares of its Class A common stock for approximately \$1.3 billion pursuant to authorizations by Charter's board of directors of \$3 billion (\$750 million authorized on July 26, 2016, \$750 million on October 25, 2016 and \$1.5 billion on December 2, 2016). Accordingly, as of December 31, 2016 and provided Charter's leverage ratio remains at 4 to 4.5 times and Charter Operating's leverage remains below 3.5 times, management has authority to cause Charter to purchase an additional \$1.7 billion of Charter's Class A common stock without taking into account shares or units that may be purchased from A/N. Effective November 1, 2016, Charter's board of directors granted authority for a new \$750 million of Class A common stock buybacks under the rolling six-month authority without taking into account any Class A common stock purchased prior to November 1. As a result, a portion of the \$1.7 billion of authority is under the authority of management to approve up to \$750 million for Class A common stock buybacks in any six-month period. In December 2016, Charter and A/N entered into a letter agreement ("Letter Agreement") that requires A/N to sell to Charter or to Charter Holdings, on a monthly basis, a number of shares of Charter Class A common stock or Charter Holdings common units that represents a pro rata participation by A/N and its affiliates in any repurchases of shares of Charter Class A common stock from persons other than A/N effected by Charter during the immediately preceding calendar month, at a purchase price equal to the average price paid by Charter for the shares repurchased from persons other than A/N during such immediately preceding calendar month. A/N and Charter both have the right to terminate or suspend the pro rata repurchase arrangement on a prospective basis once Charter or Charter Holdings have repurchased shares of Class A common stock or Charter Holdings common units from A/N and its affiliates for an aggregate purchase price of \$537 million. In December 2016, pursuant to this Letter Agreement, Charter purchased Charter Holdings common units from A/N at a price of \$289.83 per unit, or \$218 million. Charter has established a Rule 10b5-1 plan in connection with its share repurchase activity and cannot predict when or if it will repurchase more shares of Charter Class A common stock pursuant to the current plan as such plan includes a price grid including a limit where Charter would not buy shares under the Rule 10b5-1 plan currently in place. Charter may also buy shares of Charter Class A common stock, from time to time, pursuant to private transactions outside of its Rule 10b5-1 plan and any such repurchases would also trigger the repurchases from A/N pursuant to and to the extent provided in the Letter Agreement.

**Item 6. Selected Financial Data.**

The following table presents selected consolidated financial data for the periods indicated (dollars in millions, except per share data):

	Years Ended December 31,				
	2016	2015	2014	2013	2012
<b>Statement of Operations Data:</b>					
Revenues	\$ 29,003	\$ 9,754	\$ 9,108	\$ 8,155	\$ 7,504
Income from operations	\$ 3,355	\$ 1,114	\$ 971	\$ 909	\$ 915
Interest expense, net	\$ 2,499	\$ 1,306	\$ 911	\$ 846	\$ 907
Income (loss) before income taxes	\$ 820	\$ (331)	\$ 53	\$ (49)	\$ (47)
Net income (loss) attributable to Charter shareholders	\$ 3,522	\$ (271)	\$ (183)	\$ (169)	\$ (304)
Income (loss) per common share, basic	\$ 17.05	\$ (2.68)	\$ (1.88)	\$ (1.83)	\$ (3.38)
Income (loss) per common share, diluted	\$ 15.94	\$ (2.68)	\$ (1.88)	\$ (1.83)	\$ (3.38)
Weighted average shares outstanding, basic (a)	206,539,100	101,152,647	97,991,915	92,169,292	90,110,754
Weighted average shares outstanding, diluted (a)	234,791,439	101,152,647	97,991,915	92,169,292	90,110,754
<b>Balance Sheet Data (end of period):</b>					
Investment in cable properties	\$ 144,396	\$ 16,375	\$ 16,652	\$ 16,556	\$ 14,870
Total assets (b)	\$ 149,067	\$ 39,316	\$ 24,388	\$ 17,129	\$ 15,440
Total debt (b)	\$ 61,747	\$ 35,723	\$ 20,887	\$ 14,031	\$ 12,670
Total shareholders' equity (deficit)	\$ 50,366	\$ (46)	\$ 146	\$ 151	\$ 149
<b>Other Financial Data:</b>					
Ratio of earnings to fixed charges (c)	1.33	N/A	1.06	N/A	N/A
Deficiency of earnings to cover fixed charges (c)	N/A	\$ 331	N/A	\$ 49	\$ 47

- (a) Weighted average number of shares outstanding for all periods presented has been recast to reflect the application of the Parent Merger Exchange Ratio. See Note 2 to our accompanying consolidated financial statements contained in "Item 8. Financial Statements and Supplementary Data."
- (b) Years ended December 31, 2014, 2013 and 2012 have been restated to reflect the adoption of certain new accounting standards in 2015, including Accounting Standards Update ("ASU") 2015-03, *Simplifying the Presentation of Debt Issuance Costs*, and ASU 2015-17, *Balance Sheet Classification of Deferred Taxes*.
- (c) Earnings include income (loss) before non-controlling interest and income taxes plus fixed charges. Fixed charges consist of interest expense and an estimated interest component of rent expense.

Comparability of the above information from year to year is affected by acquisitions and dispositions completed by us, including the Transactions. See "Part I. Item 1. Business" for a discussion regarding the Transactions.

**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

Reference is made to "Part I. Item 1A. Risk Factors" and "Cautionary Statement Regarding Forward-Looking Statements," which describe important factors that could cause actual results to differ from expectations and non-historical information contained herein. In addition, the following discussion should be read in conjunction with the audited consolidated financial statements and accompanying notes thereto of Charter Communications, Inc. and subsidiaries included in "Part II. Item 8. Financial Statements and Supplementary Data."

**Overview**

We are the second largest cable operator in the United States and a leading broadband communications services company providing video, Internet and voice services to approximately 26.2 million residential and business customers at December 31, 2016. In addition, we sell video and online advertising inventory to local, regional and national advertising customers and fiber-delivered

communications and managed IT solutions to larger enterprise customers. We also own and operate regional sports networks and local sports, news and community channels and sell security and home management services to the residential marketplace. See

“Part I. Item 1. Business — Products and Services” for further description of these services, including customer statistics for different services.

Since 2012, Legacy Charter has actively invested in its network and operations and improved the quality and value of the products and packages that Legacy Charter offered. Through the roll-out of Spectrum pricing and packaging we have simplified our offers and improved our packaging of products, delivering more value to new and existing customers. Further, through the transition of our Legacy Charter markets to our all-digital platform, we increased our offerings to more than 200 HD channels in most of the Legacy Charter markets and offered Internet speeds of at least 60 or 100 Mbps, among other benefits. We believe that this product set combined with improved customer service, as we insource our workforce in our call centers and in our field operations, has led to lower customer churn and longer customer lifetimes.

As a result of the Transactions, 2016 revenues increased by over \$18.6 billion year over year. We also saw an increase in expenses related to our increased scale. In September 2016, we began launching SPP to Legacy TWC markets and we expect that by mid 2017, we will offer SPP in all Legacy TWC and Legacy Bright House markets. In 2017, we intend to begin converting the remaining Legacy TWC and Legacy Bright House analog markets to an all-digital platform. Our corporate organization, as well as our marketing, sales and product development departments, are now centralized. Field operations are managed through eleven regional areas, each designed to represent a combination of designated marketing areas and managed with largely the same set of field employees that were with the three legacy companies prior to completion of the Transactions. Over a multi-year period, Legacy TWC and Legacy Bright House customer care centers will migrate to Legacy Charter's model of using segmented, virtualized, U.S.-based in-house call centers. We will focus on deploying superior products and service with minimal service disruptions as we integrate our information technology and network operations. We expect customer and financial results to trend similar to Legacy Charter following the implementation of the Legacy Charter operating strategies across the Legacy TWC and Legacy Bright House markets. As a result of implementing our operating strategy at Legacy TWC and Legacy Bright House, we cannot be certain that we will be able to grow revenues or maintain our margins at recent historical rates.

The Company realized revenue, Adjusted EBITDA and income from operations during the periods presented as follows (in millions; all percentages are calculated using whole numbers. Minor differences may exist due to rounding).

	Years ended December 31,			Growth	
	2016	2015	2014	2016 over 2015	2015 over 2014
<b>Actual</b>					
Revenues	\$ 29,003	\$ 9,754	\$ 9,108	197.3%	7.1%
Adjusted EBITDA	\$ 10,592	\$ 3,406	\$ 3,190	211.0%	6.8%
Income from operations	\$ 3,355	\$ 1,114	\$ 971	201.3%	14.8%
<b>Pro Forma</b>					
Revenues	\$ 40,023	\$ 37,394		7.0%	
Adjusted EBITDA	\$ 14,464	\$ 13,004		11.2%	
Income from operations	\$ 4,801	\$ 3,396		41.4%	

Adjusted EBITDA is defined as consolidated net income (loss) plus net interest expense, income taxes, depreciation and amortization, stock compensation expense, loss on extinguishment of debt, (gain) loss on financial instruments, net, other (income) expense, net and other operating (income) expenses, such as merger and restructuring costs, other pension benefits, special charges and gain (loss) on sale or retirement of assets. See “—Use of Adjusted EBITDA and Free Cash Flow” for further information on Adjusted EBITDA and free cash flow. Growth in total revenue, Adjusted EBITDA and income from operations was primarily due to the Transactions.

On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, total revenue growth was primarily due to growth in our Internet and commercial businesses. On a pro forma basis, Adjusted EBITDA growth was primarily due to an increase in residential and commercial revenues offset by increases in programming costs and other operating costs. In addition to the factors discussed above, income from operations on a pro forma basis was affected by increases in depreciation and amortization, merger and restructuring costs and stock compensation expense.

Approximately 90%, 91% and 90% of our revenues for years ended December 31, 2016, 2015 and 2014, respectively, are attributable to monthly subscription fees charged to customers for our video, Internet, voice and commercial services provided by our cable systems. Generally, these customer subscriptions may be discontinued by the customer at any time subject to a fee for



certain commercial customers. The remaining 10%, 9% and 10% of revenue for fiscal years 2016, 2015 and 2014, respectively, is derived primarily from advertising revenues, franchise and other regulatory fee revenues (which are collected by us but then paid to local authorities), pay-per-view and VOD programming, installation, processing fees or reconnection fees charged to customers to commence or reinstate service, and commissions related to the sale of merchandise by home shopping services.

We incurred the following transition costs in connection with the Transactions (in millions).

	Years ended December 31,		
	2016	2015	2014
Operating expenses	\$ 156	\$ 72	\$ 14
Other operating expenses	\$ 970	\$ 70	\$ 38
Interest expense	\$ 390	\$ 521	\$ 75
Capital expenditures	\$ 460	\$ 115	\$ 27

Amounts included in transition operating expenses and transition capital expenditures represent incremental costs incurred to integrate the Legacy TWC and Legacy Bright House operations and to bring the three companies' systems and processes into a uniform operating structure. Costs are incremental and would not be incurred absent the integration. Other operating expenses associated with the Transactions represent merger and restructuring costs and include advisory, legal and accounting fees, employee retention costs, employee termination costs and other exit costs. Interest expense associated with the Transactions represents interest incurred on the CCO Safari II, CCO Safari III and CCOH Safari notes issued in advance of the closing of the Transactions, the proceeds of which were held in escrow to finance the Transactions.

We have a history of net losses. Our net losses were principally attributable to insufficient revenue to cover the combination of operating expenses, interest expenses that we incur on our debt, depreciation expenses resulting from the capital investments we have made, and continue to make, in our cable properties, amortization expenses related to our customer relationship intangibles and higher non-cash income tax expense. We will incur significant increases in interest expense and depreciation and amortization as a result of the Transactions and will incur restructuring and transition costs for at least one to two years, and as a result, absent non-recurring impacts such as the reversal of the income tax valuation allowance in the second quarter of 2016, we may incur net losses in the future.

### Critical Accounting Policies and Estimates

Certain of our accounting policies require our management to make difficult, subjective and/or complex judgments. Management has discussed these policies with the Audit Committee of Charter's board of directors, and the Audit Committee has reviewed the following disclosure. We consider the following policies to be the most critical in understanding the estimates, assumptions and judgments that are involved in preparing our financial statements, and the uncertainties that could affect our results of operations, financial condition and cash flows:

- Property, plant and equipment
  - Capitalization of labor and overhead costs
  - Valuation and impairment of property, plant and equipment
  - Useful lives of property, plant and equipment
- Intangible assets
  - Valuation and impairment of franchises
  - Valuation and impairment of goodwill
  - Valuation and impairment and amortization of customer relationships
- Income taxes
- Litigation
- Programming agreements
- Pension plans

In addition, there are other items within our financial statements that require estimates or judgment that are not deemed critical, such as the allowance for doubtful accounts and valuations of our financial instruments, but changes in estimates or judgment in these other items could also have a material impact on our financial statements.



### ***Property, plant and equipment***

The cable industry is capital intensive, and a large portion of our resources are spent on capital activities associated with extending, rebuilding, and upgrading our cable network. As of December 31, 2016 and 2015, the net carrying amount of our property, plant and equipment (consisting primarily of cable distribution systems) was approximately \$33.0 billion (representing 22% of total assets) and \$8.3 billion (representing 49% of total assets excluding restricted cash and cash equivalents), respectively. Total capital expenditures for the years ended December 31, 2016, 2015 and 2014 were approximately \$5.3 billion, \$1.8 billion and \$2.2 billion, respectively.

***Capitalization of labor and overhead costs.*** Costs associated with network construction, initial placement of the customer drop to the dwelling and the initial placement of outlets within a dwelling along with the costs associated with the initial deployment of customer premise equipment necessary to provide video, Internet or voices services, are capitalized. Costs capitalized include materials, direct labor, and certain indirect costs. These indirect costs are associated with the activities of personnel who assist in installation activities, and consist of compensation and overhead costs associated with these support functions. While our capitalization is based on specific activities, once capitalized, we track these costs on a composite basis by fixed asset category at the cable system level, and not on a specific asset basis. For assets that are sold or retired, we remove the estimated applicable cost and accumulated depreciation. The costs of disconnecting service and removing customer premise equipment from a dwelling and the costs to reconnect a customer drop or to redeploy previously installed customer premise equipment are charged to operating expense as incurred. Costs for repairs and maintenance are charged to operating expense as incurred, while plant and equipment replacement, including replacement of certain components, betterments, and replacement of cable drops and outlets, are capitalized.

We make judgments regarding the installation and construction activities to be capitalized. We capitalize direct labor and overhead using standards developed from actual costs and applicable operational data. We calculate standards annually (or more frequently if circumstances dictate) for items such as the labor rates, overhead rates, and the actual amount of time required to perform a capitalizable activity. For example, the standard amounts of time required to perform capitalizable activities are based on studies of the time required to perform such activities. Overhead rates are established based on an analysis of the nature of costs incurred in support of capitalizable activities, and a determination of the portion of costs that is directly attributable to capitalizable activities. The impact of changes that resulted from these studies were not material in the periods presented.

Labor costs directly associated with capital projects are capitalized. Capitalizable activities performed in connection with installations include such activities as:

- dispatching a "truck roll" to the customer's dwelling or business for service connection or placement of new equipment;
- verification of serviceability to the customer's dwelling or business (i.e., determining whether the customer's dwelling is capable of receiving service by our cable network and/or receiving advanced or Internet services);
- customer premise activities performed by in-house field technicians and third-party contractors in connection with customer installations, installation of equipment in connection with the installation of video, Internet or voice services, and equipment replacement and betterment; and
- verifying the integrity of the customer's network connection by initiating test signals downstream from the headend to the customer's digital set-top box, as well as testing signal levels at the pole or pedestal.

Judgment is required to determine the extent to which overhead costs incurred result from specific capital activities, and therefore should be capitalized. The primary costs that are included in the determination of the overhead rate are (i) employee benefits and payroll taxes associated with capitalized direct labor, (ii) direct variable costs associated with capitalizable activities, (iii) the cost of support personnel, such as care personnel and dispatchers, who assist with capitalizable installation activities, and (iv) indirect costs directly attributable to capitalizable activities.

While we believe our existing capitalization policies are appropriate, a significant change in the nature or extent of our system activities could affect management's judgment about the extent to which we should capitalize direct labor or overhead in the future. We monitor the appropriateness of our capitalization policies, and perform updates to our internal studies on an ongoing basis to determine whether facts or circumstances warrant a change to our capitalization policies. We capitalized direct labor and overhead of \$991 million, \$420 million and \$427 million, respectively, for the years ended December 31, 2016, 2015 and 2014.

***Valuation and impairment of property, plant and equipment.*** We evaluate the recoverability of our property, plant and equipment upon the occurrence of events or changes in circumstances indicating that the carrying amount of an asset may not be recoverable. Such events or changes in circumstances could include such factors as the impairment of our indefinite life franchises, changes in technological advances, fluctuations in the fair value of such assets, adverse changes in relationships with local franchise authorities, adverse changes in market conditions, or a deterioration of current or expected future operating results. A long-lived



asset is deemed impaired when the carrying amount of the asset exceeds the projected undiscounted future cash flows associated with the asset. No impairments of long-lived assets to be held and used were recorded in the years ended December 31, 2016, 2015 and 2014.

We utilize the cost approach as the primary method used to establish fair value for our property, plant and equipment in connection with business combinations. The cost approach considers the amount required to replace an asset by constructing or purchasing a new asset with similar utility, then adjusts the value in consideration of physical depreciation and functional and economic obsolescence as of the appraisal date. The cost approach relies on management's assumptions regarding current material and labor costs required to rebuild and repurchase significant components of our property, plant and equipment along with assumptions regarding the age and estimated useful lives of our property, plant and equipment.

**Useful lives of property, plant and equipment.** We evaluate the appropriateness of estimated useful lives assigned to our property, plant and equipment, based on annual analysis of such useful lives, and revise such lives to the extent warranted by changing facts and circumstances. Any changes in estimated useful lives as a result of this analysis are reflected prospectively beginning in the period in which the study is completed. Our analysis of useful lives in 2016 did not indicate a change in useful lives. The effect of a one-year decrease in the weighted average remaining useful life of our property, plant and equipment as of December 31, 2016 would be an increase in annual depreciation expense of approximately \$1.7 billion. The effect of a one-year increase in the weighted average remaining useful life of our property, plant and equipment as of December 31, 2016 would be a decrease in annual depreciation expense of approximately \$863 million.

Depreciation expense related to property, plant and equipment totaled \$5.0 billion, \$1.9 billion and \$1.8 billion for the years ended December 31, 2016, 2015 and 2014, respectively, representing approximately 19%, 21% and 22% of costs and expenses, respectively. Depreciation is recorded using the straight-line composite method over management's estimate of the useful lives of the related assets as listed below:

Cable distribution systems	7-20 years
Customer premise equipment and installations	3-8 years
Vehicles and equipment	3-6 years
Buildings and improvements	15-40 years
Furniture, fixtures and equipment	6-10 years

#### **Intangible assets**

**Valuation and impairment of franchises.** The net carrying value of franchises as of December 31, 2016 and 2015 was approximately \$67.3 billion (representing 45% of total assets) and \$6.0 billion (representing 35% of total assets excluding restricted cash and cash equivalents), respectively. For more information and a complete discussion of how we value and test franchise assets for impairment, see Note 6 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data."

We perform an impairment assessment of franchise assets annually or more frequently as warranted by events or changes in circumstances. We performed a qualitative assessment in 2016. Our assessment included consideration of the fair value appraisals of Legacy Charter and the newly-acquired operations performed as of the date of acquisition for tax and acquisition accounting purposes, respectively, along with a multitude of factors that affect the fair value of our franchise assets. Examples of such factors include environmental and competitive changes within our operating footprint, actual and projected operating performance, the consistency of our operating margins, equity and debt market trends, including changes in our market capitalization, and changes in our regulatory and political landscape, among other factors. Based on our assessment, we concluded that it was more likely than not that the estimated fair values of our franchise assets equals or exceeds their carrying values and that a quantitative impairment test is not required.

The appraisals indicated that the fair value of our franchise assets exceeded carrying value by approximately 25% in the aggregate, with the excess entirely attributable to the franchise assets of Legacy Charter to which acquisition accounting was not applied. At our unit of accounting level for franchise asset impairment testing, the amount by which fair value exceeds carrying value varies based on the extent to which the unit of accounting was comprised of newly-acquired operations. For units of accounting comprised entirely or substantially of newly-acquired operations, we believe the carrying value approximates the fair value given that there has been no significant adverse changes in factors impacting our fair value estimates since the Transaction date. For units of accounting comprised of at least 25% Legacy Charter operations, the fair value exceeded carrying value by a range of 36% to 260%.



**Valuation and impairment of goodwill.** The net carrying value of goodwill as of December 31, 2016 and 2015 was approximately \$29.5 billion (representing 20% of total assets) and \$1.2 billion (representing 7% of total assets excluding restricted cash and cash equivalents), respectively. For more information and a complete discussion on how we test goodwill for impairment, see Note 6 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data." We perform our impairment assessment of goodwill annually as of November 30<sup>th</sup>. As with our franchise impairment testing, we elected to perform a qualitative assessment of goodwill in 2016 which included the fair value appraisals and other factors described above. Based on the appraisals, we determined that the fair value of our goodwill exceeded carrying value by approximately 28% as of the closing of the Transactions. Given the limited amount of time between the closing of the Transactions and the completion of the assessment and absence of significant adverse changes in factors impacting our fair value estimates, we concluded that it is more likely than not that our goodwill is not impaired.

**Valuation, impairment and amortization of customer relationships.** The net carrying value of customer relationships as of December 31, 2016 and 2015 was approximately \$14.6 billion (representing 10% of total assets) and \$856 million (representing 5% of total assets excluding restricted cash and cash equivalents), respectively. Amortization expense related to customer relationships for the years ended December 31, 2016, 2015 and 2014 was approximately \$1.9 billion, \$249 million and \$282 million, respectively. No impairment of customer relationships was recorded in the years ended December 31, 2016, 2015 and 2014. For more information and a complete discussion on our valuation methodology and amortization method, see Note 6 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data."

#### **Income taxes**

As of December 31, 2016, Charter had approximately \$11.2 billion of federal tax net operating loss carryforwards resulting in a gross deferred tax asset of approximately \$3.9 billion. These losses resulted from the operations of Charter Holdco and its subsidiaries and from loss carryforwards received as a result of the TWC Transaction. Federal tax net operating loss carryforwards expire in the years 2018 through 2035. In addition, as of December 31, 2016, Charter had state tax net operating loss carryforwards, resulting in a gross deferred tax asset (net of federal tax benefit) of approximately \$304 million. State tax net operating loss carryforwards generally expire in the years 2017 through 2035. Such tax loss carryforwards can accumulate and be used to offset Charter's future taxable income. As of December 31, 2016, all of Charter's federal tax loss carryforwards are subject to Section 382 and other restrictions. Pursuant to these restrictions, Charter estimates that approximately \$5.4 billion in 2017, \$3.8 billion in 2018, \$432 million in 2019 and an additional \$226 million annually over each of the next five years of federal tax loss carryforwards, should become unrestricted and available for Charter's use. An additional \$415 million is currently subject to a valuation allowance. Charter's state tax loss carryforwards are subject to similar but varying restrictions.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will be realized. In evaluating the need for a valuation allowance, management takes into account various factors, including the expected level of future taxable income, available tax planning strategies and reversals of existing taxable temporary differences. Due to Legacy Charter's history of losses, Legacy Charter was historically unable to assume future taxable income in its analysis and accordingly valuation allowances were established against the deferred tax assets, net of deferred tax liabilities, from definite-lived assets for book accounting purposes. However, as a result of the TWC Transaction, deferred tax liabilities resulting from the book fair value adjustment increased significantly and future taxable income that will result from the reversal of existing temporary differences for which deferred tax liabilities are recognized, is sufficient to conclude it is more likely than not that we will realize substantially all of our deferred tax assets. As a result, Charter has reversed approximately \$3.3 billion of its valuation allowance and recognized a corresponding income tax benefit in the consolidated statements of operations for the year ended December 31, 2016. Approximately \$145 million of valuation allowance associated with federal tax net operating loss carryforwards and approximately \$55 million of valuation allowance associated with state tax loss carryforwards and other miscellaneous deferred tax assets remains on the December 31, 2016 consolidated balance sheet.

In determining our tax provision for financial reporting purposes, Charter establishes a reserve for uncertain tax positions unless such positions are determined to be "more likely than not" of being sustained upon examination, based on their technical merits. In evaluating whether a tax position has met the more-likely-than-not recognition threshold, we presume the position will be examined by the appropriate taxing authority that has full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured to determine the amount of benefit to be recognized in our financial statements. The tax position is measured as the largest amount of benefit that has a greater than 50% likelihood of being realized when the position is ultimately resolved. There is considerable judgment involved in determining whether positions taken on the tax return are "more likely than not" of being sustained. Charter adjusts its uncertain tax reserve estimates periodically because of ongoing examinations by, and settlements with, the various taxing authorities, as well as changes in tax laws, regulations and interpretations.



No tax years for Charter, Charter Holdings or Charter Holdco, for income tax purposes, are currently under examination by the IRS. Charter and Charter Holdings' 2016 tax year remains open for assessment. Legacy Charter's tax years ending 2013 through the short period return dated May 17, 2016 remain subject to examination and assessment. Years prior to 2013 remain open solely for purposes of examination of Legacy Charter's loss and credit carryforwards. The IRS is currently examining Legacy TWC's income tax returns for 2011 and 2012. Legacy TWC's tax years ending 2013 through 2015 remain subject to examination and assessment. Prior to Legacy TWC's separation from Time Warner Inc. ("Time Warner") in March 2009 (the "Separation"), Legacy TWC was included in the consolidated U.S. federal and certain state income tax returns of Time Warner. The IRS is currently examining Time Warner's 2008 through 2010 income tax returns. Time Warner's income tax returns for 2005 to 2007, which are periods prior to the separation, were settled with the exception of an immaterial item that has been referred to the IRS Appeals Division. We have unrecognized tax benefits, exclusive of interest and penalties, totaling approximately \$172 million and \$5 million as of December 31, 2016 and 2015, respectively.

### *Litigation*

Legal contingencies have a high degree of uncertainty. When a loss from a contingency becomes estimable and probable, a reserve is established. The reserve reflects management's best estimate of the probable cost of ultimate resolution of the matter and is revised as facts and circumstances change. A reserve is released when a matter is ultimately brought to closure or the statute of limitations lapses. We have established reserves for certain matters. Although these matters are not expected individually to have a material adverse effect on our consolidated financial condition, results of operations or liquidity, such matters could have, in the aggregate, a material adverse effect on our consolidated financial condition, results of operations or liquidity.

### *Programming agreements*

We exercise significant judgment in estimating programming expense associated with certain video programming contracts. Our policy is to record video programming costs based on our contractual agreements with our programming vendors, which are generally multi-year agreements that provide for us to make payments to the programming vendors at agreed upon market rates based on the number of customers to which we provide the programming service. If a programming contract expires prior to the parties' entry into a new agreement and we continue to distribute the service, we estimate the programming costs during the period there is no contract in place. In doing so, we consider the previous contractual rates, inflation and the status of the negotiations in determining our estimates. When the programming contract terms are finalized, an adjustment to programming expense is recorded, if necessary, to reflect the terms of the new contract. We also make estimates in the recognition of programming expense related to other items, such as the accounting for free periods, timing of rate increases and credits from service interruptions, as well as the allocation of consideration exchanged between the parties in multiple-element transactions.

Significant judgment is also involved when we enter into agreements that result in us receiving cash consideration from the programming vendor, usually in the form of advertising sales, channel positioning fees, launch support or marketing support. In these situations, we must determine based upon facts and circumstances if such cash consideration should be recorded as revenue, a reduction in programming expense or a reduction in another expense category (e.g., marketing).

### *Pension plans*

Upon completion of the TWC Transaction, we assumed Legacy TWC's pension plans. We sponsor two qualified defined benefit pension plans, the TWC Pension Plan and the TWC Union Pension Plan (collectively, the "TWC Pension Plans"), that provide pension benefits to a majority of Legacy TWC employees. We also provide a nonqualified defined benefit pension plan for certain employees under the TWC Excess Pension Plan. As of December 31, 2016, the accumulated benefit obligation and fair value of plan assets for the TWC Pension Plans was \$3.3 billion and \$2.9 billion, respectively, and the net underfunded liability of the TWC Pension Plans was recorded as a \$1 million noncurrent asset, \$6 million current liability and \$309 million long-term liability.

Pension benefits are based on formulas that reflect the employees' years of service and compensation during their employment period. Actuarial gains or losses are changes in the amount of either the benefit obligation or the fair value of plan assets resulting from experience different from that assumed or from changes in assumptions. We have elected to follow a mark-to-market pension accounting policy for recording the actuarial gains or losses annually during the fourth quarter, or earlier if a remeasurement event occurs during an interim period. We use a December 31 measurement date for our pension plans.

We recognized a net periodic pension benefit of \$813 million in 2016. Net periodic pension benefit or expense is determined using certain assumptions, including the expected long-term rate of return on plan assets, discount rate and expected rate of compensation increases. We determined the discount rate used to compute pension expense based on the yield of a large population of high-quality corporate bonds with cash flows sufficient in timing and amount to settle projected future defined benefit payments. In developing the expected long-term rate of return on assets, we considered the current pension portfolio's composition, past



average rate of earnings, and our asset allocation targets. We used a discount rate of 3.99% from the date of the Transaction to June 30, 2016, and 3.72% from July 1, 2016 to December 31, 2016 to compute 2016 pension expense. A decrease in the discount rate of 25 basis points would result in a \$154 million increase in our pension plan benefit obligation as of December 31, 2016 and net periodic pension expense recognized in 2016 under our mark-to-market accounting policy. Our expected long-term rate of return on plan assets used to compute 2016 pension expense was 6.50%. A decrease in the expected long-term rate of return of 25 basis points, from 6.50% to 6.25%, while holding all other assumptions constant, would result in an increase in our 2017 net periodic pension expense of approximately \$7 million. See Note 21 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data" for additional discussion on these assumptions.

## Results of Operations

The following table sets forth the consolidated statements of operations for the periods presented (dollars in millions, except per share data):

	Year Ended December 31,		
	2016	2015	2014
Revenues	\$ 29,003	\$ 9,754	\$ 9,108
Costs and Expenses:			
Operating costs and expenses (exclusive of items shown separately below)	18,655	6,426	5,973
Depreciation and amortization	6,907	2,125	2,102
Other operating expenses, net	86	89	62
	<u>25,648</u>	<u>8,640</u>	<u>8,137</u>
Income from operations	<u>3,355</u>	<u>1,114</u>	<u>971</u>
Other Expenses:			
Interest expense, net	(2,499)	(1,306)	(911)
Loss on extinguishment of debt	(111)	(128)	—
Gain (loss) on financial instruments, net	89	(4)	(7)
Other expense, net	(14)	(7)	—
	<u>(2,535)</u>	<u>(1,445)</u>	<u>(918)</u>
Income (loss) before income taxes	820	(331)	53
Income tax benefit (expense)	2,925	60	(236)
Consolidated net income (loss)	<u>3,745</u>	<u>(271)</u>	<u>(183)</u>
Less: Net income attributable to noncontrolling interests	(223)	—	—
Net income (loss) attributable to Charter shareholders	<u>\$ 3,522</u>	<u>\$ (271)</u>	<u>\$ (183)</u>
<b>EARNINGS (LOSS) PER COMMON SHARE ATTRIBUTABLE TO CHARTER SHAREHOLDERS:</b>			
Basic	<u>\$ 17.05</u>	<u>\$ (2.68)</u>	<u>\$ (1.88)</u>
Diluted	<u>\$ 15.94</u>	<u>\$ (2.68)</u>	<u>\$ (1.88)</u>
Weighted average common shares outstanding, basic	<u>206,539,100</u>	<u>101,152,647</u>	<u>97,991,915</u>
Weighted average common shares outstanding, diluted	<u>234,791,439</u>	<u>101,152,647</u>	<u>97,991,915</u>

**Revenues.** Total revenues grew \$19.2 billion or 197% in the year ended December 31, 2016 as compared to 2015 and grew \$646 million or 7.1% in the year ended December 31, 2015 as compared to 2014. Revenue growth primarily reflects the Transactions and increases in the number of residential Internet and triple play customers and in commercial business customers, growth in rates driven by higher equipment revenue and rate increases offset by a decrease in basic video customers. The Transactions increased revenues for year ended December 31, 2016 as compared to 2015 by approximately \$18.6 billion. On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, total revenue growth was 7% for the year ended December 31, 2016 compared to 2015.



Revenues by service offering were as follows (dollars in millions; all percentages are calculated using whole numbers. Minor differences may exist due to rounding):

	Years ended December 31,					Years ended December 31,		
	Actual					Pro Forma		
	2016	2015	2014	2016 vs. 2015 Growth	2015 vs. 2014 Growth	2016	2015	2016 vs. 2015 Growth
Video	\$ 11,967	\$ 4,587	\$ 4,443	160.9%	3.2%	\$ 16,390	\$ 16,029	2.3%
Internet	9,272	3,003	2,576	208.7%	16.6%	12,688	11,295	12.3%
Voice	2,005	539	575	272.2%	(6.4)%	2,905	2,842	2.2%
Residential revenue	23,244	8,129	7,594	185.9%	7.0%	31,983	30,166	6.0%
Small and medium business	2,480	764	676	224.7%	13.0%	3,409	3,009	13.3%
Enterprise	1,429	363	317	293.0%	14.8%	2,025	1,818	11.4%
Commercial revenue	3,909	1,127	993	246.7%	13.5%	5,434	4,827	12.6%
Advertising sales	1,235	309	341	300.3%	(9.5)%	1,696	1,524	11.3%
Other	615	189	180	225.0%	5.0%	910	877	4.0%
	<u>\$ 29,003</u>	<u>\$ 9,754</u>	<u>\$ 9,108</u>	197.3%	7.1%	<u>\$ 40,023</u>	<u>\$ 37,394</u>	7.0%

Video revenues consist primarily of revenues from basic and digital video services provided to our residential customers, as well as franchise fees, equipment rental and video installation revenue. Excluding the impacts of the Transactions, residential video customers increased by 42,000 in 2016 and decreased by 2,000 in 2015. The increases in video revenues are attributable to the following (dollars in millions):

	2016 compared to 2015	2015 compared to 2014
Incremental video services, price adjustments and bundle revenue allocation	\$ 103	\$ 161
Increase (decrease) in VOD and pay-per-view	(22)	15
Increase (decrease) in average basic video customers	35	(32)
TWC Transaction	6,263	—
Bright House Transaction	1,001	—
	<u>\$ 7,380</u>	<u>\$ 144</u>

On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, residential video customers decreased by 226,000 in 2016 and the increase in video revenues is attributable to the following (dollars in millions):

	2016 compared to 2015
Incremental video services, price adjustments and bundle revenue allocation	\$ 498
Decrease in VOD and pay-per-view	(69)
Decrease in average basic video customers	(68)
	<u>\$ 361</u>

Excluding the impacts of the Transactions, residential Internet customers grew by 461,000 and 442,000 customers in 2016 and 2015, respectively. The increases in Internet revenues from our residential customers are attributable to the following (dollars in millions):

	<u>2016 compared to 2015</u>	<u>2015 compared to 2014</u>
Increase in average residential Internet customers	\$ 284	\$ 242
Service level changes, price adjustments and bundle revenue allocation	62	185
TWC Transaction	5,063	—
Bright House Transaction	860	—
	<u>\$ 6,269</u>	<u>\$ 427</u>

On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, residential Internet customers increased by 1,463,000 in 2016 and the increase in Internet revenues is attributable to the following (dollars in millions):

	<u>2016 compared to 2015</u>
Increase in average residential Internet customers	\$ 957
Service level changes, price adjustments and bundle revenue allocation	436
	<u>\$ 1,393</u>

Excluding the impacts of the Transactions, residential voice customers grew by 95,000 and 159,000 customers in 2016 and 2015, respectively. The change in voice revenues from our residential customers is attributable to the following (dollars in millions):

	<u>2016 compared to 2015</u>	<u>2015 compared to 2014</u>
Increase in average residential voice customers	\$ 28	\$ 34
Price adjustments and bundle revenue allocation	(18)	(70)
TWC Transaction	1,247	—
Bright House Transaction	209	—
	<u>\$ 1,466</u>	<u>\$ (36)</u>

On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, residential voice customers increased by 368,000 in 2016 and the increase in voice revenues is attributable to the following (dollars in millions):

	<u>2016 compared to 2015</u>
Increase in average residential voice customers	\$ 229
Price adjustments and bundle revenue allocation	(166)
	<u>\$ 63</u>

Excluding the impacts of the Transactions, small and medium business PSUs increased 128,000 and 109,000 in 2016 and 2015, respectively. The increases in small and medium business commercial revenues are attributable to the following (dollars in millions):

	<u>2016 compared to 2015</u>	<u>2015 compared to 2014</u>
Increase in small and medium business customers	\$ 127	\$ 112
Price adjustments	(38)	(24)
TWC Transaction	1,408	—
Bright House Transaction	219	—
	<u>\$ 1,716</u>	<u>\$ 88</u>

On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, small and medium business PSUs increased by 291,000 in 2016 and the increase in small and medium business commercial revenues is attributable to the following (dollars in millions):

	<u>2016 compared to 2015</u>
Increase in small and medium business customers	\$ 359
Price adjustments	41
	<u>\$ 400</u>

Excluding the impacts of the Transactions, enterprise PSUs increased 6,000 and 5,000 in 2016 and 2015, respectively. On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, enterprise PSUs increased by 16,000 in 2016. The Transactions increased enterprise commercial revenues for year ended December 31, 2016 as compared to 2015 by approximately \$1.0 billion. On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, enterprise commercial revenues increased \$207 million during the year ended December 31, 2016 compared to 2015 primarily due to growth in customers.

Advertising sales revenues consist primarily of revenues from commercial advertising customers, programmers and other vendors, as well as local cable and advertising on regional sports and news channels. Advertising sales revenues increased in 2016 primarily due to the Transactions and decreased in 2015 primarily as a result of a decrease in political advertising. The Transactions increased advertising sales revenues for the year ended December 31, 2016 as compared to 2015 by \$898 million. On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, advertising sales revenues increased \$172 million during the year ended December 31, 2016 compared to 2015 primarily due to an increase in political advertising.

Other revenues consist of revenue from regional sports and news channels (excluding intercompany charges or advertising sales on those channels), home shopping, late payment fees, wire maintenance fees and other miscellaneous revenues. The increase in 2016 was primarily due to the Transactions. The Transactions increased other revenues for the year ended December 31, 2016 as compared to 2015 by \$429 million. On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, other revenues increased \$33 million during the year ended December 31, 2016 compared to 2015 primarily due to a settlement related to an early contract termination.

**Operating costs and expenses.** The increases in our operating costs and expenses are attributable to the following (dollars in millions):

	<u>2016 compared to 2015</u>	<u>2015 compared to 2014</u>
Programming	\$ 4,356	\$ 219
Regulatory, connectivity and produced content	1,032	7
Costs to service customers	3,468	26
Marketing	1,071	11
Transition costs	84	58
Other	2,218	132
	<u>\$ 12,229</u>	<u>\$ 453</u>

Programming costs were approximately \$7.0 billion, \$2.7 billion and \$2.5 billion, representing 38%, 42% and 41% of operating costs and expenses for each of the years ended December 31, 2016, 2015 and 2014, respectively. The increase in operating costs and expenses for the year ended December 31, 2016 compared to 2015 was primarily due to the Transactions.

The increase in other expense is attributable to the following (dollars in millions):

	<u>2016 compared to 2015</u>	<u>2015 compared to 2014</u>
Corporate costs	\$ 540	\$ 44
Advertising sales expense	405	10
Enterprise	390	7
Property tax and insurance	198	17
Bad debt expense	188	15
Stock compensation expense	166	23
Bank fees	114	6
Other	217	10
	<u>\$ 2,218</u>	<u>\$ 132</u>

The increases in other expense for the year ended December 31, 2016 compared to the corresponding prior periods were primarily due to the Transactions.

On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, increases in our operating costs and expenses, exclusive of items shown separately in the consolidated statements of operations, are attributable to the following (dollars in millions):

	<u>2016 compared to 2015</u>
Programming	\$ 661
Regulatory, connectivity and produced content	28
Costs to service customers	76
Marketing	53
Transition costs	84
Other	316
	<u>\$ 1,218</u>

On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, programming costs were approximately \$9.6 billion and \$9.0 billion, representing 37% and 36% of total operating costs and expenses for the years ended December 31, 2016 and 2015, respectively.



Programming costs consist primarily of costs paid to programmers for basic, digital, premium, VOD, and pay-per-view programming. The increase in pro forma programming costs is primarily a result of annual contractual rate adjustments, including increases in amounts paid for retransmission consents and the introduction of new networks offset by synergies as a result of the Transactions and lower pay-per-view programming expenses. We expect pro forma programming expenses will continue to increase due to a variety of factors, including annual increases imposed by programmers with additional selling power as a result of media consolidation, increased demands by owners of broadcast stations for payment for retransmission consent or linking carriage of other services to retransmission consent, and additional programming, particularly new services. We have been unable to fully pass these increases on to our customers nor do we expect to be able to do so in the future without a potential loss of customers.

On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, the increase in other expense is attributable to the following (dollars in millions):

	<b>2016 compared to 2015</b>
Advertising sales expense	\$ 100
Corporate costs	86
Stock compensation expense	49
Enterprise	48
Bank fees	33
	<u>\$ 316</u>

The increase in advertising sales expense relates primarily to higher advertising sales revenue. The increase in corporate costs relates primarily to increases in the number of employees including increases in engineering and IT. Stock compensation expense increased primarily due to increases in headcount and the value of equity issued.

**Depreciation and amortization.** Depreciation and amortization expense increased by \$4.8 billion in 2016 compared to 2015 primarily as a result of additional depreciation and amortization related to the Transactions, inclusive of the incremental amounts as a result of the higher fair values recorded in acquisition accounting. Depreciation and amortization expense increased by \$23 million in 2015 compared to 2014 which primarily represents depreciation on more recent capital expenditures offset by certain assets becoming fully depreciated.

**Other operating expenses, net.** The changes in other operating expenses, net are attributable to the following (dollars in millions):

	<b>2016 compared to 2015</b>	<b>2015 compared to 2014</b>
Merger and restructuring costs	\$ 900	\$ 32
Other pension benefits	(899)	—
Special charges, net	2	1
(Gain) loss on sale of assets, net	(6)	(6)
	<u>\$ (3)</u>	<u>\$ 27</u>

The increase in merger and restructuring costs is primarily due to approximately \$262 million of Legacy Charter and Legacy TWC contingent financing and advisory transaction fees paid at the closing of the Transactions as well as approximately \$642 million of employee retention and employee termination costs incurred during 2016. Other pension benefits includes the pension curtailment gain of \$675 million, rereasurement gain of \$195 million, expected return on plan assets of \$116 million offset by interest costs of \$87 million. For more information, see Note 15 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data."

**Interest expense, net.** Net interest expense increased by \$1.2 billion in 2016 from 2015 and by \$395 million in 2015 from 2014 primarily as a result of an increase of \$463 million and \$446 million, respectively, of interest expense associated with the debt incurred to fund the Transactions, and, in 2016, \$604 million associated with debt assumed from Legacy TWC.



**Loss on extinguishment of debt.** Loss on extinguishment of debt of \$111 million and \$128 million for the years ended December 31, 2016 and 2015 primarily represents losses recognized as a result of the repurchase of CCO Holdings notes. For more information, see Note 9 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data."

**Gain (loss) on financial instruments, net.** Interest rate derivative instruments are used to manage our interest costs and to reduce our exposure to increases in floating interest rates, and cross-currency derivative instruments are used to manage foreign exchange risk related to the foreign currency denominated debt assumed in the TWC Transaction. We recorded gains of \$89 million and losses of \$4 million and \$7 million during the years ended December 31, 2016, 2015 and 2014, respectively. Gains and losses on financial instruments are recognized due to changes in the fair value of our interest rate and, in 2016 our cross currency derivative instruments and the remeasurement of the fixed-rate British pound sterling denominated notes (the "Sterling Notes") into U.S. dollars. The year ended December 31, 2016 also includes an \$11 million loss realized upon termination of Legacy TWC interest rate swap derivative instruments. For more information, see Note 12 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data."

**Other expense, net.** Other expense, net primarily represents equity losses on our equity-method investments. For more information, see Note 7 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data."

**Income tax benefit (expense).** We recognized income tax benefits of \$2.9 billion and \$60 million for the years ended December 31, 2016 and 2015, respectively, and income tax expense of \$236 million for the year ended December 31, 2014. Certain of the deferred tax liabilities that were assumed in connection with the closing of the TWC Transaction will reverse and provide a source of future taxable income, resulting in a reduction of approximately \$3.3 billion of Legacy Charter's preexisting valuation allowance associated with its deferred tax assets. Such release of Legacy Charter's valuation allowance was recognized directly to income tax benefit in the consolidated statements of operations for the year ended December 31, 2016. Income tax benefit for the year ended December 31, 2016 was also impacted by a change in a state tax law that resulted in approximately \$65 million of tax benefit. The tax provision in future periods will vary based on current and future temporary differences, as well as future operating results. For more information, see Note 17 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data."

The income tax benefit in 2015 was primarily due to the deemed liquidation of Charter Holdco solely for federal and state income tax purposes, resulting in a \$187 million deferred income tax benefit offset by income tax expense primarily through increases in deferred tax liabilities. Income tax expense was recognized in 2015 and 2014 primarily through increases in deferred tax liabilities related to Legacy Charter's franchises, which are characterized as indefinite lived for book financial reporting purposes, as well as, to a lesser extent, through current federal and state income tax expense.

**Net income attributable to noncontrolling interest.** Net income attributable to noncontrolling interest for financial reporting purposes represents A/N's portion of Charter Holdings' net income based on its effective common unit ownership interest of approximately 10% and on the preferred dividend of \$93 million for the year ended December 31, 2016. For more information, see Note 11 to the accompanying consolidated financial statements contained in "Item 1. Financial Statements."

**Net income (loss) attributable to Charter shareholders.** Net income attributable to Charter shareholders was \$3.5 billion for the year ended December 31, 2016 and net loss attributable to Charter shareholders was \$271 million and \$183 million for the years ended December 31, 2016, 2015 and 2014, respectively, primarily as a result of the factors described above. On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, net income attributable to Charter shareholders was \$1.1 billion and \$159 million for the years ended December 31, 2016 and 2015, respectively.

#### **Use of Adjusted EBITDA and Free Cash Flow**

We use certain measures that are not defined by U.S. generally accepted accounting principles ("GAAP") to evaluate various aspects of our business. Adjusted EBITDA and free cash flow are non-GAAP financial measures and should be considered in addition to, not as a substitute for, consolidated net income (loss) and net cash flows from operating activities reported in accordance with GAAP. These terms, as defined by us, may not be comparable to similarly titled measures used by other companies. Adjusted EBITDA and free cash flow are reconciled to consolidated net income (loss) and net cash flows from operating activities, respectively, below.

Adjusted EBITDA is defined as consolidated net income (loss) plus net interest expense, income taxes, depreciation and amortization, stock compensation expense, loss on extinguishment of debt, (gain) loss on financial instruments, other (income) expense, net and other operating (income) expenses, such as merger and restructuring costs, other pension benefits, special charge



s and (gain) loss on sale or retirement of assets. As such, it eliminates the significant non-cash depreciation and amortization expense that results from the capital-intensive nature of our businesses as well as other non-cash or special items, and is unaffected by our capital structure or investment activities. However, this measure is limited in that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenues and our cash cost of financing. These costs are evaluated through other financial measures.

Free cash flow is defined as net cash flows from operating activities, less capital expenditures and changes in accrued expenses related to capital expenditures.

We believe that Adjusted EBITDA and free cash flow provide information useful to investors in assessing our performance and our ability to service our debt, fund operations and make additional investments with internally generated funds. In addition, Adjusted EBITDA generally correlates to the leverage ratio calculation under our credit facilities or outstanding notes to determine compliance with the covenants contained in the facilities and notes (all such documents have been previously filed with the SEC). For the purpose of calculating compliance with leverage covenants, we use Adjusted EBITDA, as presented, excluding certain expenses paid by our operating subsidiaries to other Charter entities. Our debt covenants refer to these expenses as management fees, which fees were in the amount of \$930 million, \$322 million and \$253 million for the years ended December 31, 2016, 2015 and 2014, respectively.

	Years ended December 31,		
	2016	2015	2014
	<b>Actual</b>		
Consolidated net income (loss)	\$ 3,745	\$ (271)	\$ (183)
Plus: Interest expense, net	2,499	1,306	911
Income tax (benefit) expense	(2,925)	(60)	236
Depreciation and amortization	6,907	2,125	2,102
Stock compensation expense	244	78	55
Loss on extinguishment of debt	111	128	—
(Gain) loss on derivative instruments, net	(89)	4	7
Other, net	100	96	62
Adjusted EBITDA	<u>\$ 10,592</u>	<u>\$ 3,406</u>	<u>\$ 3,190</u>
Net cash flows from operating activities	\$ 8,041	\$ 2,359	\$ 2,359
Less: Purchases of property, plant and equipment	(5,325)	(1,840)	(2,221)
Change in accrued expenses related to capital expenditures	603	28	33
Free cash flow	<u>\$ 3,319</u>	<u>\$ 547</u>	<u>\$ 171</u>

	Year Ended December 31,	
	2016	2015
	<b>Pro Forma</b>	
Consolidated net income	\$ 1,399	\$ 338
Plus: Interest expense, net	2,883	2,968
Income tax expense	498	102
Depreciation and amortization	9,555	9,348
Stock compensation expense	295	246
Loss on extinguishment of debt	111	128
(Gain) loss on financial instruments, net	(89)	4
Other, net	(188)	(130)
Adjusted EBITDA	<u>\$ 14,464</u>	<u>\$ 13,004</u>



## Liquidity and Capital Resources

### Overview

We have significant amounts of debt. The principal amount of our debt as of December 31, 2016 was \$60.0 billion, consisting of \$8.9 billion of credit facility debt, \$37.7 billion of investment grade senior secured notes and \$13.4 billion of high-yield senior unsecured notes. Our business requires significant cash to fund principal and interest payments on our debt.

Our projected cash needs and projected sources of liquidity depend upon, among other things, our actual results, and the timing and amount of our expenditures. Free cash flow was \$3.3 billion, \$547 million and \$171 million for the years ended December 31, 2016, 2015 and 2014, respectively. As of December 31, 2016, the amount available under our credit facilities was approximately \$2.8 billion and cash on hand was approximately \$1.5 billion. We expect to utilize free cash flow, cash on hand and availability under our credit facilities as well as future refinancing transactions to further extend the maturities of or reduce the principal on our obligations. The timing and terms of any refinancing transactions will be subject to market conditions. Additionally, we may, from time to time, and depending on market conditions and other factors, use cash on hand and the proceeds from securities offerings or other borrowings to retire our debt through open market purchases, privately negotiated purchases, tender offers or redemption provisions. We believe we have sufficient liquidity from cash on hand, free cash flow and Charter Operating's revolving credit facility as well as access to the capital markets to fund our projected cash needs.

We continue to evaluate the deployment of our cash on hand and anticipated future free cash flow including to invest in our business growth and other strategic opportunities, including mergers and acquisitions as well as stock repurchases and dividends. Our target leverage remains at 4 to 4.5 times, and up to 3.5 times at the Charter Operating level. In 2016, Charter purchased approximately 5.1 million shares of its Class A common stock for approximately \$1.3 billion pursuant to authorizations by Charter's board of directors of \$3 billion. Accordingly, as of December 31, 2016 and provided Charter's and Charter Operating's leverage ratios remain at target, management has authority to cause Charter to purchase an additional \$1.7 billion of Charter's Class A common stock without taking into account shares or units that may be purchased from A/N. Effective November 1, 2016, Charter's board of directors granted authority for a new \$750 million of Class A common stock buybacks under the rolling six-month authority without taking into account any Class A common stock purchased prior to November 1. As a result, a portion of the \$1.7 billion of authority is under the authority of management to approve up to \$750 million for Class A common stock buybacks in any six-month period. Charter is not obligated to acquire any particular amount of common stock, and the timing of any purchases that may occur cannot be predicted and will largely depend on market conditions and other potential uses of capital. Purchases may include open market purchases or negotiated transactions. As possible acquisitions, swaps or dispositions arise, we actively review them against our objectives including, among other considerations, improving the operational efficiency, clustering, product development or technology capabilities of our business and achieving appropriate return targets, and we may participate to the extent we believe these possibilities present attractive opportunities. However, there can be no assurance that we will actually complete any acquisitions, dispositions or system swaps, or that any such transactions will be material to our operations or results.

In December 2016, Charter and A/N exchanged 1.9 million Charter Holdings common units held by A/N for shares of Charter Class A common stock pursuant to the Letter Agreement for an aggregate purchase price of \$537 million. The Letter Agreement also requires A/N to sell to Charter or to Charter Holdings, on a monthly basis, a number of shares of Charter Class A common stock or Charter Holdings common units that represents a pro rata participation by A/N and its affiliates in any repurchases of shares of Charter Class A common stock from persons other than A/N effected by Charter during the immediately preceding calendar month, at a purchase price equal to the average price paid by Charter for the shares repurchased from persons other than A/N during such immediately preceding calendar month. Pursuant to the Letter Agreement, Charter Holdings purchased from A/N 752,767 Charter Holdings common units at a price per unit of \$289.83, or \$218 million.

### Recent Events

In January 2017, Charter Operating entered into an amendment to its Credit Agreement decreasing the applicable LIBOR margin on both the term loan E and term loan F to 2.00% and eliminating the LIBOR floor.

In February 2017, CCO Holdings and CCO Holdings Capital Corp. closed on transactions in which they issued \$1.0 billion aggregate principal amount of 5.125% senior notes due 2027. The net proceeds will be used to redeem CCO Holdings' 6.625% senior notes due 2022, pay related fees and expenses and for general corporate purposes.

### Free Cash Flow

Free cash flow increased \$2.8 billion and \$376 million during the years ended December 31, 2016 and 2015 compared to the corresponding prior periods, respectively, due to the following.

	Year ended December 31, 2016 compared to year ended December 31, 2015	Year ended December 31, 2015 compared to year ended December 31, 2014
Increase in Adjusted EBITDA	\$ 7,186	\$ 216
(Increase) decrease in capital expenditures	(3,485)	381
Changes in working capital, excluding change in accrued interest, net of effects from acquisitions	1,387	9
Increase in cash paid for interest, net	(1,602)	(196)
Increase in merger and restructuring costs	(652)	(32)
Other, net	(62)	(2)
	<u>\$ 2,772</u>	<u>\$ 376</u>

### Contractual Obligations

The following table summarizes our payment obligations as of December 31, 2016 under our long-term debt and certain other contractual obligations and commitments (dollars in millions.)

	Payments by Period				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-Term Debt Principal Payments <sup>(a)</sup>	\$ 60,036	\$ 2,197	\$ 5,743	\$ 10,344	\$ 41,752
Long-Term Debt Interest Payments <sup>(b)</sup>	38,508	3,275	6,247	5,314	23,672
Capital and Operating Lease Obligations <sup>(c)</sup>	1,324	259	405	250	410
Programming Minimum Commitments <sup>(d)</sup>	310	225	63	22	—
Other <sup>(e)</sup>	13,187	1,334	1,514	1,203	9,136
	<u>\$ 113,365</u>	<u>\$ 7,290</u>	<u>\$ 13,972</u>	<u>\$ 17,133</u>	<u>\$ 74,970</u>

<sup>(a)</sup> The table presents maturities of long-term debt outstanding as of December 31, 2016. Refer to Notes 9 and 20 to our accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data" for a description of our long-term debt and other contractual obligations and commitments.

<sup>(b)</sup> Interest payments on variable debt are estimated using amounts outstanding at December 31, 2016 and the average implied forward London Interbank Offering Rate ("LIBOR") rates applicable for the quarter during the interest rate reset based on the yield curve in effect at December 31, 2016. Actual interest payments will differ based on actual LIBOR rates and actual amounts outstanding for applicable periods.

<sup>(c)</sup> We lease certain facilities and equipment under noncancelable capital and operating leases. Leases and rental costs charged to expense for the years ended December 31, 2016, 2015 and 2014, were \$215 million, \$49 million and \$43 million, respectively.

<sup>(d)</sup> We pay programming fees under multi-year contracts typically based on a flat fee per customer, which may be fixed for the term, or may in some cases escalate over the term. Programming costs included in the accompanying statement of operations were approximately \$7.0 billion, \$2.7 billion and \$2.5 billion, for the years ended December 31, 2016, 2015 and 2014, respectively. Certain of our programming agreements are based on a flat fee per month or have guaranteed minimum payments. The table sets forth the aggregate guaranteed minimum commitments under our programming contracts.

<sup>(e)</sup> "Other" represents other guaranteed minimum commitments, including rights negotiated directly with content owners for distribution on company-owned channels or networks and commitments related to our role as an advertising and distribution sales agent for third party-owned channels or networks as well as commitments to our customer premise equipment vendors.



The following items are not included in the contractual obligations table because the obligations are not fixed and/or determinable due to various factors discussed below. However, we incur these costs as part of our operations:

- We rent utility poles used in our operations. Generally, pole rentals are cancelable on short notice, but we anticipate that such rentals will recur. Rent expense incurred for pole rental attachments for the years ended December 31, 2016, 2015 and 2014 was \$115 million, \$53 million and \$49 million, respectively.
- We pay franchise fees under multi-year franchise agreements based on a percentage of revenues generated from video service per year. We also pay other franchise related costs, such as public education grants, under multi-year agreements. Franchise fees and other franchise-related costs included in the accompanying statement of operations were \$534 million, \$212 million and \$208 million for the years ended December 31, 2016, 2015 and 2014, respectively.
- We also have \$278 million in letters of credit, of which \$220 million is secured under the Charter Operating credit facility, primarily to our various casualty carriers as collateral for reimbursement of workers' compensation, auto liability and general liability claims.
- Minimum pension funding requirements have not been presented in the table above as such amounts have not been determined beyond 2016. We made no cash contributions to the qualified pension plans in 2016; however, we are permitted to make discretionary cash contributions to the qualified pension plans in 2017. For the nonqualified pension plan, we contributed \$5 million during 2016 and will continue to make contributions in 2017 to the extent benefits are paid.

See "Part I. Item 1. Business — Transaction-Related Commitments" for a listing of commitments as a result of the Transactions.

#### *Historical Operating, Investing, and Financing Activities*

**Cash and Cash Equivalents.** We held \$1.5 billion and \$5 million in cash and cash equivalents as of December 31, 2016 and 2015, respectively. We also held \$22.3 billion in restricted cash and cash equivalents as of December 31, 2015 representing proceeds of debt raised to fund the cash portion of the TWC Transaction consideration that were held in escrow until consummation of the TWC Transaction.

**Operating Activities.** Net cash provided by operating activities increased \$5.7 billion during the year ended December 31, 2016 compared to the year ended December 31, 2015, primarily due to an increase in Adjusted EBITDA of \$7.2 billion offset by an increase in cash paid for interest, net of \$1.6 billion.

Net cash provided by operating activities remained flat at \$2.4 billion for the years ended December 31, 2015 and 2014.

**Investing Activities.** Net cash used in investing activities for the years ended December 31, 2016, 2015 and 2014, was \$11.3 billion, \$17.0 billion and \$9.3 billion, respectively. Cash used in investing activities during the year ended December 31, 2016 primarily represented the acquisitions of Legacy TWC and Legacy Bright House with long-term restricted cash and cash equivalents and an increase in capital expenditures of \$3.5 billion as compared to 2015.

The increase in 2015 compared to 2014 is primarily due to an increase in the investment of net proceeds from the issuance of the CCO Safari II notes, CCO Safari III credit facilities and CCOH Safari notes related to the TWC Transaction in long-term restricted cash and cash equivalents offset by a decrease in long-term restricted cash and cash equivalents upon repayment of the Term G Loans and CCOH Safari notes out of escrow related to the Comcast Transactions and a decrease in capital expenditures.

**Financing Activities.** Net cash provided in financing activities was \$4.8 billion, \$14.7 billion and \$6.9 billion for the years ended December 31, 2016, 2015 and 2014, respectively. Cash provided during the year ended December 31, 2016 primarily represented the issuance of \$5 billion of equity to Liberty Broadband to fund a portion of the Transactions in 2016 offset by an increase in the purchase of treasury stock of \$1.5 billion as compared to 2015.

The increase in cash provided during the year ended December 31, 2015 as compared to the corresponding period in 2014 was primarily the result of the issuance of the CCO Safari II notes, CCO Safari III credit facilities and CCOH Safari notes related to the TWC Transaction offset by the repayment of \$7.1 billion of net proceeds held in escrow related to the CCOH Safari notes and Term G Loans upon the termination of the Comcast Transactions.

#### *Capital Expenditures*

We have significant ongoing capital expenditure requirements. Capital expenditures were \$5.3 billion, \$1.8 billion and \$2.2 billion for the years ended December 31, 2016, 2015 and 2014, respectively. The increase was driven by the Transactions. On a pro forma basis, assuming the Transactions occurred as of January 1, 2015, the increase for the year ended December 31, 2016 compared



to the corresponding prior period was driven by higher product development investments, transition capital expenditures incurred in connection with the Transactions and support capital investments. See the table below for more details.

The actual amount of our capital expenditures in 2017 will depend on a number of factors, including the pace of transition planning to service a larger customer base as a result of the Transactions, our all-digital transition in the Legacy TWC and Legacy Bright House markets and growth rates of both our residential and commercial businesses.

Our capital expenditures are funded primarily from cash flows from operating activities and borrowings on our credit facility. In addition, our liabilities related to capital expenditures increased by \$603 million, \$28 million and \$33 million for the years ended December 31, 2016, 2015 and 2014, respectively.

The following tables present our major capital expenditures categories on an actual and pro forma basis, assuming the Transactions occurred as of January 1, 2015, in accordance with National Cable and Telecommunications Association ("NCTA") disclosure guidelines for the years ended December 31, 2016, 2015 and 2014. The disclosure is intended to provide more consistency in the reporting of capital expenditures among peer companies in the cable industry. These disclosure guidelines are not required disclosures under GAAP, nor do they impact our accounting for capital expenditures under GAAP (dollars in millions):

Actual	Year ended December 31,		
	2016	2015	2014
Customer premise equipment (a)	\$ 1,864	\$ 582	\$ 1,082
Scalable infrastructure (b)	1,390	523	455
Line extensions (c)	721	194	176
Upgrade/rebuild (d)	456	128	167
Support capital (e)	894	413	341
Total capital expenditures	\$ 5,325	\$ 1,840	\$ 2,221

Capital expenditures included in total related to:

Commercial services	\$ 824	\$ 260	\$ 242
Transition (f)	\$ 460	\$ 115	\$ 27
All-digital transition	\$ —	\$ —	\$ 410

Pro Forma	Year ended December 31,	
	2016	2015
Customer premise equipment (a)	\$ 2,761	\$ 2,650
Scalable infrastructure (b)	2,009	1,702
Line extensions (c)	1,005	977
Upgrade/rebuild (d)	610	594
Support capital (e)	1,160	1,046
Total capital expenditures	\$ 7,545	\$ 6,969

- (a) Customer premise equipment includes costs incurred at the customer residence to secure new customers and revenue generating units. It also includes customer installation costs and customer premise equipment (e.g., set-top boxes and cable modems).
- (b) Scalable infrastructure includes costs not related to customer premise equipment, to secure growth of new customers and revenue generating units, or provide service enhancements (e.g., headend equipment).
- (c) Line extensions include network costs associated with entering new service areas (e.g., fiber/coaxial cable, amplifiers, electronic equipment, make-ready and design engineering).
- (d) Upgrade/rebuild includes costs to modify or replace existing fiber/coaxial cable networks, including betterments.
- (e) Support capital includes costs associated with the replacement or enhancement of non-network assets due to technological and physical obsolescence (e.g., non-network equipment, land, buildings and vehicles).
- (f) Transition represents incremental costs incurred to integrate the Legacy TWC and Legacy Bright House operations and to bring the three companies' systems and processes into a uniform operating structure.



**Debt**

As of December 31, 2016, the accreted value of our total debt was approximately \$61.7 billion, as summarized below (dollars in millions):

	December 31, 2016		Interest Payment Dates	Maturity Date (b)
	Principal Amount	Accreted Value (a)		
<b>CCO Holdings, LLC:</b>				
5.250% senior notes due 2021	\$ 500	\$ 496	3/15 & 9/15	3/15/2021
6.625% senior notes due 2022	750	741	1/31 & 7/31	1/31/2022
5.250% senior notes due 2022	1,250	1,232	3/30 & 9/30	9/30/2022
5.125% senior notes due 2023	1,000	992	2/15 & 8/15	2/15/2023
5.125% senior notes due 2023	1,150	1,141	5/1 & 11/1	5/1/2023
5.750% senior notes due 2023	500	496	3/1 & 9/1	9/1/2023
5.750% senior notes due 2024	1,000	991	1/15 & 7/15	1/15/2024
5.875% senior notes due 2024	1,700	1,685	4/1 & 10/1	4/1/2024
5.375% senior notes due 2025	750	744	5/1 & 11/1	5/1/2025
5.750% senior notes due 2026	2,500	2,460	2/15 & 8/15	2/15/2026
5.500% senior notes due 2026	1,500	1,487	5/1 & 11/1	5/1/2026
5.875% senior notes due 2027	800	794	5/1 & 11/1	5/1/2027
<b>Charter Communications Operating, LLC:</b>				
3.579% senior notes due 2020	2,000	1,983	1/23 & 7/23	7/23/2020
4.464% senior notes due 2022	3,000	2,973	1/23 & 7/23	7/23/2022
4.908% senior notes due 2025	4,500	4,458	1/23 & 7/23	7/23/2025
6.384% senior notes due 2035	2,000	1,980	4/23 & 10/23	10/23/2035
6.484% senior notes due 2045	3,500	3,466	4/23 & 10/23	10/23/2045
6.834% senior notes due 2055	500	495	4/23 & 10/23	10/23/2055
Credit facilities	8,916	8,814		Varies
<b>Time Warner Cable, LLC:</b>				
5.850% senior notes due 2017	2,000	2,028	5/1 & 11/1	5/1/2017
6.750% senior notes due 2018	2,000	2,135	1/1 & 7/1	7/1/2018
8.750% senior notes due 2019	1,250	1,412	2/14 & 8/14	2/14/2019
8.250% senior notes due 2019	2,000	2,264	4/1 & 10/1	4/1/2019
5.000% senior notes due 2020	1,500	1,615	2/1 & 8/1	2/1/2020
4.125% senior notes due 2021	700	739	2/15 & 8/15	2/15/2021
4.000% senior notes due 2021	1,000	1,056	3/1 & 9/1	9/1/2021
5.750% sterling senior notes due 2031 <sup>(c)</sup>	770	834	6/2	6/2/2031
6.550% senior debentures due 2037	1,500	1,691	5/1 & 11/1	5/1/2037
7.300% senior debentures due 2038	1,500	1,795	1/1 & 7/1	7/1/2038
6.750% senior debentures due 2039	1,500	1,730	6/15 & 12/15	6/15/2039
5.875% senior debentures due 2040	1,200	1,259	5/15 & 11/15	11/15/2040
5.500% senior debentures due 2041	1,250	1,258	3/1 & 9/1	9/1/2041
5.250% sterling senior notes due 2042 <sup>(d)</sup>	800	771	7/15	7/15/2042
4.500% senior debentures due 2042	1,250	1,135	3/15 & 9/15	9/15/2042
<b>Time Warner Cable Enterprises LLC:</b>				
8.375% senior debentures due 2023	1,000	1,273	3/15 & 9/15	3/15/2023
8.375% senior debentures due 2033	1,000	1,324	7/15 & 1/15	7/15/2033

\$	60,036	\$	61,747
<u>          </u>		<u>          </u>	

- (a) The accreted values presented in the table above represent the principal amount of the debt less the original issue discount at the time of sale, deferred financing costs, and, (i) in regards to the Legacy TWC debt assumed, a fair value premium adjustment as a result of applying acquisition accounting plus/minus the accretion of those amounts to the balance sheet date and (ii) in regards to the fixed-rate British pound sterling denominated notes (the "Sterling Notes"), a remeasurement of the principal amount of the debt and any premium or discount into US dollars as of the balance sheet date. However, the amount that is currently payable if the debt becomes immediately due is equal to the principal amount of the debt. We have availability under our credit facilities of approximately \$2.8 billion as of December 31, 2016.
- (b) In general, the obligors have the right to redeem all of the notes set forth in the above table in whole or in part at their option, beginning at various times prior to their stated maturity dates, subject to certain conditions, upon the payment of the outstanding principal amount (plus a specified redemption premium) and all accrued and unpaid interest. For additional information see "Description of our Outstanding Debt" below.
- (c) Principal amount includes £625 million valued at \$770 million as of December 31, 2016 using the exchange rate as of December 31, 2016.
- (d) Principal amount includes £650 million valued at \$800 million as of December 31, 2016 using the exchange rate as of December 31, 2016.

See Note 9 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data" for further details regarding our outstanding debt and other financing arrangements, including certain information about maturities, covenants and restrictions related to such debt and financing arrangements. The agreements and instruments governing our debt and financing arrangements are complicated and you should consult such agreements and instruments which are filed with the SEC for more detailed information.

At December 31, 2016, Charter Operating had a consolidated leverage ratio of approximately 2.8 to 1.0 and a consolidated first lien leverage ratio of 2.7 to 1.0. Both ratios are in compliance with the ratios required by the Charter Operating credit facilities of 5.0 to 1.0 consolidated leverage ratio and 4.0 to 1.0 consolidated first lien leverage ratio. A failure by Charter Operating to maintain the financial covenants would result in an event of default under the Charter Operating credit facilities and the debt of CCO Holdings. See "Part I. Item 1A. Risk Factors — The agreements and instruments governing our debt contain restrictions and limitations that could significantly affect our ability to operate our business, as well as significantly affect our liquidity."

#### **Recently Issued Accounting Standards**

See Note 22 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data" for a discussion of recently issued accounting standards.

#### **Item 7A. *Quantitative and Qualitative Disclosures About Market Risk.***

We use derivative instruments to manage interest rate risk on variable debt and foreign exchange risk on the Sterling Notes, and do not hold or issue derivative instruments for speculative trading purposes.

Interest rate derivative instruments are used to manage interest costs and to reduce our exposure to increases in floating interest rates. We manage our exposure to fluctuations in interest rates by maintaining a mix of fixed and variable-rate debt. Using interest rate derivative instruments, we agree to exchange, at specified intervals through 2017, the difference between fixed and variable interest amounts calculated by reference to agreed-upon notional principal amounts.

Upon closing of the TWC Transaction, we assumed cross-currency derivative instruments. Cross-currency derivative instruments are used to effectively convert £1.275 billion aggregate principal amount of fixed-rate British pound sterling denominated debt, including annual interest payments and the payment of principal at maturity, to fixed-rate U.S. dollar denominated debt. The cross-currency derivative instruments have maturities of June 2031 and July 2042. We are required to post collateral on the cross-currency derivative instruments when such instruments are in a liability position. In May 2016, we entered into a collateral holiday agreement for 80% of both the 2031 and 2042 cross-currency swaps, which eliminates the requirement to post collateral for three years. For more information, see Note 12 to the accompanying consolidated financial statements contained in "Part II. Item 8. Financial Statements and Supplementary Data."

As of December 31, 2016 and 2015, the weighted average interest rate on the credit facility debt, including the effects of our interest rate swap agreements, was approximately 2.9% and 3.3%, respectively, and the weighted average interest rate on the senior notes was approximately 5.9% and 5.5%, respectively, resulting in a blended weighted average interest rate of 5.4% and 5.1%, respectively. The interest rate on approximately 87% and 83% of the total principal amount of our debt was effectively fixed, including the effects of our interest rate swap agreements, as of December 31, 2016 and 2015, respectively.



The table set forth below summarizes the fair values and contract terms of financial instruments subject to interest rate risk maintained by us as of December 31, 2016 (dollars in millions):

	2017	2018	2019	2020	2021	Thereafter	Total	Fair Value
<b>Debt:</b>								
Fixed Rate	\$ 2,000	\$ 2,000	\$ 3,250	\$ 3,500	\$ 2,200	\$ 38,170	\$ 51,120	\$ 55,203
Average Interest Rate	5.85%	6.75%	8.44%	4.19%	4.32%	5.84%	5.86%	
Variable Rate	\$ 197	\$ 197	\$ 296	\$ 1,716	\$ 2,928	\$ 3,582	\$ 8,916	\$ 8,943
Average Interest Rate	3.15%	3.66%	3.96%	4.49%	4.37%	4.81%	4.51%	
<b>Interest Rate Instruments:</b>								
Variable to Fixed Rate	\$ 850	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 850	\$ 5
Average Pay Rate	3.84%	—%	—%	—%	—%	—%	3.84%	
Average Receive Rate	3.70%	—%	—%	—%	—%	—%	3.70%	

As of December 31, 2016, we had \$850 million in notional amounts of interest rate derivative instruments outstanding. The notional amounts of interest rate derivative instruments do not represent amounts exchanged by the parties and, thus, are not a measure of our exposure to credit loss. The amounts exchanged are determined by reference to the notional amount and the other terms of the contracts.

The estimated fair value of the interest rate derivative instruments is determined using a present value calculation based on an implied forward LIBOR curve (adjusted for Charter Operating's or counterparties' credit risk). Interest rates on variable-rate debt are estimated using the average implied forward LIBOR for the year of maturity based on the yield curve in effect at December 31, 2016 including applicable bank spread.

#### **Item 8. Financial Statements and Supplementary Data.**

Our consolidated financial statements, the related notes thereto, and the reports of independent accountants are included in this annual report beginning on page F-I.

#### **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.**

None.

#### **Item 9A. Controls and Procedures.**

##### **Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures**

As of the end of the period covered by this report, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we have evaluated the effectiveness of the design and operation of disclosure controls and procedures with respect to the information generated for use in this annual report. The evaluation was based upon reports and certifications provided by a number of executives. Based on, and as of the date of that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective to provide reasonable assurances that information required to be disclosed in the reports we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

In designing and evaluating the disclosure controls and procedures, our management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable, not absolute, assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based upon the above evaluation, we believe that our controls provide such reasonable assurances.

On May 18, 2016, we completed the Transactions and as a result, we have incorporated internal controls over significant processes specific to the Transactions and to activities post-Transactions that we believe to be appropriate and necessary in consideration of the related integration, including controls associated with the Transactions for the valuations of certain Legacy TWC and Legacy Bright House assets and liabilities assumed, as well as adoption of common financial reporting and internal control practices for



the combined company. In October 2016, Legacy TWC was converted to the Legacy Charter's enterprise resource planning system which resulted in significant changes to the nature and type of internal controls for the most recent fiscal quarter. As we further integrate Legacy TWC and Legacy Bright House, we will continue to validate the effectiveness and integration of internal controls.

Except as described above in the preceding paragraph, during the quarter ended December 31, 2016, there was no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

#### **Management's Report on Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) for the Company. Our internal control system was designed to provide reasonable assurance to our management and board of directors regarding the preparation and fair presentation of published financial statements.

Management has assessed the effectiveness of our internal control over financial reporting as of December 31, 2016. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in *Internal Control — Integrated Framework* (2013). As permitted by guidance issued by the SEC, we have excluded from the scope of our assessment of internal control over financial reporting the operations and related assets of Legacy Bright House. As of December 31, 2016 and for the period from acquisition through December 31, 2016, both total assets and revenues subject to Bright House's internal control over financial reporting represented 9% of our consolidated total assets (including goodwill, intangibles and property, plant and equipment acquired in the Bright House Transaction and included within the scope of the assessment) and total revenues as of and for the year ended December 31, 2016. Based on management's assessment utilizing these criteria we believe that, as of December 31, 2016, our internal control over financial reporting was effective.

Our independent auditors, KPMG LLP, have audited our internal control over financial reporting as stated in their report on page F-2.

#### **Item 9B. Other Information.**

None.

**PART III****Item 10. *Directors, Executive Officers and Corporate Governance.***

The information required by Item 10 will be included in Charter's 2016 Proxy Statement (the "Proxy Statement") under the headings "Election of Class A Directors," "Section 16(a) Beneficial Ownership Reporting Requirements," and "Code of Ethics," or in amendment to this Annual Report on Form 10-K and is incorporated herein by reference.

**Item 11. *Executive Compensation.***

The information required by Item 11 will be included in the Proxy Statement under the headings "Executive Compensation," "Election of Class A Directors – Director Compensation" and "Compensation Discussion and Analysis," or in an amendment to this Annual Report on Form 10-K and is incorporated herein by reference. Information contained in the Proxy Statement or an amendment to this Annual Report on Form 10-K under the caption "Report of Compensation and Benefits Committee" is furnished and not deemed filed with the SEC.

**Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.***

The information required by Item 12 will be included in the Proxy Statement under the heading "Security Ownership of Certain Beneficial Owners and Management" or in amendment to this Annual Report on Form 10-K and is incorporated herein by reference.

**Item 13. *Certain Relationships and Related Transactions, and Director Independence.***

The information required by Item 13 will be included in the Proxy Statement under the heading "Certain Relationships and Related Transactions" and "Election of Class A Directors" or in amendment to this Annual Report on Form 10-K and is incorporated herein by reference.

**Item 14. *Principal Accounting Fees and Services.***

The information required by Item 14 will be included in the Proxy Statement under the heading "Accounting Matters" or in amendment to this Annual Report on Form 10-K and is incorporated herein by reference.

**PART IV****Item 15. Exhibits and Financial Statement Schedules.**

(a) The following documents are filed as part of this annual report:

(1) Financial Statements.

A listing of the financial statements, notes and reports of independent public accountants required by Item 8 begins on page F-1 of this annual report.

(2) Financial Statement Schedules.

No financial statement schedules are required to be filed by Items 8 and 15(c) because they are not required or are not applicable, or the required information is set forth in the applicable financial statements or notes thereto.

(3) The index to the exhibits begins on page E-1 of this annual report.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, Charter Communications, Inc. has duly caused this annual report to be signed on its behalf by the undersigned, thereunto duly authorized.

CHARTER COMMUNICATIONS, INC.,  
Registrant

By: /s/ Thomas M. Rutledge  
Thomas M. Rutledge  
Chairman and Chief Executive Officer

Date: February 16, 2017

S- 1

**POWER OF ATTORNEY**

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Richard R. Dykhouse and Kevin D. Howard, and each of them (with full power to each of them to act alone), his or her true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign on his or her behalf individually and in each capacity stated below any and all amendments (including post-effective amendments) to this annual report, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents and either of them, or their substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of Charter Communications, Inc. and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ Thomas M. Rutledge</u> Thomas M. Rutledge	Chairman, Chief Executive Officer, Director (Principal Executive Officer)	February 16, 2017
<u>/s/ Christopher L. Winfrey</u> Christopher L. Winfrey	Executive Vice President and Chief Financial Officer (Principal Financial Officer)	February 16, 2017
<u>/s/ Kevin D. Howard</u> Kevin D. Howard	Senior Vice President – Finance, Controller and Chief Accounting Officer (Principal Accounting Officer)	February 16, 2017
<u>/s/ Eric L. Zinterhofer</u> Eric L. Zinterhofer	Director	February 16, 2017
<u>/s/ W. Lance Conn</u> W. Lance Conn	Director	February 16, 2017
<u>/s/ Kim C. Goodman</u> Kim C. Goodman	Director	February 16, 2017
<u>/s/ Mauricio Ramos</u> Mauricio Ramos	Director	February 16, 2017
<u>/s/ Craig A. Jacobson</u> Craig A. Jacobson	Director	February 16, 2017
<u>/s/ Gregory Maffei</u> Gregory Maffei	Director	February 16, 2017
<u>/s/ John C. Malone</u> John C. Malone	Director	February 16, 2017
<u>/s/ John D. Markley, Jr.</u> John D. Markley, Jr.	Director	February 16, 2017
<u>/s/ David C. Merritt</u> David C. Merritt	Director	February 16, 2017
<u>/s/ Balan Nair</u> Balan Nair	Director	February 16, 2017

/s/ Michael Newhouse  
Michael Newhouse

Director

February 16, 2017

/s/ Steven Miron  
Steven Miron

Director

February 16, 2017

S- 2

### Exhibit Index

Exhibits are listed by numbers corresponding to the Exhibit Table of Item 601 in Regulation S-K.

Exhibit	Description
2.1	Agreement and Plan of Mergers, dated as of May 23, 2015, among Time Warner Cable Inc., Charter Communications, Inc., CCH I, LLC, Nina Corporation I, Inc., Nina Company II, LLC and Nina Company III, LLC (incorporated by reference to Exhibit 2.1 to the current report on Form 8-K filed by Charter Communications, Inc. on May 29, 2015 (File No. 001-33664)).
2.2	Contribution Agreement, dated March 31, 2015, by and among Advance/Newhouse Partnership, A/NPC Holdings LLC, Charter Communications, Inc., CCH I, LLC, and Charter Communications Holding Company, LLC (incorporated by reference to Exhibit 2.1 to the current report on Form 8-K filed by Charter Communications, Inc. on April 1, 2015 (File No. 001-33664)).
3.1	Amended and Restated Certificate of Incorporation of Charter Communications, Inc. (incorporated by reference to Exhibit 3.1 to the current report on Form 8-K of Charter Communications, Inc. filed on May 19, 2016 (File No. 001-33664)).
3.2	By-laws of Charter Communications, Inc. as of May 18, 2016 (incorporated by reference to Exhibit 3.2 to the current report on Form 8-K of Charter Communications, Inc. filed on May 19, 2016 (File No. 001-33664)).
4.1(a)	Amended and Restated Stockholders Agreement, dated March 31, 2015, by and among Charter Communications, Inc., Liberty Broadband Corporation and Advance/Newhouse Partnership (incorporated by reference to Exhibit 4.1 to the current report on Form 8-K filed by Charter Communications, Inc. on April 1, 2015 (File No. 001-33664)).
4.1(b)	Second Amended and Restated Stockholders Agreement, dated May 23, 2015, by and among Charter Communications, Inc., CCH I, LLC, Liberty Broadband Corporation and Advance/Newhouse Partnership (incorporated by reference to Exhibit 10.1 to the registration statement on Form S-4 filed by CCH I, LLC on June 26, 2015 (File No. 333-205240)).
10.1	Indenture dated as of May 10, 2011, by and among CCO Holdings, LLC, and CCO Holdings Capital Corp., as Issuers, Charter Communications, Inc., as Parent Guarantor, and The Bank of New York Mellon Trust Company, N.A., as Trustee (incorporated by reference to Exhibit 4.1 to the current report on Form 8-K of Charter Communications, Inc. filed on May 13, 2011 (File No. 001-33664)).
10.2	Third Supplemental Indenture dated as of January 26, 2012 by and among CCO Holdings, LLC, and CCO Holdings Capital Corp., as Issuers, Charter Communications, Inc., as Parent Guarantor, and The Bank of New York Mellon Trust Company, N.A., as Trustee (incorporated by reference to Exhibit 4.2 to the current report on Form 8-K of Charter Communications, Inc. filed on February 1, 2012 (File No. 001-33664)).
10.3	Fourth Supplemental Indenture dated August 22, 2012 relating to the 5.25% Senior Notes due 2022 by and among CCO Holdings, LLC, CCO Holdings Capital Corp. and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 10.1 to the quarterly report on Form 10-Q of Charter Communications, Inc. filed on November 6, 2012 (File No. 001-33664)).
10.4	Fifth Supplemental Indenture dated December 17, 2012 relating to the 5.125% Senior Notes due 2023 by and among CCO Holdings, LLC, CCO Holdings Capital Corp. and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 10.9 to the annual report on Form 10-K of Charter Communications, Inc. filed February 22, 2013 (File No. 001-33664)).
10.5	Sixth Supplemental Indenture relating to the 5.25% senior notes due 2021, dated as of March 14, 2013, by and among CCO Holdings, LLC, and CCO Holdings Capital Corp., as Issuers, Charter Communications, Inc., as Parent Guarantor, and The Bank of New York Mellon Trust Company, N.A., as Trustee (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K of Charter Communications, Inc. filed March 15, 2013 (File No. 001-33664)).
10.6	Seventh Supplemental Indenture relating to the 5.75% senior notes due 2023, dated as of March 14, 2013, by and among CCO Holdings, LLC, and CCO Holdings Capital Corp., as Issuers, Charter Communications, Inc., as Parent Guarantor, and The Bank of New York Mellon Trust Company, N.A., as Trustee (incorporated by reference to Exhibit 10.2 to the current report on Form 8-K of Charter Communications, Inc. filed March 15, 2013 (File No. 001-33664)).
10.7	Eighth Supplemental Indenture relating to the 5.75% senior notes due 2024, dated as of May 3, 2013, by and among CCO Holdings, LLC and CCO Holdings Capital Corp., as Issuers, Charter Communications, Inc., as Parent Guarantor, and The Bank of New York Mellon Trust Company, N.A., as Trustee (incorporated by reference to Exhibit 10.7 to the quarterly report on Form 10-Q of Charter Communications, Inc. filed on May 7, 2013 (File No. 001-33664)).
10.8	Indenture dated as of November 5, 2014, by and among CCO Holdings, LLC, CCO Holdings Capital Corp. and CCOH Safari, LLC, as Issuers, Charter Communications, Inc., as Parent Guarantor, and The Bank of New York Mellon Trust

Company, N.A., as Trustee (incorporated by reference to Exhibit 4.1 to the current report on Form 8-K of Charter Communications, Inc. filed on November 10, 2014 (File No. 001-33664)).

E- 1

---

- 10.9 Third Supplemental Indenture, dated as of April 21, 2015, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.1 to the current report on Form 8-K filed by Charter Communications, Inc. on April 22, 2015 (File No. 001-33664)).
- 10.10 Fourth Supplemental Indenture, dated as of April 21, 2015, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.2 to the current report on Form 8-K filed by Charter Communications, Inc. on April 22, 2015 (File No. 001-33664)).
- 10.11 Fifth Supplemental Indenture, dated as of April 21, 2015, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.3 to the current report on Form 8-K filed by Charter Communications, Inc. on April 22, 2015 (File No. 001-33664)).
- 10.12 Exchange and Registration Rights Agreement, dated as of April 21, 2015 relating to the 5.125% Senior Notes due 2023, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and Credit Suisse Securities (USA) LLC, Deutsche Bank Securities Inc., Goldman, Sachs & Co. and Merrill Lynch, Pierce, Fenner & Smith Incorporated, as representatives of the several Purchasers (as defined therein) (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K filed by Charter Communications, Inc. on April 22, 2015 (File No. 001-33664)).
- 10.13 Exchange and Registration Rights Agreement relating to the 5.375% Senior Notes due 2025, dated as of April 21, 2015, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and Credit Suisse Securities (USA) LLC, Deutsche Bank Securities Inc., Goldman, Sachs & Co. and Merrill Lynch, Pierce, Fenner & Smith Incorporated, as representatives of the several Purchasers (as defined therein) (incorporated by reference to Exhibit 10.2 to the current report on Form 8-K filed by Charter Communications, Inc. on April 22, 2015 (File No. 001-33664)).
- 10.14 Exchange and Registration Rights Agreement relating to the 5.875% Senior Notes due 2027, dated as of April 21, 2015, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and Credit Suisse Securities (USA) LLC, Deutsche Bank Securities Inc., Goldman, Sachs & Co. and Merrill Lynch, Pierce, Fenner & Smith Incorporated, as representatives of the several Purchasers (as defined therein) (incorporated by reference to Exhibit 10.3 to the current report on Form 8-K filed by Charter Communications, Inc. on April 22, 2015 (File No. 001-33664)).
- 10.15 Indenture, dated as of July 23, 2015, among Charter Communications Operating, LLC, Charter Communications Operating Capital Corp. and CCO Safari II, LLC, as issuers, and The Bank of New York Mellon Trust Company, N.A., as trustee and collateral agent (incorporated by reference to Exhibit 4.1 to the current report on Form 8-K filed by Charter Communications, Inc. on July 27, 2015 (File No. 001-33664)).
- 10.16 First Supplemental Indenture, dated as of July 23, 2015, among CCO Safari II, LLC, as escrow issuer, CCH II, LLC, as limited guarantor, and The Bank of New York Mellon Trust Company, N.A., as trustee and collateral agent (incorporated by reference to Exhibit 4.2 to the current report on Form 8-K filed by Charter Communications, Inc. on July 27, 2015 (File No. 001-33664)).
- 10.17 Exchange and Registration Rights Agreement, dated July 23, 2015 relating to the 3.579% Senior Secured Notes due 2020, 4.464% Senior Secured Notes due 2022, 4.908% Senior Secured Notes due 2025, 6.384% Senior Secured Notes due 2035, 6.484% Senior Secured Notes due 2045 and 6.834% Senior Secured Notes due 2055, between CCO Safari II, LLC and Goldman, Sachs & Co., Credit Suisse Securities (USA) LLC, Merrill Lynch, Pierce, Fenner & Smith Incorporated, Deutsche Bank Securities Inc. and UBS Securities LLC, as representatives of the several Purchasers (as defined therein) (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K filed by Charter Communications, Inc. on July 27, 2015 (File No. 001-33664)).
- 10.18 Indenture, dated as of November 20, 2015, among CCO Holdings, LLC, CCO Holdings Capital Corp. and CCOH Safari, LLC, as issuers, and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.1 to the current report on Form 8-K filed by Charter Communications, Inc. on November 25, 2015 (File No. 001-33664)).
- 10.19 First Supplemental Indenture, dated as of November 20, 2015, between CCOH Safari, LLC, as escrow issuer, and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.2 to the current report on Form 8-K filed by Charter Communications, Inc. on November 25, 2015 (File No. 001-33664)).
- 10.20 Exchange and Registration Rights Agreement, dated November 20, 2015 relating to the 5.750% Senior Notes due 2026, between CCOH Safari, LLC and Credit Suisse Securities (USA) LLC, Goldman, Sachs & Co., Merrill Lynch, Pierce, Fenner & Smith Incorporated, UBS Securities LLC and Deutsche Bank Securities Inc., as representatives of the

several Purchasers (as defined therein) (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K filed by Charter Communications, Inc. on November 25, 2015 (File No. 001-33664)).

10.21

Sixth Supplemental Indenture, dated as of February 19, 2016, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.1 to the current report on Form 8-K filed by Charter Communications, Inc. on February 22, 2016 (File No. 001-33664)).

E- 2

- 10.22 Exchange and Registration Rights Agreement, dated February 19, 2016, relating to the 5.875% Senior Notes due 2024, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and Deutsche Bank Securities Inc., Credit Suisse Securities (USA) LLC, Goldman, Sachs & Co., Merrill Lynch, Pierce, Fenner & Smith Incorporated, UBS Securities LLC, Citigroup Global Markets Inc. and Wells Fargo Securities, LLC, as representatives of the several Purchasers (as defined therein) (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K filed by Charter Communications, Inc. on February 22, 2016 (File No. 001-33664)).
- 10.23 Seventh Supplemental Indenture, dated as of April 21, 2016, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.1 to the current report on Form 8-K filed by Charter Communications, Inc. on April 27, 2016 (File No. 001-33664)).
- 10.24 Exchange and Registration Rights Agreement, dated April 21, 2016, relating to the 5.500% Senior Notes due 2026, among CCO Holdings, LLC, CCO Holdings Capital Corp., Charter Communications, Inc., as guarantor, and Merrill Lynch, Pierce, Fenner & Smith Incorporated, Citigroup Global Markets Inc., Credit Suisse Securities (USA) LLC, Deutsche Bank Securities Inc., Goldman, Sachs & Co., UBS Securities LLC and Wells Fargo Securities, LLC, as representatives of the several Purchasers (as defined therein) (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K filed by Charter Communications, Inc. on April 27, 2016 (File No. 001-33664)).
- 10.25 Second Supplemental Indenture, dated as of May 18, 2016, by and among Charter Communications Operating, LLC, Charter Communications Operating Capital Corp., CCO Safari II, LLC and The Bank of New York Mellon Trust Company, N.A., as trustee and collateral agent (incorporated by reference to Exhibit 4.1 to the current report on Form 8-K filed by Charter Communications, Inc. on May 24, 2016 (File No. 001-33664)).
- 10.26 Third Supplemental Indenture, dated as of May 18, 2016, by and among CCO Holdings, LLC, the subsidiary guarantors party thereto and The Bank of New York Mellon Trust Company, N.A., as trustee and collateral agent (incorporated by reference to Exhibit 4.2 to the current report on Form 8-K filed by Charter Communications, Inc. on May 24, 2016 (File No. 001-33664)).
- 10.27 Second Supplemental Indenture, dated as of May 18, 2016, by and among CCO Holdings, LLC, CCO Holdings Capital Corp., CCOH Safari, LLC and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.3 to the current report on Form 8-K filed by Charter Communications, Inc. on May 24, 2016 (File No. 001-33664)).
- 10.28 Indenture, dated as of April 30, 1992 (the "TWCE Indenture"), as amended by the First Supplemental Indenture, dated as of June 30, 1992, among Time Warner Entertainment Company, L.P. ("TWE"), Time Warner Companies, Inc. ("TWCI"), certain of TWCI's subsidiaries that are parties thereto and The Bank of New York, as Trustee (incorporated herein by reference to Exhibits 10(g) and 10(h) to TWCI's current report on Form 8-K dated June 26, 1992 and filed with the SEC on July 15, 1992 (File No. 1-8637)).
- 10.29 Second Supplemental Indenture to the TWCE Indenture, dated as of December 9, 1992, among TWE, TWCI, certain of TWCI's subsidiaries that are parties thereto and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 4.2 to Amendment No. 1 to TWE's Registration Statement on Form S-4 dated and filed with the SEC on October 25, 1993 (Registration No. 33-67688) (the "TWE October 25, 1993 Registration Statement")).
- 10.30 Third Supplemental Indenture to the TWCE Indenture, dated as of October 12, 1993, among TWE, TWCI, certain of TWCI's subsidiaries that are parties thereto and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 4.3 to the TWE October 25, 1993 Registration Statement).
- 10.31 Fourth Supplemental Indenture to the TWCE Indenture, dated as of March 29, 1994, among TWE, TWCI, certain of TWCI's subsidiaries that are parties thereto and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 4.4 to TWE's Annual Report on Form 10-K for the year ended December 31, 1993 and filed with the SEC on March 30, 1994 (File No. 1-12878)).
- 10.32 Fifth Supplemental Indenture to the TWCE Indenture, dated as of December 28, 1994, among TWE, TWCI, certain of TWCI's subsidiaries that are parties thereto and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 4.5 to TWE's Annual Report on Form 10-K for the year ended December 31, 1994 and filed with the SEC on March 30, 1995 (File No. 1-12878)).
- 10.33 Sixth Supplemental Indenture to the TWCE Indenture, dated as of September 29, 1997, among TWE, TWCI, certain of TWCI's subsidiaries that are parties thereto and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 4.7 to Historic TW Inc.'s ("Historic TW") Annual Report on Form 10-K for the year ended December 31, 1997 and filed with the SEC on March 25, 1998 (File No. 1-12259) (the "Time Warner 1997 Form 10-K")).
- 10.34 Seventh Supplemental Indenture to the TWCE Indenture, dated as of December 29, 1997, among TWE, TWCI, certain of TWCI's subsidiaries that are parties thereto and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 4.8 to the Time Warner 1997 Form 10-K).

10.35

Eighth Supplemental Indenture to the TWCE Indenture, dated as of December 9, 2003, among Historic TW, TWE, Warner Communications Inc. ("WCI"), American Television and Communications Corporation ("ATC"), TWC and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 4.10 to Time Warner Inc.'s ("Time Warner") Annual Report on Form 10-K for the year ended December 31, 2003 (File No. 1-15062)).

E- 3

- 10.36 Ninth Supplemental Indenture to the TWCE Indenture, dated as of November 1, 2004, among Historic TW, TWE, Time Warner NY Cable Inc., WCI, ATC, TWC and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 4.1 to Time Warner's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (File No. 1-15062)).
- 10.37 Tenth Supplemental Indenture to the TWCE Indenture, dated as of October 18, 2006, among Historic TW, TWE, TW NY Cable Holding Inc. ("TW NY"), Time Warner NY Cable LLC ("TW NY Cable"), TWC, WCI, ATC and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 4.1 to Time Warner's current report on Form 8-K dated and filed October 18, 2006 (File No. 1-15062)).
- 10.38 Eleventh Supplemental Indenture to the TWCE Indenture, dated as of November 2, 2006, among TWE, TW NY, TWC and The Bank of New York, as Trustee (incorporated herein by reference to Exhibit 99.1 to Time Warner's current report on Form 8-K dated and filed November 2, 2006 (File No. 1-15062)).
- 10.40 Twelfth Supplemental Indenture to the TWCE Indenture, dated as of September 30, 2012, among Time Warner Cable Enterprises LLC ("TWCE"), TWC, TW NY, Time Warner Cable Internet Holdings II LLC ("TWC Internet Holdings II") and The Bank of New York Mellon, as trustee, supplementing the Indenture dated April 30, 1992, as amended (incorporated herein by reference to Exhibit 4.2 to TWC's current report on Form 8-K dated September 30, 2012 and filed with the SEC on October 1, 2012 (File No. 1-33335) (the "TWC September 30, 2012 Form 8-K")).
- 10.41 Thirteenth Supplemental Indenture, dated as of May 18, 2016, by and among Time Warner Cable Enterprises LLC, the guarantors party thereto and The Bank of New York Mellon (formerly known as The Bank of New York), as trustee (incorporated by reference to Exhibit 4.4 to the current report on Form 8-K filed by Charter Communications, Inc. on May 24, 2016 (File No. 001-33664)).
- 10.42 Indenture, dated as of April 9, 2007 (the "TWC Indenture"), among TWC, TW NY, TWE and The Bank of New York, as trustee (incorporated herein by reference to Exhibit 4.1 to TWC's current report on Form 8-K dated April 4, 2007 and filed with the SEC on April 9, 2007 (File No. 1-33335) (the "TWC April 4, 2007 Form 8-K")).
- 10.43 First Supplemental Indenture to the TWC Indenture, dated as of April 9, 2007, among TWC, TW NY, TWE and The Bank of New York, as trustee (incorporated herein by reference to Exhibit 4.2 to the TWC April 4, 2007 Form 8-K).
- 10.44 Second Supplemental Indenture to the TWC Indenture, dated as of September 30, 2012, among TWC, TW NY, TWCE, TWC Internet Holdings II and The Bank of New York Mellon, as trustee, supplementing the Indenture dated April 9, 2007, as amended (incorporated herein by reference to Exhibit 4.1 to the TWC September 30, 2012 Form 8-K).
- 10.45 Third Supplemental Indenture, dated as of May 18, 2016, by and among Time Warner Cable Inc., TWC NewCo LLC and The Bank of New York Mellon (formerly known as The Bank of New York), as trustee (incorporated by reference to Exhibit 4.5 to the current report on Form 8-K filed by Charter Communications, Inc. on May 24, 2016 (File No. 001-33664)).
- 10.46 Fourth Supplemental Indenture, dated as of May 18, 2016, by and among TWC NewCo LLC, the guarantors party thereto and The Bank of New York Mellon (formerly known as The Bank of New York), as trustee (incorporated by reference to Exhibit 4.6 to the current report on Form 8-K filed by Charter Communications, Inc. on May 24, 2016 (File No. 001-33664)).
- 10.47 Form of TWC 5.85% Exchange Notes due 2017 (included as Exhibit B to the First Supplemental Indenture incorporated herein by reference to Exhibit 4.2 to the TWC April 4, 2007 Form 8-K).
- 10.48 Form of TWC 6.55% Exchange Debentures due 2037 (included as Exhibit C to the First Supplemental Indenture incorporated herein by reference to Exhibit 4.2 to the TWC April 4, 2007 Form 8-K).
- 10.49 Form of TWC 6.75% Notes due 2018 (incorporated herein by reference to Exhibit 4.2 to TWC's current report on Form 8-K dated June 16, 2008 and filed with the SEC on June 19, 2008 (File No. 1-33335) (the "TWC June 16, 2008 Form 8-K")).
- 10.50 Form of TWC 7.30% Debentures due 2038 (incorporated herein by reference to Exhibit 4.3 to the TWC June 16, 2008 Form 8-K).
- 10.51 Form of TWC 8.75% Notes due 2019 (incorporated herein by reference to Exhibit 4.2 to TWC's current report on Form 8-K dated November 13, 2008 and filed with the SEC on November 18, 2008) (File No. 1-33335).
- 10.52 Form of TWC 8.25% Notes due 2019 (incorporated herein by reference to Exhibit 4.2 to TWC's current report on Form 8-K dated March 23, 2009 and filed with the SEC on March 26, 2009 (File No. 1-33335)).
- 10.53 Form of TWC 6.75% Debentures due 2039 (incorporated herein by reference to Exhibit 4.1 to TWC's current report on Form 8-K dated June 24, 2009 and filed with the SEC on June 29, 2009 (File No. 1-33335)).
- 10.54 Form of TWC 3.5% Notes due 2015 (incorporated herein by reference to Exhibit 4.1 to TWC's current report on Form 8-K dated December 8, 2009 and filed with the SEC on December 11, 2009 (File No. 1-33335) (the "TWC December 8, 2009 Form 8-K")).



- 10.56 Form of TWC 4.125% Notes due 2021 (incorporated herein by reference to Exhibit 4.1 to TWC's current report on Form 8-K dated November 9, 2010 and filed with the SEC on November 15, 2010 (File No. 1-33335) (the "TWC November 9, 2010 Form 8-K").
- 10.57 Form of TWC 5.875% Debentures due 2040 (incorporated herein by reference to Exhibit 4.2 to the TWC November 9, 2010 Form 8-K).
- 10.58 Form of TWC 5.75% Note due 2031 (incorporated herein by reference to Exhibit 4.1 to TWC's current report on Form 8-K dated and filed with the SEC on May 26, 2011 (File No. 1-33335)).
- 10.59 Form of TWC 4% Note due 2021 (incorporated herein by reference to Exhibit 4.1 to TWC's current report on Form 8-K dated September 7, 2011 and filed with the SEC on September 12, 2011 (File No. 1-33335) (the "TWC September 7, 2011 Form 8-K").
- 10.60 Form of TWC 5.5% Debenture due 2041 (incorporated herein by reference to Exhibit 4.2 to the TWC September 7, 2011 Form 8-K).
- 10.61 Form of TWC 4.5% Debenture due 2042 (incorporated herein by reference to Exhibit 4.1 to TWC's current report on Form 8-K dated August 7, 2012 and filed with the SEC on August 10, 2012 (File No. 1-33335)).
- 10.62 Form of TWC 5.25% Note due 2042 (incorporated herein by reference to Exhibit 4.1 to TWC's current report on Form 8-K dated and filed with the SEC on June 27, 2012 (File No. 1-33335)).
- 10.63 Form of 5.500% Senior Notes due 2026 (incorporated herein by reference to Exhibit 10.1 to the current report on Form 8-K of Charter Communications, Inc. filed April 27, 2016).
- 10.64 Amendment No. 5, dated as of August 24, 2015, to the Amended and Restated Credit Agreement dated as of April 11, 2012 between Charter Communications Operating, LLC, as borrower, CCO Holdings, LLC, as guarantor, and Bank of America, N.A., as administrative agent (incorporated by reference to Exhibit 10.2 to the current report on Form 8-K of Charter Communications, Inc. filed on August 28, 2015 (File No. 001-33664)).
- 10.65 Incremental Activation Notice, dated as of August 24, 2015 delivered by Charter Communications Operating, LLC, CCO Holdings, LLC, the subsidiary guarantors party thereto, each Term H Lender party thereto to, each Term I Lender party thereto and Bank of America, N.A., as Administrative Agent under the Amended and Restated Credit Agreement, dated as of April 11, 2012 (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K of Charter Communications, Inc. filed on August 28, 2015 (File No. 001-33664)).
- 10.66 Escrow Credit Agreement, dated as of August 24, 2015, between CCO Safari III, LLC, as borrower, and Bank of America, N.A., as administrative agent, and the lenders party thereto (incorporated by reference to Exhibit 10.3 to the current report on Form 8-K of Charter Communications, Inc. filed on August 28, 2015 (File No. 001-33664)).
- 10.67(a) Restatement Agreement dated as of May 18, 2016, by and among Charter Communications Operating, LLC, CCO Holdings, LLC, the subsidiary guarantors party thereto, Bank of America, N.A., as administrative agent and the lenders party thereto (incorporated by reference to Exhibit 10.5 to the current report on Form 8-K of Charter Communications, Inc. filed on May 24, 2016 (File No. 001-33664)).
- 10.67(b) Amendment No. 1 dated as of December 23, 2016, to the Amended and Restated Credit Agreement dated as of March 18, 1999, as amended and restated on May 18, 2016, by and among Charter Communications Operating, LLC, CCO Holdings, LLC, the Lenders Party thereto and Bank of America, N.A., as Administrative Agent (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K of Charter Communications, Inc. filed on December 30, 2016 (File No. 001-33664)).
- 10.67(c) Incremental Activation Notice, dated as of May 18, 2016, by and among Charter Communications Operating, LLC, CCO Holdings, LLC, the subsidiary guarantors party thereto, Bank of America, N.A., as administrative agent and the lenders party thereto (incorporated by reference to Exhibit 10.4 to the current report on Form 8-K of Charter Communications, Inc. filed on May 24, 2016 (File No. 001-33664)).
- 10.68 Amended and Restated Guarantee and Collateral Agreement made by CCO Holdings, LLC, Charter Communications Operating, LLC and certain of its subsidiaries in favor of Bank of America, N.A., as administrative agent, as amended and restated as of March 31, 2010 (incorporated by reference to Exhibit 10.2 to the current report on Form 8-K of Charter Communications, Inc. filed on April 6, 2010 (File No. 001-33664)).
- 10.69 Collateral Agreement, dated as of May 18, 2016, by Charter Communications Operating, LLC, Charter Communications Operating Capital Corp. and the other grantors party thereto in favor of The Bank of New York Mellon Trust Company, N.A., as collateral agent (incorporated by reference to Exhibit 10.6 to the current report on Form 8-K of Charter Communications, Inc. filed on May 24, 2016 (File No. 001-33664)).
- 10.70 First Lien Intercreditor Agreement, dated as of May 18, 2016, by and among Charter Communications Operating, LLC, the other grantors party thereto, Bank of America, N.A., as credit agreement collateral agent for the credit agreement secured parties, The Bank of New York Mellon Trust Company, N.A., as notes collateral agent for the indenture

secured parties, and each additional agent from time to time party thereto (incorporated by reference to Exhibit 10.7 to the current report on Form 8-K of Charter Communications, Inc. filed on May 24, 2016 (File No. 001-33664)).

- 10.71 Joinder Agreement to Registration Rights Agreement, dated as of May 18, 2016, by and among CCO Safari II, LLC, CCH II, LLC, Charter Communications Operating, LLC, Charter Communications Operating Capital Corp., CCO Holdings, LLC and the other guarantors party thereto (incorporated herein by reference to Exhibit 10.1 to the current report on Form 8-K of Charter Communications, Inc. filed May 24, 2016).
- 10.72 Joinder Agreement to Registration Rights Agreement, dated as of May 18, 2016, by CCO Holdings, LLC and CCO Holdings Capital Corp (incorporated herein by reference to Exhibit 10.2 to the current report on Form 8-K of Charter Communications, Inc. filed May 24, 2016).
- 10.73 Escrow Assumption Agreement, dated as of May 18, 2016, by and among CCO Safari III, LLC, Charter Communications Operating, LLC, Bank of America, N.A., as escrow administrative agent and Bank of America, N.A., as administrative agent (incorporated herein by reference to Exhibit 10.3 to the current report on Form 8-K of Charter Communications, Inc. filed May 24, 2016).
- 10.74 Amended and Restated Limited Liability Company Agreement of Charter Communications Holdings, LLC, dated as of May 18, 2016, by and among Charter Holdings, Charter, CCH II, LLC, Advance/Newhouse Partnership and the other party or parties thereto (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K of Charter Communications, Inc. filed on May 19, 2016 (File No. 001-33664)).
- 10.75 Exchange Agreement, dated as of May 18, 2016, by and among Charter Holdings, Charter, Advance/Newhouse Partnership and the other party or parties thereto (incorporated by reference to Exhibit 10.2 to the current report on Form 8-K of Charter Communications, Inc. filed on May 19, 2016 (File No. 001-33664)).
- 10.76 Registration Rights Agreement, dated as of May 18, 2016, by and among Charter, Advance/Newhouse Partnership and Liberty Broadband (incorporated by reference to Exhibit 10.3 to the current report on Form 8-K of Charter Communications, Inc. filed on May 19, 2016 (File No. 001-33664)).
- 10.77 Tax Receivables Agreement, dated as of May 18, 2016, by and among Charter, Advance/Newhouse Partnership and the other party or parties thereto (incorporated by reference to Exhibit 10.4 to the current report on Form 8-K of Charter Communications, Inc. filed on May 19, 2016 (File No. 001-33664)).
- 10.78+ Charter Communications, Inc. Executive Bonus Plan (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q of Charter Communications, Inc. filed on May 8, 2012 (File No. 001-33664)).
- 10.79+ Charter Communications, Inc. 2016 Executive Incentive Performance Plan (incorporated by reference to Appendix A to the proxy statement for the Charter Communications, Inc. 2016 Annual Meeting of Stockholders filed March 17, 2016 (File No. 001-33664)).
- 10.80+ Charter Communications, Inc. Amended and Restated 2009 Stock Incentive Plan (incorporated by reference to Exhibit 10.6 to the Current Report on Form 8-K of Charter Communications, Inc. filed on May 19, 2016 (File No. 001-33664)).
- 10.81+ Amendment to the Charter Communications, Inc. Amended and Restated 2009 Stock Incentive Plan, dated as of October 25, 2016 (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K of Charter Communications, Inc. filed on October 28, 2016 (File No. 001-33664)).
- 10.82+ Charter Communications, Inc.'s Amended and Restated Supplemental Deferred Compensation Plan, dated as of September 1, 2011(incorporated by reference to Exhibit 10.1 to the current report on Form 8-K filed by Charter Communications, Inc. on September 2, 2011 (File No. 001-33664)).
- 10.83+ Form of Non-Qualified Time Vesting Stock Option Agreement dated April 26, 2011(incorporated by reference to Exhibit 10.3 to the quarterly report on Form 10-Q filed by Charter Communications, Inc. on August 2, 2011 (File No. 001-33664)).
- 10.84+ Form of Non-Qualified Price Vesting Stock Option Agreement dated April 26, 2011(incorporated by reference to Exhibit 10.2 to the quarterly report on Form 10-Q filed by Charter Communications, Inc. on August 2, 2011 (File No. 001-33664)).
- 10.85+ Form of Notice of LTIP Award Agreement Changes (RSU Awards) (incorporated by reference to Exhibit 10.3 to the current report on Form 8-K filed by Charter Communications, inc. on January 22, 2014 (File No. 001-33664)).
- 10.86+ Form of Notice of LTIP Award Agreement Changes (Time-Vesting Option Awards) (incorporated by reference to Exhibit 10.4 to the current report on Form 8-K filed by Charter Communications, Inc. on January 22, 2014 (File No. 001-33664)).
- 10.87+ Form of Notice of LTIP Award Agreement Changes (Restricted Stock Awards) (incorporated by reference to Exhibit 10.5 to the current report on Form 8-K filed by Charter Communications, inc. on January 22, 2014 (File No. 001-33664)).
- 10.88+ Form of Notice of LTIP Award Agreement Changes (Performance-Vesting Option Awards) (incorporated by reference to Exhibit 10.6 to the current report on Form 8-K filed by Charter Communications, Inc. on January 22, 2014 (File No.

001-33664)).

- 10.89+ Form of Stock Option Agreement dated January 15, 2014 (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K filed by Charter Communications, Inc. on January 22, 2014 (File No. 001-33664)).
- 10.90+ Form of Restricted Stock Unit Agreement dated January 15, 2014 (incorporated by reference to Exhibit 10.2 to the current report on Form 8-K filed by Charter Communications, Inc. on January 22, 2014 (File No. 001-33664)).

E- 6

- 10.91(a)+ Employment Agreement between Thomas Rutledge and Charter Communications, Inc., dated as of May 17, 2016 (incorporated by reference to Exhibit 10.5 to the current report on Form 8-K of Charter Communications, Inc. filed on May 19, 2016 (File No. 001-33664)).
- 10.91(b)+ Time-Vesting Stock Option Agreement dated as of December 19, 2011 by and between Charter Communications, Inc. and Thomas M. Rutledge (incorporated by reference to Exhibit 10.2 to the current report on Form 8-K filed by Charter Communications, Inc. on December 19, 2011 (File No. 001-33664)).
- 10.91(c)+ Performance-Vesting Stock Option Agreement dated as of December 19, 2011 by and between Charter Communications, Inc. and Thomas M. Rutledge (incorporated by reference to Exhibit 10.4 to the current report on Form 8-K filed by Charter Communications, Inc. on December 19, 2011 (File No. 001-33664)).
- 10.92(a)+ Employment Agreement dated effective as of November 2, 2016 by and between Charter Communications, Inc. and John Bickham (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q of Charter Communications, Inc. filed on November 3, 2016 (File No. 001-33664)).
- 10.92(b)+ Time-Vesting Stock Option Agreement dated as of April 30, 2012 by and between Charter Communications, Inc. and John Bickham (incorporated by reference to Exhibit 10.2 to the current report on Form 8-K filed by Charter Communications, Inc. on May 1, 2012 (File No. 001-33664)).
- 10.92(c)+ Performance-Vesting Stock Option Agreement dated as of April 30, 2012 by and between Charter Communications, Inc. and John Bickham (incorporated by reference to Exhibit 10.4 to the current report on Form 8-K filed by Charter Communications, Inc. on May 1, 2012 (File No. 001-33664)).
- 10.93+ Form of First Amended and Restated Indemnification Agreement (incorporated by reference to Exhibit 10.3 to the quarterly report on Form 10-Q of Charter Communications, Inc. filed on August 6, 2013 (File No. 001-33664)).
- 10.94+ Amendment to the Employment Agreement, dated as of February 11, 2016, by and between Charter Communications, Inc. and Thomas Rutledge (incorporated by reference to Exhibit 10.1 to the current report on Form 8-K filed by Charter Communications, Inc. on February 12, 2016 (File No. 001-33664)).
- 10.95+ Time Warner Cable Inc. 2006 Stock Incentive Plan (incorporated herein by reference to Exhibit 10.45 to TWC's current report on Form 8-K dated February 13, 2007 and filed with the SEC on February 13, 2007).
- 10.96+ Time Warner Cable Inc. 2006 Stock Incentive Plan, as amended, effective March 12, 2009 (incorporated herein by reference to Exhibit 10.1 to TWC's Quarterly Report on Form 10-Q for the quarter ended March 31, 2009).
- 10.97+ Time Warner Cable Inc. 2011 Stock Incentive Plan (incorporated herein by reference to Annex A to TWC's definitive Proxy Statement dated April 6, 2011 and filed with the SEC on April 6, 2011).
- 10.98+ Form of Amendment to Nonqualified Stock Option Agreements Granted Under the Charter Communications, Inc. Amended and Restated 2009 Stock Incentive Plan, dated as of October 25, 2016 (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K of Charter Communications, Inc. filed on October 28, 2016 (File No. 001-33664)).
- 10.99+ Employment Agreement dated effective as of November 2, 2016 by and between Charter Communications, Inc. and Christopher L. Winfrey (incorporated by reference to Exhibit 10.2 to the Quarterly Report on Form 10-Q of Charter Communications, Inc. filed on November 3, 2016 (File No. 001-33664)).
- 10.100+ Employment Agreement dated effective as of November 2, 2016 by and between Charter Communications, Inc. and Jonathan Hargis (incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q of Charter Communications, Inc. filed on November 3, 2016 (File No. 001-33664)).
- 10.101\*+ Employment Agreement dated as of November 10, 2016 by and between Charter Communications, Inc. and David Eilen.
- 10.102\*+ Form of Performance-Vesting Stock Option Agreement granted to certain executive officers in 2016 under the Charter Communications, Inc. Amended and Restated 2009 Stock Incentive Plan.
- 10.103\*+ Form of Performance-Vesting Restricted Stock Unit Agreement granted to certain executive officers in 2016 under the Charter Communications, Inc. Amended and Restated 2009 Stock Incentive Plan.
- 10.104 Letter Agreement, dated as of December 23, 2016, between Charter Communications, Inc. and Advance/Newhouse Partnership (incorporated by reference to Exhibit 99.1 to the Current Report on Form 8-K of Charter Communications, Inc. filed on December 28, 2016 (File No. 001-33664)).
- 12.1\* Computation of Ratio of Earnings to Fixed Charges.
- 21.1\* Subsidiaries of Charter Communications, Inc.
- 23.1\* Consent of KPMG LLP.
- 31.1\* Certificate of Chief Executive Officer pursuant to Rule 13a-14(a)/Rule 15d-14(a) under the Securities Exchange Act of 1934.

- 31.2\* Certificate of Chief Financial Officer pursuant to Rule 13a-14(a)/Rule 15d-14(a) under the Securities Exchange Act of 1934.
- 32.1\* Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer).

- 32.2\* Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Financial Officer).
- 101 The following financial information from the Annual Report of Charter Communications, Inc. on Form 10-K for the year ended December 31, 2016, filed with the SEC on February 16, 2017, formatted in eXtensible Business Reporting Language: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations, (iii) Consolidated Statements of Comprehensive Income (Loss), (iv) Consolidated Statements of Changes in Shareholders' Equity (Deficit), (v) Consolidated Statements of Cash Flows, and (vi) Notes to Consolidated Financial Statements.

\* Filed herewith.

+ Management compensatory plan or arrangement

## INDEX TO FINANCIAL STATEMENTS

	<b>Page</b>
Audited Financial Statements	
<u>Report of Independent Registered Public Accounting Firm</u>	<u>F- 2</u>
<u>Consolidated Balance Sheets as of December 31, 2016 and 2015</u>	<u>F- 4</u>
<u>Consolidated Statements of Operations for the Years Ended December 31, 2016, 2015 and 2014</u>	<u>F- 5</u>
<u>Consolidated Statements of Comprehensive Income (Loss) for the Years Ended December 31, 2016, 2015 and 2014</u>	<u>F- 6</u>
<u>Consolidated Statements of Changes in Shareholders' Equity (Deficit) for the Years Ended December 31, 2016, 2015 and 2014</u>	<u>F- 7</u>
<u>Consolidated Statements of Cash Flows for the Years Ended December 31, 2016, 2015 and 2014</u>	<u>F- 8</u>
<u>Notes to Consolidated Financial Statements</u>	<u>F- 9</u>

### Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders  
Charter Communications, Inc.:

We have audited the accompanying consolidated balance sheets of Charter Communications, Inc. and subsidiaries (the Company) as of December 31, 2016 and 2015, and the related consolidated statements of operations, comprehensive income (loss), changes in shareholders' equity (deficit), and cash flows for each of the years in the three-year period ended December 31, 2016. We also have audited the Company's internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting (Item 9A). Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Charter Communications, Inc. and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Charter Communications, Inc. acquired Bright House Networks, LLC (Legacy Bright House) during 2016. Management excluded from its assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2016, the operations and related assets of Legacy Bright House. As of December 31, 2016 and for the period from acquisition through December 31, 2016, both total assets and revenues subject to Legacy Bright House's internal control over financial reporting represented approximately 9% of the Company's consolidated total assets (including goodwill, intangible assets, and property, plant and equipment acquired from Legacy Bright House that are included within the scope of the assessment) and consolidated total revenues as of and for the year ended December 31, 2016. Our audit of internal control over financial reporting of Charter Communications, Inc. also excluded an evaluation of the internal control over financial reporting of Bright House Networks, LLC as of December 31, 2016.

(signed) KPMG LLP

St. Louis, Missouri  
February 15, 2017

F- 3

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(dollars in millions, except share data)

ASSETS	December 31,	
	2016	2015
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 1,535	\$ 5
Accounts receivable, less allowance for doubtful accounts of \$124 and \$21, respectively	1,432	279
Prepaid expenses and other current assets	333	61
Total current assets	3,300	345
<b>RESTRICTED CASH AND CASH EQUIVALENTS</b>	—	22,264
<b>INVESTMENT IN CABLE PROPERTIES:</b>		
Property, plant and equipment, net of accumulated depreciation of \$11,103 and \$6,518, respectively	32,963	8,345
Customer relationships, net	14,608	856
Franchises	67,316	6,006
Goodwill	29,509	1,168
Total investment in cable properties, net	144,396	16,375
<b>OTHER NONCURRENT ASSETS</b>	1,371	332
Total assets	\$ 149,067	\$ 39,316
<b>LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)</b>		
<b>CURRENT LIABILITIES:</b>		
Accounts payable and accrued liabilities	\$ 7,544	\$ 1,972
Current portion of long-term debt	2,028	—
Total current liabilities	9,572	1,972
<b>LONG-TERM DEBT</b>	59,719	35,723
<b>DEFERRED INCOME TAXES</b>	26,665	1,590
<b>OTHER LONG-TERM LIABILITIES</b>	2,745	77
<b>SHAREHOLDERS' EQUITY (DEFICIT):</b>		
Class A common stock; \$.001 par value; 900 million shares authorized; 268,897,792 and 112,438,828 shares issued and outstanding, respectively	—	—
Class B common stock; \$.001 par value; 1,000 and 25 million shares authorized, respectively; 1 and no shares issued and outstanding, respectively	—	—
Preferred stock; \$.001 par value; 250 million shares authorized; no shares issued and outstanding	—	—
Additional paid-in capital	39,413	2,028
Retained earnings (accumulated deficit)	733	(2,061)
Accumulated other comprehensive loss	(7)	(13)
Total Charter shareholders' equity (deficit)	40,139	(46)

Noncontrolling interests	10,227	—
Total shareholders' equity (deficit)	<u>50,366</u>	<u>(46)</u>
Total liabilities and shareholders' equity (deficit)	<u>\$ 149,067</u>	<u>\$ 39,316</u>

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

F- 4

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(dollars in millions, except per share and share data)

	Year Ended December 31,		
	2016	2015	2014
REVENUES	\$ 29,003	\$ 9,754	\$ 9,108
COSTS AND EXPENSES:			
Operating costs and expenses (exclusive of items shown separately below)	18,655	6,426	5,973
Depreciation and amortization	6,907	2,125	2,102
Other operating expenses, net	86	89	62
	<u>25,648</u>	<u>8,640</u>	<u>8,137</u>
Income from operations	<u>3,355</u>	<u>1,114</u>	<u>971</u>
OTHER EXPENSES:			
Interest expense, net	(2,499)	(1,306)	(911)
Loss on extinguishment of debt	(111)	(128)	—
Gain (loss) on financial instruments, net	89	(4)	(7)
Other expense, net	(14)	(7)	—
	<u>(2,535)</u>	<u>(1,445)</u>	<u>(918)</u>
Income (loss) before income taxes	820	(331)	53
Income tax benefit (expense)	2,925	60	(236)
Consolidated net income (loss)	<u>3,745</u>	<u>(271)</u>	<u>(183)</u>
Less: Net income attributable to noncontrolling interests	(223)	—	—
Net income (loss) attributable to Charter shareholders	<u>\$ 3,522</u>	<u>\$ (271)</u>	<u>\$ (183)</u>
EARNINGS (LOSS) PER COMMON SHARE ATTRIBUTABLE TO CHARTER SHAREHOLDERS:			
Basic	<u>\$ 17.05</u>	<u>\$ (2.68)</u>	<u>\$ (1.88)</u>
Diluted	<u>\$ 15.94</u>	<u>\$ (2.68)</u>	<u>\$ (1.88)</u>
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:			
Basic	<u>206,539,100</u>	<u>101,152,647</u>	<u>97,991,915</u>
Diluted	<u>234,791,439</u>	<u>101,152,647</u>	<u>97,991,915</u>

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

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
(dollars in millions)

	Year Ended December 31,		
	2016	2015	2014
Consolidated net income (loss)	\$ 3,745	\$ (271)	\$ (183)
Net impact of interest rate derivative instruments	8	9	19
Foreign currency translation adjustment	(2)	—	—
Consolidated comprehensive income (loss)	3,751	(262)	(164)
Less: Comprehensive income attributable to noncontrolling interests	(223)	—	—
Comprehensive income (loss) attributable to Charter shareholders	\$ 3,528	\$ (262)	\$ (164)

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

F- 6

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (DEFICIT)**  
(dollars in millions)

	Class A Common Stock	Class B Common Stock	Additional Paid-in Capital	Retained Earnings (Accumulated Deficit)	Treasury Stock	Accumulated Other Comprehensive Loss	Total Charter Shareholders' Equity (Deficit)	Non- controlling Interests	Total Shareholders' Equity (Deficit)
BALANCE, December 31, 2013	\$ —	\$ —	\$ 1,760	\$ (1,568)	\$ —	\$ (41)	\$ 151	\$ —	\$ 151
Net loss	—	—	—	(183)	—	—	(183)	—	(183)
Changes in accumulated other comprehensive loss, net	—	—	—	—	—	19	19	—	19
Stock compensation expense, net	—	—	55	—	—	—	55	—	55
Exercise of stock options and warrants	—	—	123	—	—	—	123	—	123
Purchase of treasury stock	—	—	—	—	(19)	—	(19)	—	(19)
Retirement of treasury stock	—	—	(8)	(11)	19	—	—	—	—
BALANCE, December 31, 2014	—	—	1,930	(1,762)	—	(22)	146	—	146
Net loss	—	—	—	(271)	—	—	(271)	—	(271)
Changes in accumulated other comprehensive loss, net	—	—	—	—	—	9	9	—	9
Stock compensation expense, net	—	—	78	—	—	—	78	—	78
Exercise of stock options and warrants	—	—	30	—	—	—	30	—	30
Purchase of treasury stock	—	—	—	—	(38)	—	(38)	—	(38)
Retirement of treasury stock	—	—	(10)	(28)	38	—	—	—	—
BALANCE, December 31, 2015	—	—	2,028	(2,061)	—	(13)	(46)	—	(46)
Net income	—	—	—	3,522	—	—	3,522	223	3,745
Stock compensation expense, net	—	—	244	—	—	—	244	—	244
Accelerated vesting of equity awards	—	—	248	—	—	—	248	—	248
Settlement of restricted stock units	—	—	(59)	—	—	—	(59)	—	(59)
Exercise of stock options	—	—	86	—	—	—	86	—	86
Purchase of treasury stock	—	—	—	—	(1,562)	—	(1,562)	—	(1,562)
Retirement of treasury stock	—	—	(834)	(728)	1,562	—	—	—	—
Issuance of shares to Liberty Broadband for cash	—	—	5,000	—	—	—	5,000	—	5,000
Converted TWC Awards in the TWC Transaction	—	—	514	—	—	—	514	—	514
Issuance of shares in TWC Transaction	—	—	32,164	—	—	—	32,164	—	32,164
Issuance of subsidiary equity in Bright House Transaction	—	—	—	—	—	—	—	10,134	10,134
Partnership formation and change in ownership, net of tax	—	—	(364)	—	—	—	(364)	589	225
Purchase of noncontrolling interest, net of tax	—	—	(19)	—	—	—	(19)	(187)	(206)
Exchange of Charter Holdings units held by A/N, net of tax and TRA effects	—	—	405	—	—	—	405	(460)	(55)
Distributions to noncontrolling interest	—	—	—	—	—	—	—	(96)	(96)
Noncontrolling interests assumed in acquisitions	—	—	—	—	—	—	—	24	24
Changes in accumulated other comprehensive loss, net	—	—	—	—	—	6	6	—	6
BALANCE, December 31, 2016	\$ —	\$ —	\$ 39,413	\$ 733	\$ —	\$ (7)	\$ 40,139	\$ 10,227	\$ 50,366

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

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(dollars in millions)

	Year Ended December 31,		
	2016	2015	2014
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Consolidated net income (loss)	\$ 3,745	\$ (271)	\$ (183)
Adjustments to reconcile consolidated net income (loss) to net cash flows from operating activities:			
Depreciation and amortization	6,907	2,125	2,102
Stock compensation expense	244	78	55
Accelerated vesting of equity awards	248	—	—
Noncash interest (income) expense	(256)	28	37
Other pension benefits	(899)	—	—
Loss on extinguishment of debt	111	128	—
(Gain) loss on financial instruments, net	(89)	4	7
Deferred income taxes	(2,958)	(65)	233
Other, net	8	11	10
Changes in operating assets and liabilities, net of effects from acquisitions and dispositions:			
Accounts receivable	(160)	5	(51)
Prepaid expenses and other assets	111	(3)	(9)
Accounts payable, accrued liabilities and other	1,029	319	158
Net cash flows from operating activities	<u>8,041</u>	<u>2,359</u>	<u>2,359</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Purchases of property, plant and equipment	(5,325)	(1,840)	(2,221)
Change in accrued expenses related to capital expenditures	603	28	33
Sales (purchases) of cable systems, net	(28,810)	—	11
Change in restricted cash and cash equivalents	22,264	(15,153)	(7,111)
Other, net	(22)	(67)	(16)
Net cash flows from investing activities	<u>(11,290)</u>	<u>(17,032)</u>	<u>(9,304)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Borrowings of long-term debt	12,344	26,045	8,806
Repayments of long-term debt	(10,521)	(11,326)	(1,980)
Payments for debt issuance costs	(284)	(36)	(6)
Issuance of equity	5,000	—	—
Purchase of treasury stock	(1,562)	(38)	(19)
Proceeds from exercise of stock options and warrants	86	30	123
Settlement of restricted stock units	(59)	—	—
Purchase of noncontrolling interest	(218)	—	—
Distributions to noncontrolling interest	(96)	—	—
Proceeds from termination of interest rate derivatives	88	—	—
Other, net	1	—	3
Net cash flows from financing activities	<u>4,779</u>	<u>14,675</u>	<u>6,927</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>1,530</b>	<b>2</b>	<b>(18)</b>

7/20/2017

Document

CASH AND CASH EQUIVALENTS, beginning of period	5	3	21
CASH AND CASH EQUIVALENTS, end of period	<u>\$ 1,535</u>	<u>\$ 5</u>	<u>\$ 3</u>
CASH PAID FOR INTEREST	<u>\$ 2,685</u>	<u>\$ 1,064</u>	<u>\$ 851</u>
CASH PAID FOR TAXES	<u>\$ 63</u>	<u>\$ 3</u>	<u>\$ 13</u>

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

F- 8

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

## 1. Organization and Basis of Presentation

### *Organization*

Charter Communications, Inc. (together with its controlled subsidiaries, "Charter," or the "Company") is the second largest cable operator in the United States and a leading broadband communications company providing video, Internet and voice services to residential and business customers. In addition, the Company sells video and online advertising inventory to local, regional and national advertising customers and fiber-delivered communications and managed information technology solutions to larger enterprise customers. The Company also owns and operates regional sports networks and local sports, news and lifestyle channels and sells security and home management services to the residential marketplace.

Charter is a holding company whose principal asset is a controlling equity interest in Charter Communications Holdings, LLC ("Charter Holdings"), an indirect owner of Charter Communications Operating, LLC ("Charter Operating") under which substantially all of the operations reside. All significant intercompany accounts and transactions among consolidated entities have been eliminated.

### *Basis of Presentation*

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and the rules and regulations of the Securities and Exchange Commission (the "SEC").

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Areas involving significant judgments and estimates include capitalization of labor and overhead costs; depreciation and amortization costs; purchase accounting valuations of assets and liabilities including, but not limited to, property, plant and equipment, intangibles and goodwill; pension benefits; income taxes; contingencies and programming expense. Actual results could differ from those estimates.

## 2. Mergers and Acquisitions

### **TWC Transaction**

On May 18, 2016, the transactions contemplated by the Agreement and Plan of Mergers dated as of May 23, 2015 (the "Merger Agreement"), by and among Time Warner Cable Inc. ("Legacy TWC"), Charter Communications, Inc. prior to the closing of the Merger Agreement ("Legacy Charter"), CCH I, LLC, previously a wholly owned subsidiary of Legacy Charter ("New Charter") and certain other subsidiaries of New Charter were completed (the "TWC Transaction," and together with the Bright House Transaction described below, the "Transactions"). As a result of the TWC Transaction, New Charter became the new public parent company that holds the operations of the combined companies and was renamed Charter Communications, Inc.

Pursuant to the terms of the Merger Agreement, upon consummation of the TWC Transaction, each outstanding share of Legacy TWC common stock (other than Legacy TWC common stock held by Liberty Broadband Corporation ("Liberty Broadband") and Liberty Interactive Corporation ("Liberty Interactive" and, collectively, the "Liberty Parties")), was converted into the right to receive, at the option of each such holder of Legacy TWC common stock, either (a) \$100 in cash and Charter Class A common stock equivalent to 0.5409 shares of Legacy Charter Class A common stock (the "Option A Consideration") or (b) \$115 in cash and Charter Class A common stock equivalent to 0.4562 shares of Legacy Charter Class A common stock (the "Option B Consideration"). The actual number of shares of Charter Class A common stock that Legacy TWC stockholders received, excluding the Liberty Parties, was calculated by multiplying the exchange ratios of 0.5409 or 0.4562 specified above by 0.9042 (the "Parent Merger Exchange Ratio"), which was also the exchange ratio that was used to determine the number of shares of Charter Class A common stock that Legacy Charter stockholders received per share of Legacy Charter Class A common stock. Such exchange ratio did not impact the aggregate value represented by the shares of Charter Class A common stock issued in the TWC Transaction; however, it did impact the actual number of shares issued in the TWC Transaction.

Out of approximately 277 million shares of TWC common stock outstanding at the closing of the TWC Transaction, excluding TWC common stock held by the Liberty Parties, approximately 274 million shares were converted into the right to receive the



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
**(dollars in millions, except share or per share data or where indicated)**

Option A Consideration and approximately 3 million shares were converted into the right to receive the Option B Consideration. The Liberty Parties received approximately one share of Charter Class A common stock for each share of Legacy TWC common stock they owned (equivalent to 1.106 shares of Legacy Charter Class A common stock multiplied by the Parent Merger Exchange Ratio).

As of the date of completion of the Transactions, the total value of the TWC Transaction was approximately \$85 billion, including cash, equity and Legacy TWC assumed debt. The purchase price also includes an estimated pre-combination vesting period fair value of \$514 million for Legacy TWC equity awards converted into Charter awards upon closing of the TWC Transaction ("Converted TWC Awards") and \$69 million of cash paid to former Legacy TWC employees and non-employee directors who held equity awards, whether vested or not vested.

#### **Bright House Transaction**

Also, on May 18, 2016, Legacy Charter and Advance/Newhouse Partnership ("A/N"), the former parent of Bright House Networks, LLC ("Bright House"), completed their previously announced transaction, pursuant to a definitive Contribution Agreement (the "Contribution Agreement"), under which Charter acquired Bright House (the "Bright House Transaction"). Pursuant to the Bright House Transaction, Charter became the owner of the membership interests in Bright House and the other assets primarily related to Bright House (other than certain excluded assets and liabilities and non-operating cash). As of the date of acquisition, the purchase price totaled approximately \$12.2 billion consisting of (a) \$2.0 billion in cash, (b) 25 million convertible preferred units of Charter Holdings with a face amount of \$2.5 billion that pay a 6% annual preferential dividend, (c) approximately 31.0 million common units of Charter Holdings that are exchangeable into Charter Class A common stock on a one-for-one basis and (d) one share of Charter Class B common stock. These Charter Holdings common and convertible preferred units held by A/N are recorded in noncontrolling interests as permanent equity in the consolidated balance sheet. See Note 11 for conversion features of the Charter Holdings common and preferred units and Note 10 for the terms of the Charter Class B common stock.

#### **Liberty Transaction**

In connection with the TWC Transaction, Legacy Charter and Liberty Broadband completed their previously announced transactions pursuant to their investment agreement, in which Liberty Broadband purchased for cash approximately 22.0 million shares of Charter Class A common stock valued at \$4.3 billion at the closing of the TWC Transaction to partially finance the cash portion of the TWC Transaction consideration, and in connection with the Bright House Transaction, Liberty Broadband purchased approximately 3.7 million shares of Charter Class A common stock valued at \$700 million at the closing of the Bright House Transaction (the "Liberty Transaction").

#### **Financing for the Transactions**

Charter partially financed the cash portion of the purchase price of the Transactions with additional indebtedness and cash on hand. In 2015, Legacy Charter issued \$15.5 billion aggregate principal amount of CCO Safari II, LLC ("CCO Safari II") senior secured notes, \$3.8 billion aggregate principal amount of CCO Safari III, LLC ("CCO Safari III") senior secured bank loans and \$2.5 billion aggregate principal amount of CCOH Safari, LLC ("CCOH Safari") senior unsecured notes. The net proceeds were initially deposited into escrow accounts. Upon closing of the TWC Transaction, the proceeds were released from escrow and the CCOH Safari notes became obligations of CCO Holdings, LLC ("CCO Holdings"), an indirect wholly-owned subsidiary of Charter Holdings, and CCO Holdings Capital Corp. ("CCO Holdings Capital"), and the CCO Safari II notes and CCO Safari III credit facilities became obligations of Charter Operating and Charter Communications Operating Capital Corp. CCOH Safari merged into CCO Holdings and CCO Safari II and CCO Safari III merged into Charter Operating.

In connection with the closing of the Bright House Transaction, Charter Operating closed on a \$2.6 billion aggregate principal amount term loan A facility ("Term Loan A") pursuant to the terms of Charter Operating's Amended and Restated Credit Agreement dated May 18, 2016 (the "Credit Agreement") of which \$2.0 billion was used to fund the cash portion of the Bright House Transaction and \$638 million was used to prepay and terminate Charter Operating's existing Term A-1 Loans. See Note 9.

#### **Acquisition Accounting**

The Transactions enable Charter to apply its operating strategy to a larger set of assets, accelerate product development and innovation through greater scale as well as more effectively compete in medium and large commercial markets. The operating



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

results of Legacy TWC and Legacy Bright House have been included in the Company's consolidated statements of operations for the period from the date of the Transactions through December 31, 2016. Revenues included in the Company's consolidated statements of operations were \$16.0 billion and \$2.6 billion for Legacy TWC and Legacy Bright House, respectively, for the year ended December 31, 2016.

Charter applied acquisition accounting to the Transactions. The total purchase price was allocated to the identifiable tangible and intangible assets acquired and the liabilities assumed based on their estimated fair values. The fair values were primarily based on third-party valuations using assumptions developed by management and other information compiled by management including, but not limited to, future expected cash flows. The excess of the purchase price over those fair values was recorded as goodwill. Goodwill recognized in the Transactions is representative of resources that do not meet the definition of an identifiable intangible asset and include buy-side synergies, economies of scale of the combined operations, increased market share, assembled workforces and improved credit rating.

The fair values of the assets acquired and liabilities assumed were preliminarily determined using the income, cost and market approaches. The fair values were primarily based on significant inputs that are not observable in the market and thus represent a Level 3 measurement, other than long-term debt assumed in the TWC Transaction, which represents a Level 1 measurement. See Note 13.

Property, plant and equipment was valued utilizing the cost approach. The cost approach considers the amount required to replace an asset by constructing or purchasing a new asset with similar utility, then adjusts the value in consideration of all forms of depreciation as of the appraisal date as described below:

- Physical depreciation - the loss in value or usefulness attributable solely to use of the asset and physical causes such as wear and tear and exposure to the elements.
- Functional obsolescence - the loss in value due to factors inherent in the asset itself and due to changes in technology, design or process resulting in inadequacy, overcapacity, lack of functional utility or excess operating costs.
- Economic obsolescence - the loss in value due to unfavorable external conditions such as economics of the industry or geographic area, or change in ordinances.

The cost approach relies on assumptions regarding current material and labor costs required to rebuild and repurchase significant components of property, plant and equipment along with assumptions regarding the age and estimated useful lives of property, plant and equipment.

Franchise rights and customer relationships were valued using an income approach model based on the present value of the estimated discrete future cash flows attributable to each of the intangible assets identified. See Note 6 for more information on the income approach model. The weighted average life of customer relationships acquired in the TWC Transaction and Bright House Transaction was 11 years and 10 years, respectively.

The fair value of equity investments was based on either applying implied multiples to estimated cash flows or utilizing a discounted cash flow model. The implied multiples were estimated based on precedent transactions and comparable companies. The discounted cash flow model required estimating the present value of future cash flows of the investee.

Legacy TWC long-term debt assumed was adjusted to fair value based on quoted market prices. At the acquisition date, the quoted market values of all but two of Legacy TWC's bonds were higher than the principal amount of the related debt instrument, which resulted in the recognition of a net debt premium of approximately \$2.4 billion. The quoted market value of a debt instrument is higher than the principal amount of the debt when the market interest rates are lower than the stated interest rate of the debt. This debt premium is amortized as a reduction to interest expense over the remaining life of the applicable debt.

Generally, no fair value adjustments were reflected in current assets and current liabilities as carrying value is estimated to approximate fair value because of the short-term nature of the items, except for risk management obligations. Risk management obligations assumed including various claims for workers compensation, employment practices, and auto and general liabilities were measured at fair value as of the acquisition date based on an actuarially determined study. Fair value adjustments were reflected in other noncurrent assets and other long-term liabilities relating to contract-based assets and liabilities, capital lease obligations, deferred liabilities and net pension liabilities. Out-of-market contract-based assets and liabilities relating to non-cancelable executory contracts and operating leases were recognized based on discounted cash flow models to the extent the terms



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

of the non-cancelable contracts are favorable or unfavorable compared with the relative market terms of the same or similar contract at the acquisition date. The out-of-market element will be amortized as if the contract were consummated at market terms on the acquisition date. Capital lease obligations were measured at fair value based on the present value of amounts to be paid under the lease agreement using a market participant discount rate. Deferred liabilities were not recorded in acquisition accounting to the extent there was no associated payment obligation or substantive performance obligation. The net pension liabilities assumed in the TWC Transaction were measured at fair value based on an actuarially determined projected benefit obligation, less the fair value of pension investments, as of the acquisition date. See Note 21 for fair value assumptions considered in acquisition accounting for the net pension liabilities.

Deferred tax assets and liabilities were recorded for the deferred tax impact of acquisition accounting adjustments primarily related to property, plant and equipment, franchises, customer relationships and assumed Legacy TWC long-term debt. The incremental deferred tax liabilities were calculated primarily based on the tax effect of the step-up in book basis of net assets of Legacy TWC excluding the amount attributable to nondeductible goodwill.

The Charter Class A common stock issued to Legacy TWC stockholders and Charter Holdings common units issued to A/N were valued based on the opening share price of Charter Class A common stock on the acquisition date. The convertible preferred units of Charter Holdings issued to A/N were valued at approximately \$3.2 billion based on a binomial lattice model for convertible bonds that models the future changes in the common equity value of Charter. The valuation relies on management's assumptions including risk-free interest rate, volatility and discount yield. The pre-combination vesting period fair value of the Converted TWC Awards was based on the portion of the requisite service period completed at the acquisition date by Legacy TWC employee award holders applied to the total fair value of the Converted TWC Awards.

The allocation of the purchase price to certain assets and liabilities is preliminary and is subject to change based on additional information that may be obtained during the measurement period primarily related to working capital measurement. The Company will continue to obtain information to assist in finalizing the fair value of net assets acquired and liabilities assumed, which is not expected to differ materially from the preliminary estimates herein. The Company will apply any measurement period adjustments, including any related impacts to net income (loss), in the reporting period in which the adjustments are determined. The tables below present the calculation of the purchase price and the preliminary allocation of the purchase price to the assets acquired and liabilities assumed in the Transactions.

***TWC Purchase Price***

Shares of Charter Class A common stock issued (including the Liberty Parties) (in millions)	143.0
Charter Class A common stock closing price per share	\$ 224.91
Fair value of Charter Class A common stock issued	<u>\$ 32,164</u>
Cash paid to Legacy TWC stockholders (excluding the Liberty Parties)	\$ 27,770
Pre-combination vesting period fair value of Converted TWC Awards	514
Cash paid for Legacy TWC non-employee equity awards	69
Total purchase price	<u>\$ 60,517</u>

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

*TWC Preliminary Allocation of Purchase Price*

Cash and cash equivalents	\$ 1,058
Current assets	1,308
Property, plant and equipment	21,413
Customer relationships	13,460
Franchises	54,085
Goodwill	28,292
Other noncurrent assets	1,040
Accounts payable and accrued liabilities	(3,925)
Debt	(24,900)
Deferred income taxes	(28,148)
Other long-term liabilities	(3,162)
Noncontrolling interests	(4)
	<u>\$ 60,517</u>

Since completion of the initial estimates in the second quarter of 2016, the Company made measurement period adjustments to the fair value of certain assets acquired and liabilities assumed in the TWC Transaction, including a decrease of \$163 million to property, plant and equipment; a decrease of \$240 million to customer relationships; an increase of \$690 million to franchises; an increase to other operating net liabilities of \$215 million; and a decrease of \$4 million to deferred income taxes; resulting in a net decrease to goodwill of \$76 million. These adjustments were made primarily to reflect updated appraisal results.

The measurement period adjustment to intangibles resulted in a decrease of \$20 million in amortization expense relating to the prior quarters that was recorded in the fourth quarter of 2016. The measurement period adjustment to property, plant and equipment resulted in an increase of \$12 million in depreciation expense relating to the second quarter that was recorded in the third quarter of 2016. The Company may record additional measurement period adjustments in future periods.

*Bright House Purchase Price*

Charter Holdings common units issued to A/N (in millions)	31.0
Charter Class A common stock closing price per share	\$ 224.91
Fair value of Charter Holdings common units issued to A/N	<u>\$ 6,971</u>
Fair value of Charter Holdings convertible preferred units issued to A/N	3,163
Cash paid to A/N	2,022
Total purchase price	<u>\$ 12,156</u>

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

*Bright House Preliminary Allocation of Purchase Price*

Current assets	\$ 131
Property, plant and equipment	2,884
Customer relationships	2,150
Franchises	7,225
Goodwill	44
Other noncurrent assets	86
Accounts payable and accrued liabilities	(330)
Other long-term liabilities	(12)
Noncontrolling interests	(22)
	\$ 12,156

Since completion of the initial estimates in the second quarter of 2016, the Company made measurement period adjustments to the fair value of certain assets acquired and liabilities assumed in the Bright House Transaction, including a decrease of \$382 million to property, plant and equipment; an increase of \$110 million to customer relationships; an increase of \$381 million to franchises; and a decrease of \$1 million to current assets resulting in a decrease to goodwill of \$108 million. These adjustments were made primarily to reflect updated appraisal results.

The measurement period adjustment to intangibles resulted in an increase of \$7 million in amortization expense relating to the prior quarters that was recorded in the fourth quarter of 2016. The measurement period adjustment to property, plant and equipment in the third quarter had an inconsequential impact on depreciation expense recorded in the prior quarter. The Company may record additional measurement period adjustments in future periods.

**Selected Pro Forma Financial Information**

The following unaudited pro forma financial information of the Company is based on the historical consolidated financial statements of Legacy Charter, Legacy TWC and Legacy Bright House and is intended to provide information about how the Transactions and related financing may have affected the Company's historical consolidated financial statements if they had closed as of January 1, 2015. The pro forma financial information below is based on available information and assumptions that the Company believes are reasonable. The pro forma financial information is for illustrative and informational purposes only and is not intended to represent or be indicative of what the Company's financial condition or results of operations would have been had the transactions described above occurred on the date indicated. The pro forma financial information also should not be considered representative of the Company's future financial condition or results of operations.

	Year Ended December 31,	
	2016	2015
Revenues	\$ 40,023	\$ 37,394
Net income attributable to Charter shareholders	\$ 1,070	\$ 159
Earnings per common share attributable to Charter shareholders:		
Basic	\$ 3.97	\$ 0.59
Diluted	\$ 3.91	\$ 0.58

**3. Summary of Significant Accounting Policies**

*Consolidation*

The accompanying consolidated financial statements include the accounts of Charter and all entities in which Charter has a controlling interest. The Company consolidates based upon evaluation of the Company's power, through voting rights or similar rights, to direct

the activities of another entity that most significantly impact the entity's economic performance; its obligation to

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

absorb the expected losses of the entity; and its right to receive the expected residual returns of the entity. Charter controls and consolidates Charter Holdings. The noncontrolling interest on the Company's balance sheet primarily represents A/N's minority equity interests in Charter Holdings. See Note 11. All significant inter-company accounts and transactions among consolidated entities have been eliminated in consolidation.

***Cash and Cash Equivalents***

The Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents. These investments are carried at cost, which approximates market value. Cash and cash equivalents consist primarily of money market funds and commercial paper.

***Restricted Cash and Cash Equivalents***

Proceeds from the issuance of certain long-term debt were deposited into escrow accounts and were used for acquisition financing and were contractually restricted as to their withdrawal or use. See Note 2. The amounts held in escrow were classified as noncurrent restricted cash and cash equivalents in the Company's consolidated balance sheets as of December 31, 2015. The Company's restricted cash and cash equivalents were primarily invested in money market funds and 90-day or less commercial paper. The changes in restricted cash and cash equivalents are presented as an investing activity in the Company's consolidated statements of cash flows.

***Property, Plant and Equipment***

Additions to property, plant and equipment are recorded at cost, including all material, labor and certain indirect costs associated with the construction of cable transmission and distribution facilities. While the Company's capitalization is based on specific activities, once capitalized, costs are tracked on a composite basis by fixed asset category at the cable system level and not on a specific asset basis. For assets that are sold or retired, the estimated historical cost and related accumulated depreciation is removed. Costs associated with the initial placement of the customer drop to the dwelling and the initial placement of outlets within a dwelling along with the costs associated with the initial deployment of customer premise equipment necessary to provide video, Internet or voice services are capitalized. Costs capitalized include materials, direct labor, and certain indirect costs. Indirect costs are associated with the activities of the Company's personnel who assist in installation activities and consist of compensation and other costs associated with these support functions. Indirect costs primarily include employee benefits and payroll taxes, vehicle and occupancy costs, and the costs of sales and dispatch personnel associated with capitalizable activities. The costs of disconnecting service and removing customer premise equipment from a dwelling and the costs to reconnect a customer drop or to redeploy previously installed customer premise equipment are charged to operating expense as incurred. Costs for repairs and maintenance are charged to operating expense as incurred, while plant and equipment replacement, including replacement of certain components, betterments, including replacement of cable drops and outlets, are capitalized.

Depreciation is recorded using the straight-line composite method over management's estimate of the useful lives of the related assets as follows:

Cable distribution systems	7-20 years
Customer premise equipment and installations	3-8 years
Vehicles and equipment	3-6 years
Buildings and improvements	15-40 years
Furniture, fixtures and equipment	6-10 years

***Asset Retirement Obligations***

Certain of the Company's franchise agreements and leases contain provisions requiring the Company to restore facilities or remove equipment in the event that the franchise or lease agreement is not renewed. The Company expects to continually renew its franchise agreements and therefore cannot reasonably estimate any liabilities associated with such agreements. A remote possibility exists that franchise agreements could be terminated unexpectedly, which could result in the Company incurring significant expense in complying with restoration or removal provisions. The Company does not have any significant liabilities related to asset retirements recorded in its consolidated financial statements.



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

*Valuation of Long-Lived Assets*

The Company evaluates the recoverability of long-lived assets (e.g., property, plant and equipment and finite-lived intangible assets) to be held and used when events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Such events or changes in circumstances could include such factors as impairment of the Company's indefinite life assets, changes in technological advances, fluctuations in the fair value of such assets, adverse changes in relationships with local franchise authorities, adverse changes in market conditions or a deterioration of operating results. If a review indicates that the carrying value of such asset is not recoverable from estimated undiscounted cash flows, the carrying value of such asset is reduced to its estimated fair value. While the Company believes that its estimates of future cash flows are reasonable, different assumptions regarding such cash flows could materially affect its evaluations of asset recoverability. No impairments of long-lived assets to be held and used were recorded in 2016, 2015 and 2014.

*Other Noncurrent Assets*

Other noncurrent assets primarily include investments, trademarks, right-of-entry costs and other intangible assets. The Company accounts for its investments in less than majority owned investees under either the equity or cost method. The Company applies the equity method to investments when it has the ability to exercise significant influence over the operating and financial policies of the investee. The Company's share of the investee's earnings (losses) is included in other expense, net in the consolidated statements of operations. The Company monitors its investments for indicators that a decrease in investment value has occurred that is other than temporary. If it has been determined that an investment has sustained an other than temporary decline in value, the investment is written down to fair value with a charge to earnings. Investments acquired are measured at fair value utilizing the acquisition method of accounting. The difference between the fair value and the amount of underlying equity in net assets for most equity method investments is due to previously unrecognized intangible assets at the investee. These amounts are amortized as a component of equity earnings (losses), recorded within other expense, net over the estimated useful life of the asset. Trademarks have been determined to have an indefinite life and are tested annually for impairment. Right-of-entry costs represent costs incurred related to agreements entered into with landlords, real estate companies or owners to gain access to a building in order to provide cable service. Right-of-entry costs are generally deferred and amortized to amortization expense over the term of the agreement.

*Revenue Recognition*

Revenues from residential and commercial video, Internet and voice services are recognized when the related services are provided. Advertising sales are recognized at estimated realizable values in the period that the advertisements are broadcast. In some cases, the Company coordinates the advertising sales efforts of other cable operators in a certain market and remits amounts received from customers less an agreed-upon percentage to such cable operator. For those arrangements in which the Company acts as a principal, the Company records the revenues earned from the advertising customer on a gross basis and the amount remitted to the cable operator as an operating expense.

Fees imposed on the Company by various governmental authorities are passed through on a monthly basis to the Company's customers and are periodically remitted to authorities. Fees of \$711 million, \$255 million and \$248 million for the years ended December 31, 2016, 2015 and 2014, respectively, are reported in video, voice and commercial revenues, on a gross basis with a corresponding operating expense because the Company is acting as a principal. Other taxes, such as sales taxes imposed on the Company's customers, collected and remitted to state and local authorities, are recorded on a net basis because the Company is acting as an agent in such situation.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

The Company's revenues by product line are as follows:

	Year Ended December 31,		
	2016	2015	2014
Video	\$ 11,967	\$ 4,587	\$ 4,443
Internet	9,272	3,003	2,576
Voice	2,005	539	575
Residential revenue	23,244	8,129	7,594
Small and medium business	2,480	764	676
Enterprise	1,429	363	317
Commercial revenue	3,909	1,127	993
Advertising sales	1,235	309	341
Other	615	189	180
	<u>\$ 29,003</u>	<u>\$ 9,754</u>	<u>\$ 9,108</u>

#### *Programming Costs*

The Company has various contracts to obtain video programming from vendors whose compensation is typically based on a flat fee per customer. The cost of the right to exhibit network programming under such arrangements is recorded in operating expenses in the month the programming is available for exhibition. Programming costs are paid each month based on calculations performed by the Company and are subject to periodic audits performed by the programmers. Certain programming contracts contain incentives to be paid by the programmers. The Company receives these payments and recognizes the incentives on a straight-line basis over the life of the programming agreement as a reduction of programming expense. Programming costs included in the statements of operations were \$7.0 billion, \$2.7 billion and \$2.5 billion for the years ended December 31, 2016, 2015 and 2014, respectively.

#### *Advertising Costs*

Advertising costs associated with marketing the Company's products and services are generally expensed as costs are incurred.

#### *Multiple-Element Transactions*

In the normal course of business, the Company enters into multiple-element transactions where it is simultaneously both a customer and a vendor with the same counterparty or in which it purchases multiple products and/or services, or settles outstanding items contemporaneous with the purchase of a product or service from a single counterparty. Transactions, although negotiated contemporaneously, may be documented in one or more contracts. The Company's policy for accounting for each transaction negotiated contemporaneously is to record each element of the transaction based on the respective estimated fair values of the products or services purchased and the products or services sold. In determining the fair value of the respective elements, the Company refers to quoted market prices (where available), historical transactions or comparable cash transactions. Cash consideration received from a vendor is recorded as a reduction in the price of the vendor's product unless (i) the consideration is for the reimbursement of a specific, incremental, identifiable cost incurred, in which case the cash consideration received would be recorded as a reduction in such cost (e.g., marketing costs), or (ii) an identifiable benefit in exchange for the consideration is provided, in which case revenue would be recognized for this element.

#### *Stock-Based Compensation*

Restricted stock, restricted stock units, stock options as well as equity awards with market conditions are measured at the grant date fair value and amortized to stock compensation expense over the requisite service period. The fair value of options is estimated on the

date of grant using the Black-Scholes option-pricing model and the fair value of equity awards with market conditions is estimated on the date of grant using Monte Carlo simulations. The grant date weighted average assumptions used during the years

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

ended December 31, 2016, 2015 and 2014, respectively, were: risk-free interest rate of 1.7%, 1.5% and 2.0%; expected volatility of 25.4%, 34.7% and 36.9%; and expected lives of 1.3 years, 6.5 years and 6.5 years. Weighted average assumptions for 2016 include the assumptions used for the Converted TWC Awards. Volatility assumptions were based on historical volatility of Legacy Charter and Legacy TWC. The Company's volatility assumptions represent management's best estimate and were partially based on historical volatility of Legacy TWC due to the completion of the Transactions. Expected lives were estimated using historical exercise data. The valuations assume no dividends are paid.

#### *Pension Plans*

The Company sponsors the TWC Pension Plan, TWC Union Pension Plan and TWC Excess Pension Plan (as defined in Note 21). Pension benefits are based on formulas that reflect the employees' years of service and compensation during their employment period. Actuarial gains or losses are changes in the amount of either the benefit obligation or the fair value of plan assets resulting from experience different from that assumed or from changes in assumptions. The Company has elected to follow a mark-to-market pension accounting policy for recording the actuarial gains or losses annually during the fourth quarter, or earlier if a remeasurement event occurs during an interim period.

#### *Income Taxes*

The Company recognizes deferred tax assets and liabilities for temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities and expected benefits of utilizing loss carryforwards. Since substantially all the Company's operations are held through its partnership interest in Charter Holdings, the primary deferred tax component recorded in the consolidated balance sheet relates to the excess financial reporting outside basis, excluding amounts attributable to nondeductible goodwill, over Charter's tax basis in its investment in the partnership. Valuation allowances are established when management determines that it is more likely than not that some portion or the entire deferred tax asset will not be realized. The impact on deferred taxes of changes in tax rates and tax law, if any, applied to the years during which temporary differences are expected to be settled, are reflected in the consolidated financial statements in the period of enactment. In determining the Company's tax provision for financial reporting purposes, the Company establishes a reserve for uncertain tax positions unless such positions are determined to be "more likely than not" of being sustained upon examination, based on their technical merits. There is considerable judgment involved in making such a determination. Interest and penalties are recognized on uncertain income tax positions as part of the income tax provision. See Note 17.

#### *Segments*

The Company's operations are managed and reported to its Chief Executive Officer ("CEO"), the Company's chief operating decision maker, on a consolidated basis. The CEO assesses performance and allocates resources based on the consolidated results of operations. Under this organizational and reporting structure, the Company has one reportable segment, cable services.

#### **4. Allowance for Doubtful Accounts**

Activity in the allowance for doubtful accounts is summarized as follows for the years presented:

	Year Ended December 31,		
	2016	2015	2014
Balance, beginning of period	\$ 21	\$ 22	\$ 19
Charged to expense	328	135	122
Uncollected balances written off, net of recoveries	(225)	(136)	(119)
Balance, end of period	<u>\$ 124</u>	<u>\$ 21</u>	<u>\$ 22</u>

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

## 5. Property, Plant and Equipment

Property, plant and equipment consists of the following as of December 31, 2016 and 2015:

	December 31,	
	2016	2015
Cable distribution systems	\$ 23,317	\$ 8,158
Customer premise equipment and installations	12,867	4,632
Vehicles and equipment	1,212	384
Buildings and improvements	3,426	570
Furniture, fixtures and equipment	3,244	1,119
	<u>44,066</u>	<u>14,863</u>
Less: accumulated depreciation	(11,103)	(6,518)
	<u>\$ 32,963</u>	<u>\$ 8,345</u>

The Company periodically evaluates the estimated useful lives used to depreciate its assets and the estimated amount of assets that will be abandoned or have minimal use in the future. A significant change in assumptions about the extent or timing of future asset retirements, or in the Company's use of new technology and upgrade programs, could materially affect future depreciation expense.

Depreciation expense for the years ended December 31, 2016, 2015 and 2014 was \$5.0 billion, \$1.9 billion, and \$1.8 billion, respectively. Property, plant and equipment increased by \$24.3 billion as a result of the Transactions. See Note 2.

## 6. Franchises, Goodwill and Other Intangible Assets

Franchise rights represent the value attributed to agreements or authorizations with local and state authorities that allow access to homes in cable service areas. For valuation purposes, they are defined as the future economic benefits of the right to solicit and service potential customers (customer marketing rights), and the right to deploy and market new services to potential customers (service marketing rights).

Management estimates the fair value of franchise rights at the date of acquisition and determines if the franchise has a finite life or an indefinite life. The Company has concluded that all of its franchises, including those acquired as part of the Transactions, qualify for indefinite life treatment given that there are no legal, regulatory, contractual, competitive, economic or other factors which limit the period over which these rights will contribute to our cash flows. We reassess this determination periodically or whenever events or substantive changes in circumstances occur.

The estimated fair value of franchises is determined utilizing an income approach model based on the present value of the estimated discrete future cash flows attributable to each of the intangible assets identified assuming a discount rate. The fair value of franchises is determined based on estimated discrete discounted future cash flows using assumptions consistent with internal forecasts. The franchise after-tax cash flow is calculated as the after-tax cash flow generated by the potential customers obtained. The sum of the present value of the franchises' after-tax cash flow in years 1 through 10 and the continuing value of the after-tax cash flow beyond year 10 yields the fair value of the franchises.

This approach makes use of unobservable factors such as projected revenues, expenses, capital expenditures, customer trends, and a discount rate applied to the estimated cash flows. The determination of the franchise discount rate is derived from the Company's weighted average cost of capital, which uses a market participant's cost of equity and after-tax cost of debt and reflects the risks inherent in the cash flows. The Company estimates discounted future cash flows using reasonable and appropriate assumptions including among others, penetration rates for video, Internet, and voice; revenue growth rates; operating margins; and capital expenditures. The assumptions are based on the Company's and its peers' historical operating performance adjusted for current and expected competitive and economic factors surrounding the cable industry. The estimates and assumptions made in the Company's valuations are inherently subject to significant uncertainties, many of which are beyond its control, and there is no assurance that these results can be achieved. The primary assumptions for which there is a reasonable possibility of the occurrence of a variation that would significantly affect the measurement value include the assumptions regarding revenue growth.



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
**(dollars in millions, except share or per share data or where indicated)**

programming expense growth rates, the amount and timing of capital expenditures, actual customer trends and the discount rate utilized.

All franchises are tested for impairment annually or more frequently as warranted by events or changes in circumstances. Franchise assets are aggregated into essentially inseparable units of accounting to conduct valuations. The units of accounting generally represent geographical clustering of our cable systems into groups. The Company assesses qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that an indefinite lived intangible asset has been impaired. If, after this optional qualitative assessment, the Company determines that it is not more likely than not that an indefinite lived intangible asset has been impaired, then no further quantitative testing is necessary. In completing the qualitative impairment testing, the Company evaluates a multitude of factors that affect the fair value of our franchise assets. Examples of such factors include environmental and competitive changes within our operating footprint, actual and projected operating performance, the consistency of our operating margins, equity and debt market trends, including changes in our market capitalization, and changes in our regulatory and political landscape, among other factors. After consideration of the qualitative factors, in 2016 the Company concluded that it is more likely than not that the fair value of the franchise assets in each unit of accounting exceeds the carrying value of such assets and therefore did not perform a quantitative analysis. Periodically, the Company will elect to perform a quantitative analysis for impairment testing. If the Company elects or is required to perform a quantitative analysis to test its franchise assets for impairment, the methodology described above is utilized.

The fair value of goodwill is determined using both an income approach and market approach. The Company's income approach model used for its goodwill valuation is consistent with that used for its franchise valuation noted above except that cash flows from the entire business enterprise are used for the goodwill valuation. The Company's market approach model estimates the fair value of the reporting unit based on market prices in actual precedent transactions of similar businesses and market valuations of guideline public companies. Goodwill is tested for impairment as of November 30 of each year, or more frequently as warranted by events or changes in circumstances. Accounting guidance also permits an optional qualitative assessment for goodwill to determine whether it is more likely than not that the carrying value of a reporting unit exceeds its fair value. If, after this qualitative assessment, the Company determines that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount then no further quantitative testing would be necessary. If the Company elects or is required to perform the two-step test under the accounting guidance, the first step involves a comparison of the estimated fair value of the reporting unit to its carrying amount. If the estimated fair value of the reporting unit exceeds its carrying amount, goodwill of the reporting unit is not considered impaired and the second step of the goodwill impairment is not necessary. If the carrying amount of a reporting unit exceeds its estimated fair value, then the second step of the goodwill impairment test must be performed, and a comparison of the implied fair value of the reporting unit's goodwill is compared to its carrying amount to determine the amount of impairment, if any. As with the Company's franchise impairment testing, in 2016 the Company elected to perform a qualitative goodwill impairment assessment and concluded that goodwill is not impaired.

Customer relationships are recorded at fair value as of the date acquired less accumulated amortization. Customer relationships, for valuation purposes, represent the value of the business relationship with existing customers, and are calculated by projecting the discrete future after-tax cash flows from these customers, including the right to deploy and market additional services to these customers. The present value of these after-tax cash flows yields the fair value of the customer relationships. The use of different valuation assumptions or definitions of franchises or customer relationships, such as our inclusion of the value of selling additional services to our current customers within customer relationships versus franchises, could significantly impact our valuations and any resulting impairment. Customer relationships are amortized on an accelerated sum of years' digits method over useful lives of 8-15 years based on the period over which current customers are expected to generate cash flows. The Company periodically evaluates the remaining useful lives of its customer relationships to determine whether events or circumstances warrant revision to the remaining periods of amortization. Customer relationships are evaluated for impairment upon the occurrence of events or changes in circumstances indicating that the carrying amount of an asset may not be recoverable. Customer relationships are deemed impaired when the carrying value exceeds the projected undiscounted future cash flows associated with the customer relationships. No impairment of customer relationships was recorded in the years ended December 31, 2016, 2015 or 2014.

The fair value of trademarks is determined using the relief-from-royalty method, a variation of the income approach, which applies a fair royalty rate to estimated revenue derived under the Company's trademarks. The fair value of the intangible is estimated to be the present value of the royalty saved because the Company owns the trademarks. Royalty rates are estimated based on a review of market royalty rates in the communications and entertainment industries. As the Company expects to continue to use each trademark indefinitely, trademarks have been assigned an indefinite life and are tested annually for impairment using either a qualitative analysis or quantitative analysis as elected by management. As with the Company's franchise impairment testing, in



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

2016 the Company elected to perform a qualitative trademark impairment assessment and concluded that trademarks are not impaired.

As of December 31, 2016 and 2015, indefinite-lived and finite-lived intangible assets are presented in the following table:

	December 31,					
	2016			2015		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Indefinite-lived intangible assets:						
Franchises	\$ 67,316	\$ —	\$ 67,316	\$ 6,006	\$ —	\$ 6,006
Goodwill	29,509	—	29,509	1,168	—	1,168
Trademarks	159	—	159	159	—	159
Other intangible assets	4	—	4	4	—	4
	<u>\$ 96,988</u>	<u>\$ —</u>	<u>\$ 96,988</u>	<u>\$ 7,337</u>	<u>\$ —</u>	<u>\$ 7,337</u>
Finite-lived intangible assets:						
Customer relationships	\$ 18,226	\$ (3,618)	\$ 14,608	\$ 2,616	\$ (1,760)	\$ 856
Other intangible assets	615	(128)	487	173	(82)	91
	<u>\$ 18,841</u>	<u>\$ (3,746)</u>	<u>\$ 15,095</u>	<u>\$ 2,789</u>	<u>\$ (1,842)</u>	<u>\$ 947</u>

Other intangible assets consist primarily of right-of-entry costs. Amortization expense related to customer relationships and other intangible assets for the years ended December 31, 2016, 2015 and 2014 was \$1.9 billion, \$271 million and \$299 million, respectively. Franchises, goodwill and customer relationships increased by \$61.3 billion, \$28.3 billion and \$15.6 billion, respectively, as a result of the Transactions. See Note 2.

The Company expects amortization expense on its finite-lived intangible assets will be as follows.

2017	\$ 2,743
2018	2,461
2019	2,178
2020	1,886
2021	1,602
Thereafter	4,225
	<u>\$ 15,095</u>

Actual amortization expense in future periods could differ from these estimates as a result of new intangible asset acquisitions or divestitures, changes in useful lives, impairments and other relevant factors.

## 7. Investments

In connection with the Transactions, the Company acquired approximately \$508 million of Legacy TWC and Legacy Bright House equity-method and cost-method investments, which were adjusted to fair value as a result of applying acquisition accounting. The equity-method investments acquired include Sterling Entertainment Enterprises, LLC ("Sterling" - d/b/a SportsNet New York - 26.8% owned), MLB Network, LLC ("MLB Network" - 6.4% owned), iN Demand L.L.C. ("iN Demand" - 39.8% owned) and National Cable Communications LLC ("NCC" - 20.0% owned), among other less significant equity-method and cost-method investments. Sterling and MLB Network are primarily engaged in the development of sports programming services. iN Demand provides programming on a video on demand, pay-per-view and subscription basis. NCC represents multi-video program distributors to advertisers.



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Investments consisted of the following as of December 31, 2016 and 2015:

	December 31,	
	2016	2015
Equity-method investments	519	53
Other investments	11	2
<b>Total investments</b>	<b>\$ 530</b>	<b>\$ 55</b>

The Company's equity-method investments balance as of December 31, 2016 reflected in the table above includes differences between the acquisition date fair value of certain investments acquired in the Transactions and the underlying equity in the net assets of the investee, referred to as a basis difference. As discussed in Note 2, this basis difference is amortized as a component of equity earnings. The remaining unamortized basis difference is \$436 million as of December 31, 2016.

The Company applies the equity method of accounting to these and other less significant equity-method investments, all of which are recorded in other noncurrent assets in the consolidated balance sheets as of December 31, 2016 and 2015. For the years ended December 31, 2016 and 2015, net losses from equity-method investments were \$14 million and \$7 million, respectively, which were recorded in other expense, net in the consolidated statements of operations.

#### 8. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities consist of the following as of December 31, 2016 and 2015:

	December 31,	
	2016	2015
Accounts payable – trade	\$ 454	\$ 134
Deferred revenue	352	96
Accrued liabilities:		
Programming costs	1,783	451
Compensation	1,111	191
Capital expenditures	1,107	296
Interest	958	445
Taxes and regulatory fees	538	128
Property and casualty	394	74
Other	847	157
	<b>\$ 7,544</b>	<b>\$ 1,972</b>

#### 9. Long-Term Debt

Long-term debt consists of the following as of December 31, 2016 and 2015:

	December 31,			
	2016		2015	
	Principal Amount	Accreted Value	Principal Amount	Accreted Value
CCOH Safari, LLC:				
5.750% senior notes due February 15, 2026	\$ —	\$ —	\$ 2,500	\$ 2,499
CCO Safari II, LLC:				

7/20/2017

Document

3.579% senior notes due July 23, 2020	—	—	2,000	1,999
4.464% senior notes due July 23, 2022	—	—	3,000	2,998

F- 22

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

4.908% senior notes due July 23, 2025	—	—	4,500	4,497
6.384% senior notes due October 23, 2035	—	—	2,000	1,999
6.484% senior notes due October 23, 2045	—	—	3,500	3,498
6.834% senior notes due October 23, 2055	—	—	500	500
CCO Safari III, LLC:				
Credit facilities	—	—	3,800	3,788
CCO Holdings, LLC:				
7.000% senior notes due January 15, 2019	—	—	600	594
7.375% senior notes due June 1, 2020	—	—	750	744
5.250% senior notes due March 15, 2021	500	496	500	496
6.500% senior notes due April 30, 2021	—	—	1,500	1,487
6.625% senior notes due January 31, 2022	750	741	750	740
5.250% senior notes due September 30, 2022	1,250	1,232	1,250	1,229
5.125% senior notes due February 15, 2023	1,000	992	1,000	990
5.125% senior notes due May 1, 2023	1,150	1,141	1,150	1,140
5.750% senior notes due September 1, 2023	500	496	500	495
5.750% senior notes due January 15, 2024	1,000	991	1,000	990
5.875% senior notes due April 1, 2024	1,700	1,685	—	—
5.375% senior notes due May 1, 2025	750	744	750	744
5.750% senior notes due February 15, 2026	2,500	2,460	—	—
5.500% senior notes due May 1, 2026	1,500	1,487	—	—
5.875% senior notes due May 1, 2027	800	794	800	794
Charter Communications Operating, LLC:				
3.579% senior notes due July 23, 2020	2,000	1,983	—	—
4.464% senior notes due July 23, 2022	3,000	2,973	—	—
4.908% senior notes due July 23, 2025	4,500	4,458	—	—
6.384% senior notes due October 23, 2035	2,000	1,980	—	—
6.484% senior notes due October 23, 2045	3,500	3,466	—	—
6.834% senior notes due October 23, 2055	500	495	—	—
Credit facilities	8,916	8,814	3,552	3,502
Time Warner Cable, LLC:				
5.850% senior notes due May 1, 2017	2,000	2,028	—	—
6.750% senior notes due July 1, 2018	2,000	2,135	—	—
8.750% senior notes due February 14, 2019	1,250	1,412	—	—
8.250% senior notes due April 1, 2019	2,000	2,264	—	—
5.000% senior notes due February 1, 2020	1,500	1,615	—	—
4.125% senior notes due February 15, 2021	700	739	—	—
4.000% senior notes due September 1, 2021	1,000	1,056	—	—
5.750% sterling senior notes due June 2, 2031 <sup>(a)</sup>	770	834	—	—
6.550% senior debentures due May 1, 2037	1,500	1,691	—	—
7.300% senior debentures due July 1, 2038	1,500	1,795	—	—
6.750% senior debentures due June 15, 2039	1,500	1,730	—	—
5.875% senior debentures due November 15, 2040	1,200	1,259	—	—
5.500% senior debentures due September 1, 2041	1,250	1,258	—	—

7/20/2017

Document

5.250% sterling senior notes due July 15, 2042 <sup>(b)</sup>

800

771

—

—

4.500% senior debentures due September 15, 2042

1,250

1,135

—

—

Time Warner Cable Enterprises LLC:

F- 23

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

8.375% senior debentures due March 15, 2023	1,000	1,273	—	—
8.375% senior debentures due July 15, 2033	1,000	1,324	—	—
<b>Total debt</b>	60,036	61,747	35,902	35,723
Less current portion:				
5.850% senior notes due May 1, 2017	(2,000)	(2,028)	—	—
<b>Long-term debt</b>	\$ 58,036	\$ 59,719	\$ 35,902	\$ 35,723

(a) Principal amount includes £625 million valued at \$770 million as of December 31, 2016 using the exchange rate at that date.

(b) Principal amount includes £650 million valued at \$800 million as of December 31, 2016 using the exchange rate at that date.

The accreted values presented in the table above represent the principal amount of the debt less the original issue discount at the time of sale, deferred financing costs, and, (i) in regards to the Legacy TWC debt assumed, a fair value premium adjustment as a result of applying acquisition accounting plus/minus the accretion of those amounts to the balance sheet date and (ii) in regards to the fixed-rate British pound sterling denominated notes (the "Sterling Notes"), a remeasurement of the principal amount of the debt and any premium or discount into US dollars as of the balance sheet date. See Note 12. However, the amount that is currently payable if the debt becomes immediately due is equal to the principal amount of the debt. The Company has availability under the Charter Operating credit facilities of approximately \$2.8 billion as of December 31, 2016.

In December 2016, Charter Operating entered into an amendment to its Credit Agreement decreasing the applicable LIBOR margin on the term loan A, term loan H, term loan I and revolver to 1.75%, 2.00%, 2.25% and 1.75%, respectively, eliminating the LIBOR floor on the term loan H and term loan I and extending the maturity of term loan H to 2022 and term loan I to 2024. The Company recorded a loss on extinguishment of debt of \$1 million for the year ended December 31, 2016 related to these transactions.

In February 2016, CCO Holdings and CCO Holdings Capital jointly issued \$1.7 billion aggregate principal amount of 5.875% senior notes due 2024 (the "2024 Notes") and, in April 2016, they issued \$1.5 billion aggregate principal amount of 5.500% senior notes due 2026 (the "2026 Notes") at a price of 100.075% of the aggregate principal amount. The net proceeds from both issuances were used to repurchase all of CCO Holdings' 7.000% senior notes due 2019, 7.375% senior notes due 2020 and 6.500% senior notes due 2021 and to pay related fees and expenses and for general corporate purposes. These debt repurchases resulted in a loss on extinguishment of debt of \$110 million for the year ended December 31, 2016.

In April 2015, CCO Holdings and CCO Holdings Capital closed on transactions in which they issued \$1.15 billion aggregate principal amount of 5.125% senior unsecured notes due 2023 (the "2023 Notes"), \$750 million aggregate principal amount of 5.375% senior unsecured notes due 2025 (the "2025 Notes") and \$800 million aggregate principal amount of 5.875% senior unsecured notes due 2027 (the "2027 Notes"). The net proceeds from the issuance of the 2023 Notes and 2025 Notes were used to finance tender offers and a subsequent call in which \$1.0 billion aggregate principal amount of CCO Holdings' outstanding 7.250% senior notes due 2017 and \$700 million aggregate principal amount of CCO Holdings' outstanding 8.125% senior notes due 2020 were repurchased, as well as for general corporate purposes. The net proceeds from the issuance of the 2027 Notes were used to call \$800 million of the \$1.4 billion aggregate principal amount of CCO Holdings' outstanding 7.000% senior notes due 2019. These debt repurchases resulted in a loss on extinguishment of debt of \$123 million for the year ended December 31, 2015.

The Company also recorded a loss on extinguishment of debt of approximately \$5 million for the year ended December 31, 2015 as a result of the repayment of debt upon termination of the proposed transactions with Comcast Corporation ("Comcast").

#### CCO Holdings Notes

The CCO Holdings notes are senior debt obligations of CCO Holdings and CCO Holdings Capital and rank equally with all other current and future unsecured, unsubordinated obligations of CCO Holdings and CCO Holdings Capital. They are structurally subordinated to all obligations of subsidiaries of CCO Holdings.

CCO Holdings may redeem some or all of the CCO Holdings notes at any time at a premium. The optional redemption price declines to 100% of the respective series' principal amount, plus accrued and unpaid interest, if any, on or after varying dates in 2017 through 2024.



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

In addition, at any time prior to varying dates in 2017 through 2021, CCO Holdings may redeem up to 35% (40% in regards to certain notes issued in 2015 and 2016) of the aggregate principal amount of the notes at a premium plus accrued and unpaid interest to the redemption date, with the net cash proceeds of one or more equity offerings (as defined in the indenture); provided that certain conditions are met. In the event of specified change of control events, CCO Holdings must offer to purchase the outstanding CCO Holdings notes from the holders at a purchase price equal to 101% of the total principal amount of the notes, plus any accrued and unpaid interest.

***High-Yield Restrictive Covenants; Limitation on Indebtedness.***

The indentures governing the CCO Holdings notes contain certain covenants that restrict the ability of CCO Holdings, CCO Holdings Capital and all of their restricted subsidiaries to:

- incur additional debt;
- pay dividends on equity or repurchase equity;
- make investments;
- sell all or substantially all of their assets or merge with or into other companies;
- sell assets;
- in the case of restricted subsidiaries, create or permit to exist dividend or payment restrictions with respect to CCO Holdings, guarantee their parent companies debt, or issue specified equity interests;
- engage in certain transactions with affiliates; and
- grant liens.

The above limitations in certain circumstances regarding incurrence of debt, payment of dividends and making investments contained in the indentures of CCO Holdings permit CCO Holdings and its restricted subsidiaries to perform the above, so long as, after giving pro forma effect to the above, the leverage ratio would be below a specified level for the issuer. The leverage ratio under the indentures is 6.0 to 1.0.

**Charter Operating Notes**

The Charter Operating notes are guaranteed by CCO Holdings, TWC, LLC (as defined below), TWCE (as defined below) and substantially all of the operating subsidiaries of Charter Operating (collectively, the "Subsidiary Guarantors"). In addition, the Charter Operating notes are secured by a perfected first priority security interest in substantially all of the assets of Charter Operating to the extent such liens can be perfected under the Uniform Commercial Code by the filing of a financing statement and the liens rank equally with the liens on the collateral securing obligations under the Charter Operating credit facilities. Charter Operating may redeem some or all of the Charter Operating notes at any time at a premium.

The Charter Operating notes are subject to the terms and conditions of the indenture governing the Charter Operating notes. The Charter Operating notes contain customary representations and warranties and affirmative covenants with limited negative covenants. The Charter Operating indenture also contains customary events of default.

**Charter Operating Credit Facilities**

The Charter Operating credit facilities have an outstanding principal amount of \$8.9 billion at December 31, 2016 as follows:

- term loan A with a remaining principal amount of \$2.5 billion, which is repayable in quarterly installments and aggregating \$132 million in 2017 and 2018, \$231 million in 2019 and \$264 million in 2020, with the remaining balance due at final maturity on May 18, 2021. Pricing on term loan A is LIBOR plus 1.75%;
- term loan E with a remaining principal amount of approximately \$1.4 billion, which is repayable in equal quarterly installments and aggregating \$15 million in each loan year, with the remaining balance due at final maturity on July 1, 2020. Pricing on term loan E is LIBOR plus 2.25% with a LIBOR floor of 0.75% (see Note 25 for amendments to the Charter Operating credit facilities completed in 2017);
- term loan F with a remaining principal amount of approximately \$1.2 billion, which is repayable in equal quarterly installments and aggregating \$12 million in each loan year, with the remaining balance due at final maturity on January



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
**(dollars in millions, except share or per share data or where indicated)**

- 3, 2021. Pricing on term loan F is LIBOR plus 2.25% with a LIBOR floor of 0.75% (see Note 25 for amendments to the Charter Operating credit facilities completed in 2017);
- term loan H with a remaining principal amount of approximately \$993 million, which is repayable in equal quarterly installments and aggregating \$10 million in each loan year, with the remaining balance due at final maturity on January 15, 2022. Pricing on term loan H is LIBOR plus 2.00%;
  - term loan I with a remaining principal amount of approximately \$2.8 billion, which is repayable in equal quarterly installments and aggregating \$28 million in each loan year, with the remaining balance due at final maturity on January 15, 2024. Pricing on term loan I is LIBOR plus 2.25%; and
  - revolving loan allowing for borrowings of up to \$3.0 billion, maturing on May 18, 2021. Pricing on the revolving loan is LIBOR plus 1.75% with a commitment fee of 0.30%. As of December 31, 2016, \$220 million of the revolving loan was utilized to collateralize a like principal amount of letters of credit out of \$278 million of letters of credit issued on the Company's behalf.

Amounts outstanding under the Charter Operating credit facilities bear interest, at Charter Operating's election, at a base rate or LIBOR (0.77% and 0.42% as of December 31, 2016 and December 31, 2015, respectively), as defined, plus an applicable margin.

The Charter Operating credit facilities also allow us to enter into incremental term loans in the future, with amortization as set forth in the notices establishing such term loans. Although the Charter Operating credit facilities allow for the incurrence of a certain amount of incremental term loans subject to pro forma compliance with its financial maintenance covenants, no assurance can be given that the Company could obtain additional incremental term loans in the future if Charter Operating sought to do so or what amount of incremental term loans would be allowable at any given time under the terms of the Charter Operating credit facilities.

The obligations of Charter Operating under the Charter Operating credit facilities are guaranteed by the Subsidiary Guarantors. The obligations are also secured by (i) a lien on substantially all of the assets of Charter Operating and the Subsidiary Guarantors, to the extent such lien can be perfected under the Uniform Commercial Code by the filing of a financing statement, and (ii) a pledge by CCO Holdings of the equity interests owned by it in any of Charter Operating's subsidiaries, as well as intercompany obligations owing to it by any of such entities.

#### ***Restrictive Covenants***

The Charter Operating credit facilities contain representations and warranties, and affirmative and negative covenants customary for financings of this type. The financial covenants measure performance against standards set for leverage to be tested as of the end of each quarter. The Charter Operating credit facilities contain provisions requiring mandatory loan prepayments under specific circumstances, including in connection with certain sales of assets, so long as the proceeds have not been reinvested in the business. Additionally, the Charter Operating credit facilities provisions contain an allowance for restricted payments so long as the consolidated leverage ratio is no greater than 3.5 after giving pro forma effect to such restricted payment. The Charter Operating credit facilities permit Charter Operating and its subsidiaries to make distributions to pay interest on the currently outstanding subordinated and parent company indebtedness, provided that, among other things, no default has occurred and is continuing under the Charter Operating credit facilities. The Charter Operating credit facilities also contain customary events of default.

#### **Assumed Legacy TWC Indebtedness**

The Company assumed approximately \$22.4 billion in aggregate principal amount of Time Warner Cable, LLC (successor to Legacy TWC outstanding debt obligations, "TWC, LLC") senior notes and debentures and Time Warner Cable Enterprises LLC ("TWCE") senior debentures with varying maturities. The Company applied acquisition accounting to Legacy TWC, and as a result, the debt assumed was adjusted to fair value using quoted market values as of the closing date. This fair value adjustment resulted in recognition of a net debt premium of approximately \$2.4 billion.

#### ***TWC, LLC Senior Notes and Debentures***

The TWC, LLC senior notes and debentures are guaranteed by CCO Holdings, Charter Operating, TWCE and the Subsidiary Guarantors and rank equally with the liens on the collateral securing obligations under the Charter Operating notes and credit facilities. Interest on each series of TWC, LLC senior notes and debentures is payable semi-annually (with the exception of the Sterling Notes, which is payable annually) in arrears.



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

The TWC, LLC indenture contains customary covenants relating to restrictions on the ability of TWC, LLC or any material subsidiary to create liens and on the ability of TWC, LLC and TWCE to consolidate, merge or convey or transfer substantially all of their assets. The TWC, LLC indenture also contains customary events of default.

The TWC, LLC senior notes and debentures may be redeemed in whole or in part at any time at TWC, LLC's option at a redemption price equal to the greater of (i) all of the applicable principal amount being redeemed and (ii) the sum of the present values of the remaining scheduled payments on the applicable TWC, LLC senior notes and debentures discounted to the redemption date on a semi-annual basis (with the exception of the Sterling Notes, which are on an annual basis), at a comparable government bond rate plus a designated number of basis points as further described in the indenture and the applicable note or debenture, plus, in each case, accrued but unpaid interest to, but not including, the redemption date.

The Company may offer to redeem all, but not less than all, of the Sterling Notes in the event of certain changes in the tax laws of the U.S. (or any taxing authority in the U.S.). This redemption would be at a redemption price equal to 100% of the principal amount, together with accrued and unpaid interest on the Sterling Notes to, but not including, the redemption date.

#### *TWCE Senior Debentures*

The TWCE senior debentures are guaranteed by CCO Holdings, Charter Operating, TWC, LLC and the Subsidiary Guarantors and rank equally with the liens on the collateral securing obligations under the Charter Operating notes and credit facilities. Interest on each series of TWCE senior debentures is payable semi-annually in arrears. The TWCE senior debentures are not redeemable before maturity.

The TWCE indenture contains customary covenants relating to restrictions on the ability of TWCE or any material subsidiary to create liens and on the ability of TWC, LLC and TWCE to consolidate, merge or convey or transfer substantially all of their assets. The TWCE indenture also contains customary events of default.

#### **Limitations on Distributions**

Distributions by the Company's subsidiaries to a parent company for payment of principal on parent company notes are restricted under the indentures and credit facilities discussed above, unless there is no default under the applicable indenture and credit facilities, and unless each applicable subsidiary's leverage ratio test is met at the time of such distribution. As of December 31, 2016, there was no default under any of these indentures or credit facilities and each subsidiary met its applicable leverage ratio tests based on December 31, 2016 financial results. Such distributions would be restricted, however, if any such subsidiary fails to meet these tests at the time of the contemplated distribution. In the past, certain subsidiaries have from time to time failed to meet their leverage ratio test. There can be no assurance that they will satisfy these tests at the time of the contemplated distribution. Distributions by Charter Operating for payment of principal on parent company notes are further restricted by the covenants in its credit facilities.

However, without regard to leverage, during any calendar year or any portion thereof during which the borrower is a flow-through entity for tax purposes, and so long as no event of default exists, the borrower may make distributions to the equity interests of the borrower in an amount sufficient to make permitted tax payments.

In addition to the limitation on distributions under the various indentures, distributions by the Company's subsidiaries may be limited by applicable law, including the Delaware Limited Liability Company Act, under which the Company's subsidiaries may make distributions if they have "surplus" as defined in the act.

#### **Liquidity and Future Principal Payments**

The Company continues to have significant amounts of debt, and its business requires significant cash to fund principal and interest payments on its debt, capital expenditures and ongoing operations. As set forth below, the Company has significant future principal payments. The Company continues to monitor the capital markets, and it expects to undertake refinancing transactions and utilize free cash flow and cash on hand to further extend or reduce the maturities of its principal obligations. The timing and terms of any refinancing transactions will be subject to market conditions.



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Based upon outstanding indebtedness as of December 31, 2016, the amortization of term loans, and the maturity dates for all senior and subordinated notes, total future principal payments on the total borrowings under all debt agreements as of December 31, 2016, are as follows:

<b>Year</b>	<b>Amount</b>
2017	\$ 2,197
2018	2,197
2019	3,546
2020	5,216
2021	5,128
Thereafter	41,752
	<u>\$ 60,036</u>

#### 10. Common Stock

Charter's Class A common stock and Class B common stock are identical except with respect to certain voting, transfer and conversion rights. Holders of Class A common stock are entitled to one vote per share. Charter's Class B common stock represents the share issued to A/N in connection with the Bright House Transaction. One share of Charter's Class B common stock has a number of votes reflecting the voting power of the Charter Holdings common units and Charter Holdings convertible preferred units held by A/N as of the applicable record date on an if-converted, if-exchanged basis, and is generally intended to reflect A/N's economic interests in Charter Holdings.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

The following table summarizes our shares outstanding for the three years ended December 31, 2016:

	Class A Common Stock	Class B Common Stock
BALANCE, December 31, 2013	106,144,075	—
Exercise of stock options	640,342	—
Restricted stock issuances, net of cancellations	9,090	—
Stock issuances from exercise of warrants	5,243,167	—
Restricted stock unit vesting	104,270	—
Purchase of treasury stock	(141,257)	—
BALANCE, December 31, 2014	111,999,687	—
Exercise of stock options	579,173	—
Restricted stock issuances, net of cancellations	6,920	—
Restricted stock unit vesting	98,831	—
Purchase of treasury stock	(245,783)	—
BALANCE, December 31, 2015	112,438,828	—
Reorganization of common stock	(10,771,404)	—
Issuance of shares in TWC Transaction	143,012,155	—
Issuance of shares to Liberty Broadband for cash	25,631,339	—
Issuance of share to A/N in Bright House Transaction	—	1
Exchange of Charter Holdings units held by A/N	1,852,832	—
Exercise of stock options	1,014,664	—
Restricted stock issuances, net of cancellations	9,811	—
Restricted stock unit vesting	1,738,792	—
Purchase of treasury stock	(6,029,225)	—
BALANCE, December 31, 2016	268,897,792	1

The shares outstanding balances shown above as of and prior to December 31, 2015 represent historical shares outstanding of Legacy Charter before applying the Parent Merger Exchange Ratio. The 10.8 million shares associated with the reorganization of Charter Class A common stock represents the reduction to Legacy Charter Class A common shares outstanding as of the acquisition date as a result of applying the Parent Merger Exchange Ratio. See Note 2.

In December 2016, A/N exchanged 1.9 million Charter Holdings common units for Charter Class A common stock. See Note 11.

### *Share Repurchases*

In 2016, the Company purchased approximately 5.1 million shares of Charter Class A common stock for approximately \$1.3 billion pursuant to authorizations by Charter's board of directors of \$3 billion. Accordingly, as of December 31, 2016 and provided Charter's leverage ratio remains at 4 to 4.5 times and Charter Operating's leverage remains below 3.5 times, management has authority to cause the Company to purchase an additional \$1.7 billion of Charter's Class A common stock without taking into account shares or units that may be purchased from A/N. Effective November 1, 2016, Charter's board of directors granted authority for a new \$750 million of Class A common stock buybacks under the rolling six-month authority without taking into account any Class A common stock purchased prior to November 1. As a result, a portion of the \$1.7 billion of authority is under the authority of management to approve up to \$750 million for Class A common stock buybacks in any six-month period.

During the years ended December 31, 2016, 2015 and 2014, the Company withheld 908,066, 177,696 and 127,725 shares, respectively, of its common stock in payment of \$216 million, \$38 million and \$19 million, respectively, of tax withholdings owed by employees

upon vesting of restricted shares and stock options. During the years ended December 31, 2016 and 2015, Company

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

also withheld 50,503 shares and 44,541 shares, respectively, of its Class A common stock representing the exercise costs owed by employees upon exercise of stock options.

In December 31, 2016 and 2015, Charter's board of directors approved the retirement of the then currently outstanding treasury stock and those shares were retired as of December 31, 2016 and 2015.

The Company accounted for treasury stock using the cost method and the treasury shares upon repurchase were reflected on the Company's consolidated balance sheets as a component of total shareholders' equity. Upon retirement, these treasury shares are allocated between additional paid-in capital and accumulated deficit based on the cost of original issue included in additional paid-in capital.

In 2014, the Company issued approximately 5.2 million shares of Charter Class A common stock as a result of exercises by holders who received warrants pursuant to the Joint Plan of Reorganization upon the Company's emergence from bankruptcy in 2009. The exercises resulted in proceeds to the Company of approximately \$90 million. As of December 31, 2016 and 2015, there were no warrants outstanding.

#### **11. Noncontrolling Interests**

Noncontrolling interests represents consolidated subsidiaries of which the Company owns less than 100%. The Company is a holding company whose principal asset is a controlling equity interest in Charter Holdings, the indirect owner of the Company's cable systems. Noncontrolling interests on the Company's balance sheet primarily includes A/N's equity interests in Charter Holdings, which is comprised of a common ownership interest and a convertible preferred ownership interest.

In connection with the closing of the Bright House Transaction, Charter Holdings issued approximately 31.0 million common units to A/N, which are exchangeable at any time into either Charter Class A common stock on a one-for-one basis, or, at Charter's option, cash, based on the then current market price of Charter Class A common stock. Net income (loss) of Charter Holdings attributable to A/N's common noncontrolling interest for financial reporting purposes is based on the weighted average effective common ownership interest of approximately 10% which was \$129 million for the year ended December 31, 2016. Charter Holdings distributed \$3 million to A/N as a pro rata tax distribution on its common units during the year ended December 31, 2016. Charter Holdings also issued approximately 25 million convertible preferred units to A/N with a face amount of \$2.5 billion that pay a 6% annual preferred dividend. The 6% annual preferred dividend is paid quarterly in cash, if and when declared, provided that, if dividends are suspended at any time, the dividends will accrue until they are paid. Net income (loss) of Charter Holdings attributable to the preferred noncontrolling interest for financial reporting purposes is based on the preferred dividend which was \$93 million for the year ended December 31, 2016. Each convertible preferred unit is convertible into either 0.37334 of a Charter Holdings common unit (if then held by A/N) or 0.37334 of a share of Charter Class A common stock (if then held by a third party), representing a conversion price of \$267.85 per unit, based on a conversion feature as defined in the Limited Liability Company Agreement of Charter Holdings. After May 18, 2021, Charter may redeem the convertible preferred units if the price of Charter Class A common stock exceeds 130% of the conversion price. These Charter Holdings common and convertible preferred units held by A/N are recorded in noncontrolling interests as permanent equity in the consolidated balance sheet.

The common units and convertible preferred units issued to A/N as consideration for the Bright House Transaction were initially measured at their fair value of \$7.0 billion and \$3.2 billion, respectively, in accordance with acquisition accounting. However, upon formation of Charter Holdings and subsequent to the acquisition, the carrying amounts of the controlling and noncontrolling interests were adjusted to reflect the relative effective common ownership interest in Charter Holdings. This resulted in an increase to noncontrolling interest of approximately \$589 million and a corresponding decrease to additional paid-in capital of \$589 million, net of \$225 million of deferred income taxes, for the year ended December 31, 2016.

In December 2016, Charter and A/N entered into a letter agreement (the "Letter Agreement") pursuant to which A/N exchanged 1.9 million Charter Holdings common units held by A/N for shares of Charter Class A common stock for an aggregate purchase price of \$537 million. The common units exchanged had a net carrying value in noncontrolling interest of approximately \$460 million. The exchange of A/N common units resulted in a tax step-up of the assets of Charter Holdings which is further discussed in Note 17. The Letter Agreement also requires A/N to sell to Charter or to Charter Holdings, on a monthly basis, a number of shares of Charter Class A common stock or Charter Holdings common units that represents a pro rata participation by A/N and its affiliates in any repurchases of shares of Charter Class A common stock from persons other than A/N effected by Charter during the immediately preceding calendar month, at a purchase price equal to the average price paid by Charter for the shares repurchased.



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

from persons other than A/N during such immediately preceding calendar month. Pursuant to the Letter Agreement, Charter Holdings purchased from A/N 752,767 Charter Holdings common units at a price per unit of \$289.83, or \$218 million. The common units purchased had a net carrying value in noncontrolling interest of approximately \$187 million. As of December 31, 2016, A/N held 28.4 million Charter Holdings common units.

## 12. Accounting for Derivative Instruments and Hedging Activities

The Company uses derivative instruments to manage interest rate risk on variable debt and foreign exchange risk on the Sterling Notes, and does not hold or issue derivative instruments for speculative trading purposes.

Interest rate derivative instruments are used to manage interest costs and to reduce the Company's exposure to increases in floating interest rates. The Company manages its exposure to fluctuations in interest rates by maintaining a mix of fixed and variable rate debt. Using interest rate derivative instruments, the Company agrees to exchange, at specified intervals through 2017, the difference between fixed and variable interest amounts calculated by reference to agreed-upon notional principal amounts. As of December 31, 2016 and 2015, the Company had \$850 million and \$1.1 billion, respectively, in notional amounts of interest rate derivative instruments outstanding. The notional amounts of interest rate derivative instruments do not represent amounts exchanged by the parties and, thus, are not a measure of exposure to credit loss. The amounts exchanged were determined by reference to the notional amount and the other terms of the contracts.

Upon closing of the TWC Transaction, the Company acquired interest rate derivative instrument assets with a fair value of \$85 million (excluding accrued interest), which were terminated and settled with their respective counterparties in the second quarter of 2016 with an \$88 million cash payment to the Company of which \$14 million was for interest accrued through the date of termination. The termination resulted in an \$11 million loss for the year ended December 31, 2016 which was recorded in gain (loss) on financial instruments, net in the consolidated statements of operations.

Upon closing of the TWC Transaction, the Company assumed cross-currency derivative instrument liabilities with a fair value of \$72 million (excluding accrued interest). Cross-currency derivative instruments are used to effectively convert £1.275 billion aggregate principal amount of fixed-rate British pound sterling denominated debt, including annual interest payments and the payment of principal at maturity, to fixed-rate U.S. dollar denominated debt. The cross-currency swaps have maturities of June 2031 and July 2042. The Company is required to post collateral on the cross-currency derivative instruments when the derivative contracts are in a liability position. In May 2016, the Company entered into a collateral holiday agreement for 80% of both the 2031 and 2042 cross-currency swaps, which eliminates the requirement to post collateral for three years.

The effect of derivative instruments on the consolidated balance sheets is presented in the table below:

	December 31,	
	2016	2015
<b>Interest Rate Derivatives</b>		
Accrued interest	\$ 5	\$ 3
Other long-term liabilities	\$ —	\$ 10
Accumulated other comprehensive loss	\$ (5)	\$ (13)
<b>Cross-Currency Derivatives</b>		
Other long-term liabilities	\$ 251	\$ —

The Company's interest rate and cross-currency derivative instruments are not designated as hedges and are marked to fair value each period, with the impact recorded as a gain or loss on financial instruments, net in the consolidated statements of operations. While these derivative instruments are not designated as cash flow hedges for accounting purposes, management continues to believe such instruments are correlated with the respective debt, thus managing associated risk.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

The effect of financial instruments on the consolidated statements of operations is presented in the table below.

	Year Ended December 31,		
	2016	2015	2014
<b>Gain (Loss) on Financial Instruments, Net:</b>			
Change in fair value of interest rate derivative instruments	\$ 8	\$ 5	\$ 12
Change in fair value of cross-currency derivative instruments	(179)	—	—
Remeasurement of Sterling Notes to U.S. dollars	279	—	—
Loss on termination of interest rate derivative instruments	(11)	—	—
Loss reclassified from accumulated other comprehensive loss due to discontinuance of hedge accounting	(8)	(9)	(19)
	<u>\$ 89</u>	<u>\$ (4)</u>	<u>\$ (7)</u>

### 13. Fair Value Measurements

The accounting guidance establishes a three-level hierarchy for disclosure of fair value measurements, based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date, as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 – inputs to the valuation methodology are unobservable and significant to the fair value measurement.

#### *Financial Assets and Liabilities*

The Company has estimated the fair value of its financial instruments as of December 31, 2016 and 2015 using available market information or other appropriate valuation methodologies. Considerable judgment, however, is required in interpreting market data to develop the estimates of fair value. Accordingly, the estimates presented in the accompanying consolidated financial statements are not necessarily indicative of the amounts the Company would realize in a current market exchange.

The carrying amounts of cash and cash equivalents, receivables, payables and other current assets and liabilities approximate fair value because of the short maturity of those instruments.

The Company's cash and cash equivalents as of December 31, 2016 and restricted cash and cash equivalents as of December 31, 2015 were primarily invested in money market funds and 90 day or less commercial paper. The money market funds are valued at the closing price reported by the fund sponsor from an actively traded exchange and commercial paper is valued at cost plus the accretion of the discount on a yield to maturity basis, which approximated fair value. The money market funds and commercial paper potentially subject the Company to concentration of credit risk. The amount invested within any one financial instrument did not exceed \$250 million and \$1.5 billion as of December 31, 2016 and December 31, 2015, respectively. As of December 31, 2016 and 2015, there were no significant concentrations of financial instruments in a single investee, industry or geographic location.

Interest rate derivative instruments are valued using a present value calculation based on an implied forward LIBOR curve (adjusted for Charter Operating's and counterparties' credit risk). The weighted average pay rate for the Company's currently effective interest rate derivative instruments was 1.59% and 1.61% at December 31, 2016 and 2015, respectively (exclusive of applicable spreads).

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

The Company's financial instruments that are accounted for at fair value on a recurring basis are presented in the table below.

	December 31, 2016		December 31, 2015	
	Level 1	Level 2	Level 1	Level 2
<b>Assets</b>				
Money market funds	\$ 1,205	\$ —	\$ 14,330	\$ —
Commercial paper	\$ —	\$ —	\$ —	\$ 7,934
<b>Liabilities</b>				
Interest rate derivative instruments	\$ —	\$ 5	\$ —	\$ 13
Cross-currency derivative instruments	\$ —	\$ 251	\$ —	\$ —

A summary of the carrying value and fair value of the Company's debt at December 31, 2016 and 2015 is as follows:

	December 31, 2016		December 31, 2015	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<b>Debt</b>				
Senior notes and debentures	\$ 52,933	\$ 55,203	\$ 28,433	\$ 28,744
Credit facilities	\$ 8,814	\$ 8,943	\$ 7,290	\$ 7,274

The estimated fair value of the Company's senior notes and debentures as of December 31, 2016 and 2015 is based on quoted market prices in active markets and is classified within Level 1 of the valuation hierarchy, while the estimated fair value of the Company's credit facilities is based on quoted market prices in inactive markets and is classified within Level 2.

#### *Non-financial Assets and Liabilities*

The Company's nonfinancial assets such as equity-method investments, franchises, property, plant, and equipment, and other intangible assets are not measured at fair value on a recurring basis; however, they are subject to fair value adjustments in certain circumstances, such as upon a business combination and when there is evidence that an impairment may exist. No impairments were recorded in 2016, 2015 and 2014. Upon closing of the Transactions, all of Legacy TWC and Legacy Bright House nonfinancial assets and liabilities were recorded at fair values. See Note 2.

#### **14. Operating Costs and Expenses**

Operating costs and expenses, exclusive of items shown separately in the consolidated statements of operations, consist of the following for the periods presented:

	Year Ended December 31,		
	2016	2015	2014
Programming	\$ 7,034	\$ 2,678	\$ 2,459
Regulatory, connectivity and produced content	1,467	435	428
Costs to service customers	5,173	1,705	1,679
Marketing	1,699	628	617
Transition costs	156	72	14
Other	3,126	908	776
	\$ 18,655	\$ 6,426	\$ 5,973



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Programming costs consist primarily of costs paid to programmers for basic, premium, digital, video on demand, and pay-per-view programming. Regulatory, connectivity and produced content costs represent payments to franchise and regulatory authorities, costs directly related to providing video, Internet and voice services as well as payments for sports, local and news content produced by the Company. Included in regulatory, connectivity and produced content costs is content acquisition costs for the Los Angeles Lakers' basketball games and Los Angeles Dodgers' baseball games which are recorded as games are exhibited over the applicable season. Costs to service customers include costs related to field operations, network operations and customer care for the Company's residential and small and medium business customers, including internal and third-party labor for installations, service and repairs, maintenance, billing and collection, occupancy and vehicle costs. Marketing costs represent the costs of marketing to current and potential commercial and residential customers including labor costs. Transition costs represent incremental costs incurred to integrate the TWC and Bright House operations and to increase the scale of the Company's business as a result of the Transactions. See Note 2. Other includes bad debt expense, corporate overhead, advertising sales expenses, indirect costs associated with the Company's enterprise business customers and regional sports and news networks, property tax expense and insurance expense and stock compensation expense, among others.

**15. Other Operating Expenses, Net**

Other operating expenses, net consist of the following for the years presented:

	Year Ended December 31,		
	2016	2015	2014
Merger and restructuring costs	\$ 970	\$ 70	\$ 38
Other pension benefits	(899)	—	—
Special charges, net	17	15	14
(Gain) loss on sale of assets, net	(2)	4	10
	<u>\$ 86</u>	<u>\$ 89</u>	<u>\$ 62</u>

*Merger and restructuring costs*

Merger and restructuring costs represent costs incurred in connection with merger and acquisition transactions and related restructuring, such as advisory, legal and accounting fees, employee retention costs, employee termination costs related to the Transactions and other exit costs. The Company expects to incur additional merger and restructuring costs in connection with the Transactions. Changes in accruals for merger and restructuring costs from January 1, 2016 through December 31, 2016 are presented below:

	Employee Retention Costs	Employee Termination Costs	Transaction and Advisory Costs	Other Costs	Total
Liability, December 31, 2015	\$ —	\$ —	\$ 33	\$ —	\$ 33
Liability assumed in the Transactions	80	9	3	—	92
Costs incurred	26	337	318	41	722
Cash paid	(99)	(102)	(329)	(41)	(571)
Remaining liability, December 31, 2016	<u>\$ 7</u>	<u>\$ 244</u>	<u>\$ 25</u>	<u>\$ —</u>	<u>\$ 276</u>

In addition to the costs indicated above, the Company recorded \$248 million of expense related to accelerated vesting of equity awards of terminated employees for the year ended December 31, 2016.

*Other pension benefits*

Other pension benefits include the pension curtailment gain, remeasurement gain, expected return on plan assets and interest cost components of net periodic pension benefit. See Note 21.



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

*Special charges, net*

Special charges, net primarily includes employee termination costs not related to the Transactions and net amounts of litigation settlements.

*(Gain) loss on sale of assets, net*

(Gain) loss on sale of assets, net represents the net (gain) loss recognized on the sales and disposals of fixed assets and cable systems.

**16. Stock Compensation Plans**

Legacy Charter's 2009 Stock Incentive Plan (assumed by Charter upon closing of the Transactions) provides for grants of nonqualified stock options, incentive stock options, stock appreciation rights, dividend equivalent rights, performance units and performance shares, share awards, phantom stock, restricted stock units and restricted stock. Directors, officers and other employees of the Company and its subsidiaries, as well as others performing consulting services for the Company, are eligible for grants under the 2009 Stock Incentive Plan. In April 2016, Charter's board of directors and stockholders approved an additional 9 million shares of Charter Class A common stock (or units convertible into Charter Class A common stock) under the 2009 Stock Incentive Plan which now allows for the issuance of up to 21 million shares of Charter Class A common stock (or units convertible into Charter Class A common stock).

At the closing of the TWC Transaction, Legacy TWC employee equity awards were converted into Charter Class A common stock equity awards on the same terms and conditions as were applicable under the Legacy TWC equity awards, except that the number of shares covered by each award and the option exercise prices were adjusted for the Stock Award Exchange Ratio (as defined in the Merger Agreement) such that the intrinsic value of the Converted TWC Awards was approximately equal to that of the original awards at the closing of the Transactions. The Converted TWC Awards represented approximately 4.2 million Charter restricted stock units and 0.8 million Charter stock options (0.5 million of which were exercisable at the time of conversion) and continue to be subject to the terms of the Legacy TWC equity plans. The Converted TWC Awards were measured at their fair value as of the closing of the TWC Transaction. Of that fair value, \$514 million related to Legacy TWC employee pre-combination service and was treated as consideration transferred in the TWC Transaction (see Note 2), while \$539 million relates to post-combination service and is being amortized to stock compensation expense over the remaining vesting period of the awards. The fair values of the Converted TWC Awards were based on a valuation using assumptions developed by management and other information compiled by management including, but not limited to, historical volatility and exercise trends of Legacy Charter and Legacy TWC. The Parent Merger Exchange Ratio was also applied to outstanding Legacy Charter equity awards and option exercise prices; however, the terms of the equity awards did not change as a result of the Transactions.

Legacy Charter Stock options and restricted stock units cliff vest upon the three year anniversary of each grant. Stock options generally expire ten years from the grant date and restricted stock units have no voting rights. Certain stock options and restricted stock units vest based on achievement of stock price hurdles. Restricted stock generally vests annually over one year beginning from the date of grant. Legacy TWC restricted stock units that were converted into Charter restricted stock units generally vest 50% on each of the third and fourth anniversary of the grant date. Legacy TWC stock options that were converted into Charter stock options vest ratably over a four-year period and expire ten years from the grant date.

As of December 31, 2016, total unrecognized compensation remaining to be recognized in future periods totaled \$262 million for stock options, \$1 million for restricted stock and \$279 million for restricted stock units and the weighted average period over which they are expected to be recognized is 4 years for stock options, 4 months for restricted stock and 3 years for restricted stock units. The Company recorded \$244 million, \$78 million and \$55 million of stock compensation expense for the years ended December 31, 2016, 2015 and 2014, respectively, which is included in operating costs and expenses. The Company also recorded \$248 million of expense for the year ended December 31, 2016 related to accelerated vesting of equity awards of terminated employees which is recorded in merger and restructuring costs.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

A summary of the activity for the Company's stock options (after applying the Parent Merger Exchange Ratio) for the years ended December 31, 2016, 2015 and 2014, is as follows (shares in thousands, except per share data):

	Year Ended December 31,								
	2016			2015			2014		
	Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value	Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value	Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value
Outstanding, beginning of period	3,923	\$ 122.03		3,336	\$ 95.44		2,841	\$ 66.20	
Granted	5,999	\$ 218.91		1,176	\$ 177.14		1,116	\$ 151.24	
Converted TWC Awards	839	\$ 86.46		—	\$ —		—	\$ —	
Exercised	(1,015)	\$ 96.33	\$ 146	(524)	\$ 72.27	\$ 68	(579)	\$ 58.07	\$ 55
Canceled	(154)	\$ 173.98		(65)	\$ 155.23		(42)	\$ 115.65	
Outstanding, end of period	<u>9,592</u>	<u>\$ 181.39</u>	<u>\$ 1,022</u>	<u>3,923</u>	<u>\$ 122.03</u>		<u>3,336</u>	<u>\$ 95.44</u>	
Weighted average remaining contractual life	<u>8</u> years			<u>7</u> years			<u>7</u> years		
Options exercisable, end of period	<u>1,665</u>	<u>\$ 71.71</u>	<u>\$ 360</u>	<u>1,224</u>	<u>\$ 61.88</u>		<u>1,193</u>	<u>\$ 61.76</u>	
Options expected to vest, end of period	<u>7,686</u>	<u>\$ 205.49</u>	<u>\$ 634</u>						
Weighted average fair value of options granted	<u>\$ 47.42</u>			<u>\$ 66.20</u>			<u>\$60.92</u>		

A summary of the activity for the Company's restricted stock (after applying the Parent Merger Exchange Ratio) for the years ended December 31, 2016, 2015 and 2014, is as follows (shares in thousands, except per share data):

	Year Ended December 31,					
	2016		2015		2014	
	Shares	Weighted Average Grant Price	Shares	Weighted Average Grant Price	Shares	Weighted Average Grant Price
Outstanding, beginning of period	197	\$ 65.79	390	\$ 63.30	590	\$ 62.09
Granted	10	\$ 231.83	6	\$ 201.34	8	\$ 153.25
Vested	(197)	\$ 65.79	(199)	\$ 65.16	(208)	\$ 63.43
Canceled	—	\$ —	—	\$ —	—	\$ —
Outstanding, end of period	<u>10</u>	<u>\$ 231.81</u>	<u>197</u>	<u>\$ 65.79</u>	<u>390</u>	<u>\$ 63.30</u>

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

A summary of the activity for the Company's restricted stock units (after applying the Parent Merger Exchange Ratio) for the years ended December 31, 2016, 2015 and 2014, is as follows (shares in thousands, except per share data):

	Year Ended December 31,					
	2016		2015		2014	
	Shares	Weighted Average Grant Price	Shares	Weighted Average Grant Price	Shares	Weighted Average Grant Price
Outstanding, beginning of period	337	\$ 150.96	294	\$ 115.01	260	\$ 82.64
Granted	895	\$ 213.09	148	\$ 179.17	139	\$ 151.00
Converted TWC Awards	4,162	\$ 224.90	—	\$ —	—	\$ —
Vested	(1,739)	\$ 219.60	(90)	\$ 78.65	(94)	\$ 77.67
Canceled	(342)	\$ 219.91	(15)	\$ 155.43	(11)	\$ 124.44
Outstanding, end of period	<u>3,313</u>	<u>\$ 192.41</u>	<u>337</u>	<u>\$ 150.96</u>	<u>294</u>	<u>\$ 115.01</u>

#### 17. Income Taxes

Substantially all of the Company's operations are held through Charter Holdings and its direct and indirect subsidiaries. Charter Holdings and the majority of its subsidiaries are generally limited liability companies that are not subject to income tax. However, certain of these limited liability companies are subject to state income tax. In addition, the subsidiaries that are corporations are subject to income tax. Generally, the taxable income, gains, losses, deductions and credits of Charter Holdings are passed through to its members, Charter and A/N. Charter is responsible for its share of taxable income or loss of Charter Holdings allocated to it in accordance with the LLC Agreement and partnership tax rules and regulations. As a result, Charter's primary deferred tax component recorded in the consolidated balance sheets relates to its excess financial reporting outside basis, excluding amounts attributable to nondeductible goodwill, over Charter's tax basis in the investment in Charter Holdings.

Charter Holdings, the indirect owner of the Company's cable systems, generally allocates its taxable income, gains, losses, deductions and credits proportionately according to the members' respective ownership interests, except for special allocations required under Section 704(c) of the Internal Revenue Code and the Treasury Regulations ("Section 704(c)"). Pursuant to Section 704(c) and the LLC Agreement, each item of income, gain, loss and deduction with respect to any property contributed to the capital of the partnership shall, solely for tax purposes, be allocated among the members so as to take into account any variation between the adjusted basis of such property to the partnership for U.S. federal income tax purposes and its initial gross asset value using the "traditional method" as described in the Treasury Regulations.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

*Income Tax Benefit (Expense)*

For the years ended December 31, 2016, 2015, and 2014, the Company recorded deferred income tax benefit (expense) as shown below. The tax provision in future periods will vary based on current and future temporary differences, as well as future operating results.

	Year Ended December 31,		
	2016	2015	2014
Current expense:			
Federal income taxes	\$ (4)	\$ (1)	\$ (1)
State income taxes	(29)	(4)	(2)
Current income tax expense	<u>(33)</u>	<u>(5)</u>	<u>(3)</u>
Deferred benefit (expense):			
Federal income taxes	2,549	53	(192)
State income taxes	409	12	(41)
Deferred income tax benefit (expense)	<u>2,958</u>	<u>65</u>	<u>(233)</u>
Income tax benefit (expense)	<u>\$ 2,925</u>	<u>\$ 60</u>	<u>\$ (236)</u>

Income tax benefit for the year ended December 31, 2016 was recognized primarily through the reversal of approximately \$3.3 billion of valuation allowance (see further discussion below), net of tax effect of permanent differences, a decrease to the anticipated blended state rate applied to Legacy Charter deferred tax balances as a result of the Transactions, a change in a state tax law, and prior to the closing of the Transactions, increases (decreases) in deferred tax liabilities related to Charter's franchises which are characterized as indefinite-lived for book financial reporting purposes.

Prior to July 2, 2015, Charter Communications Holding Company, LLC ("Charter Holdco") was treated as a partnership for tax purposes. Effective on July 2, 2015, Charter elected to treat two of its wholly owned subsidiaries as disregarded entities for federal and state income tax purposes (the "Election"). The subsidiaries that made the Election were two of the three partners in Charter Holdco. This Election resulted in a deemed liquidation of Charter Holdco into Charter solely for federal and state income tax purposes, and resulted in a net increase of \$638 million to the tax basis of Charter Holdco's amortizable and depreciable assets. After the Election, all taxable income, gains, losses, deductions and credits of Charter Holdco and its indirect limited liability company subsidiaries were treated as income of Charter. In addition, the indirect subsidiaries of Charter Holdco that are corporations joined the Charter consolidated group. The impact of the Election to the Charter income tax provision, net of valuation allowance, was \$187 million of income tax benefit recorded as a discrete tax event during the year ended December 31, 2015.

The Company's effective tax rate differs from that derived by applying the applicable federal income tax rate of 35% for the years ended December 31, 2016, 2015, and 2014, respectively, as follows:

	Year Ended December 31,		
	2016	2015	2014
Statutory federal income taxes	\$ (288)	\$ 116	\$ (18)
Statutory state income taxes, net	(36)	(4)	(2)
Nondeductible expenses	(62)	(12)	(10)
Net income attributable to noncontrolling interest	78	—	—
Change in valuation allowance	3,171	(250)	(203)
Organizational restructuring	—	187	—
Federal tax credits	16	18	—
State rate changes	65	4	(3)

7/20/2017

Document

Other

(19)

1-

—

Income tax benefit (expense)

\$ 2,925

\$ 60

\$ (236)

F- 38

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

The change in the valuation allowance above differs from the change between the beginning and ending deferred tax position due to a change in deferred tax assets and the establishment of a valuation allowance on the net operating losses which results in no impact to the consolidated statements of operations.

*Deferred Tax Assets (Liabilities)*

The tax effects of these temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 2016 and 2015 are presented below.

	December 31,	
	2016	2015
Deferred tax assets:		
Loss carryforwards	\$ 4,127	\$ 4,247
Goodwill	—	315
Other intangibles	—	211
Accrued and other	243	227
Total gross deferred tax assets	4,370	5,000
Less: valuation allowance	(200)	(3,186)
Deferred tax assets	\$ 4,170	\$ 1,814
Deferred tax liabilities:		
Investment in partnership	\$ (30,832)	\$ —
Indefinite-lived intangibles	—	(1,582)
Property, plant and equipment	—	(1,822)
Accrued and other	(3)	—
Deferred tax liabilities	(30,835)	(3,404)
Net deferred tax liabilities	\$ (26,665)	\$ (1,590)

Net deferred tax liabilities included approximately \$25 million and \$28 million at December 31, 2016 and 2015, respectively, relating to certain indirect subsidiaries that file separate income tax returns.

*Valuation Allowance*

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will be realized. In evaluating the need for a valuation allowance, management takes into account various factors, including the expected level of future taxable income, available tax planning strategies and reversals of existing taxable temporary differences. Due to Legacy Charter's history of losses, Legacy Charter was historically unable to assume future taxable income in its analysis and accordingly valuation allowances were established against the deferred tax assets, net of deferred tax liabilities, from definite-lived assets for book accounting purposes. However, as a result of the TWC Transaction, deferred tax liabilities resulting from the book fair value adjustment increased significantly and future taxable income that will result from the reversal of existing temporary differences for which deferred tax liabilities are recognized, is sufficient to conclude it is more likely than not that the Company will realize substantially all of its deferred tax assets. As a result, Charter reversed approximately \$3.3 billion of its valuation allowance and recognized a corresponding income tax benefit in the consolidated statements of operations for the year ended December 31, 2016. Approximately \$145 million of valuation allowance associated with federal tax net operating loss carryforwards acquired in the TWC Transaction and approximately \$55 million of valuation allowance associated with state tax loss carryforwards and other miscellaneous deferred tax assets remains on the December 31, 2016 consolidated balance sheet.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

*Net Operating Loss Carryforwards*

As of December 31, 2016, Charter had approximately \$11.2 billion of federal tax net operating loss carryforwards resulting in a gross deferred tax asset of approximately \$3.9 billion. Federal tax net operating loss carryforwards expire in the years 2018 through 2035. These losses resulted from the operations of Charter Holdco and its subsidiaries. In addition, as of December 31, 2016, Charter had state tax net operating loss carryforwards, resulting in a gross deferred tax asset (net of federal tax benefit) of approximately \$304 million. State tax net operating loss carryforwards generally expire in the years 2017 through 2035.

Upon closing of the TWC Transaction, Charter experienced a third "ownership change" as defined in Section 382 of the Internal Revenue Code; resulting in a third set of limitations on Charter's use of its existing federal and state net operating losses, capital losses, and tax credit carryforwards. Both the first ownership change limitations that applied as a result of Legacy Charter's emergence from bankruptcy in 2009 and second ownership change limitations that applied as a result of Liberty Media Corporation's purchase in 2013 of a 27% beneficial interest in Legacy Charter will also continue to apply. As of December 31, 2016, all of Charter's federal tax loss carryforwards are subject to Section 382 and other restrictions. Pursuant to these restrictions, Charter estimates that approximately \$5.4 billion in 2017, \$3.8 billion in 2018, \$432 million in 2019 and an additional \$226 million annually over each of the next five years of federal tax loss carryforwards should become unrestricted and available for Charter's use. An additional \$415 million is currently subject to a valuation allowance. Since the limitation amounts accumulate for future use to the extent they are not utilized in any given year, Charter believes its loss carryforwards should become fully available to offset future taxable income. Charter's state loss carryforwards are subject to similar, but varying, limitations on their future use. If Charter was to experience another "ownership change" in the future, its ability to use its loss carryforwards could be subject to further limitations.

*Tax Receivable Agreement*

Under the LLC Agreement, A/N has rights to: (1) convert at any time some or all of its preferred units in Charter Holdings for common units in Charter Holdings, and (2) exchange at any time some or all of its common units in Charter Holdings for Charter's Class A common stock or cash, at Charter's option. Pursuant to a Tax Receivable Agreement ("TRA") between Charter and A/N, Charter must pay to A/N 50% of the tax benefit when realized by Charter from the step-up in tax basis resulting from any future exchange or sale of the preferred and common units. Charter did not record a liability for this obligation as of the acquisition date since the tax benefit is dependent on uncertain future events that are outside of Charter's control, such as the timing of a conversion or exchange. A future exchange or sale is not based on a fixed and determinable date and the exchange or sale is not certain to occur. If all of A/N's partnership units were to be exchanged or sold in the future, the undiscounted value of the obligation is currently estimated to be in the range of zero to \$3 billion depending on measurement of the tax step-up in the future and Charter's ability to realize the tax benefit in the periods following the exchange or sale. Factors impacting these calculations include, but are not limited to, the fair value of the equity at the time of the exchange and the effective tax rates when the benefits are realized.

In connection with the Letter Agreement between Charter and A/N whereby 1.9 million Charter Holdings common units held by A/N were exchanged for shares of Charter Class A common stock for an aggregate purchase price of \$537 million, an immediate step-up of \$580 million in the tax basis of the assets of Charter Holdings occurred. As it relates to the exchange and tax step-up, a net deferred tax asset of approximately \$82 million was recorded and a resulting TRA liability owed to A/N of \$137 million which, as a transaction with a shareholder, was recorded directly to additional paid in capital. The TRA liability is recorded on an iterative, undiscounted basis and included in other long-term liabilities on the consolidated balance sheets as of December 31, 2016.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

*Uncertain Tax Positions*

In connection with the TWC Transaction, the Company assumed \$181 million of gross unrecognized tax benefits, exclusive of interest and penalties, which are recorded within other long-term liabilities. The net amount of the unrecognized tax benefits that could impact the effective tax rate is \$154 million. The Company has determined that it is reasonably possible that its existing reserve for uncertain tax positions as of December 31, 2016 could decrease by \$35 million during the year ended December 31, 2017 related to various ongoing audits, settlement discussions and expiration of statute of limitations with various state and local agencies; however, various events could cause the Company's current expectations to change in the future. These uncertain tax positions, if ever recognized in the financial statements, would be recorded in the consolidated statements of operations as part of the income tax provision. A reconciliation of the beginning and ending amount of unrecognized tax benefits, exclusive of interest and penalties, included in other long-term liabilities on the accompanying consolidated balance sheets of the Company is as follows:

BALANCE, December 31, 2014	\$	—
Additions on current year tax positions		5
		<hr/>
BALANCE, December 31, 2015		5
Additions on prior year tax positions		1
Additions on current year tax positions		7
Additions on tax positions assumed in the TWC Transaction		181
Reductions on settlements and expirations with taxing authorities		(22)
		<hr/>
BALANCE, December 31, 2016	\$	<u>172</u>

No tax years for Charter, Charter Holdings, or Charter Communications Holding Company, LLC for income tax purposes, are currently under examination by the IRS. Legacy Charter's tax years ending 2013 through the short period return dated May 17, 2016 remain subject to examination and assessment. Years prior to 2013 remain open solely for purposes of examination of Legacy Charter's loss and credit carryforwards. The IRS is currently examining Legacy TWC's income tax returns for 2011 and 2012. Legacy TWC's tax years ending 2013 through 2015 remain subject to examination and assessment. Prior to Legacy TWC's separation from Time Warner Inc. ("Time Warner") in March 2009 (the "Separation"), Legacy TWC was included in the consolidated U.S. federal and certain state income tax returns of Time Warner. The IRS is currently examining Time Warner's 2008 through 2010 income tax returns. Time Warner's income tax returns for 2005 to 2007, which are periods prior to the Separation, were settled with the exception of an immaterial item that has been referred to the IRS Appeals Division. The Company does not anticipate that these examinations will have a material impact on the Company's consolidated financial position or results of operations. In addition, the Company is also subject to ongoing examinations of the Company's tax returns by state and local tax authorities for various periods. Activity related to these state and local examinations did not have a material impact on the Company's consolidated financial position or results of operations in 2016, nor does the Company anticipate a material impact in the future.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

**18. Earnings (Loss) Per Share**

Basic earnings (loss) per common share is computed by dividing net income (loss) attributable to Charter shareholders by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per common share considers the impact of potentially dilutive securities using the treasury stock and if-converted methods and is based on the weighted average number of shares used for the basic earnings per share calculation, adjusted for the dilutive effect of stock options, restricted stock, restricted stock units, equity awards with market conditions and Charter Holdings convertible preferred units and common units. Weighted average number of shares outstanding for all periods presented has been recast to reflect the application of the Parent Merger Exchange Ratio. Basic loss per common share equaled diluted loss per common share for the years ended December 31, 2015 and 2014 because the Company incurred a net loss during those periods. The following is the computation of diluted earnings per common share for the year ended December 31, 2016.

	<b>2016</b>
Numerator:	
Net income attributable to Charter shareholders	\$ 3,522
Effect of dilutive securities:	
Charter Holdings common units	129
Charter Holdings convertible preferred units	93
Net income attributable to Charter shareholders after assumed conversions	\$ 3,744
Denominator:	
Weighted average common shares outstanding, basic	206,539,100
Effect of dilutive securities:	
Assumed exercise or issuance of shares relating to stock plans	3,088,871
Weighted average Charter Holdings common units	19,333,227
Weighted average Charter Holdings convertible preferred units	5,830,241
Weighted average common shares outstanding, diluted	234,791,439
Basic earnings per common share attributable to Charter shareholders	\$ 17.05
Diluted earnings per common share attributable to Charter shareholders	\$ 15.94

**19. Related Party Transactions**

The following sets forth certain transactions in which the Company and the directors, executive officers, and affiliates of the Company are involved or, in the case of the management arrangements, subsidiaries that are debt issuers that pay certain of their parent companies for services.

Charter is a party to management arrangements with Spectrum Management Holding Company, LLC ("Spectrum Management") and certain of their subsidiaries. Under these agreements, Charter, Spectrum Management and Charter Holdco provide management services for the cable systems owned or operated by their subsidiaries. Costs associated with providing these services are charged directly to the Company's operating subsidiaries. All other costs incurred on behalf of Charter's operating subsidiaries are considered a part of the management fee. These costs are recorded as a component of operating costs and expenses, in the accompanying consolidated financial statements. The management fee charged to the Company's operating subsidiaries approximated the expenses incurred by Spectrum Management, Charter Holdco and Charter on behalf of the Company's operating subsidiaries in 2016, 2015 and 2014.

***Liberty Broadband and A/N***

On May 23, 2015, in connection with the execution of the Merger Agreement and the amendment of the Contribution Agreement, Charter entered into the Amended and Restated Stockholders Agreement with Liberty Broadband, A/N and Legacy Charter (the "Stockholders Agreement") and the Charter Holdings Limited Liability Operating Agreement ("LLC Agreement") with Liberty



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Broadband and A/N. As of the closing of the Merger Agreement and the Contribution Agreement on May 18, 2016, the Stockholders Agreement replaced Legacy Charter's existing stockholders agreement with Liberty Broadband, dated September 29, 2014, and superseded the amended and restated stockholders agreement among Legacy Charter, Charter, Liberty Broadband and A/N, dated March 31, 2015.

Under the terms of the Stockholders Agreement, the number of Charter's directors is fixed at 13, and includes its chief executive officer. Upon the closing of the Bright House Transaction, two designees selected by A/N became members of the board of directors of Charter and three designees selected by Liberty Broadband continued as members of the board of directors of Charter. The remaining eight directors are not affiliated with either A/N or Liberty Broadband. Each of A/N and Liberty Broadband is entitled to nominate at least one director to each of the committees of Charter's board of directors, subject to applicable stock exchange listing rules and certain specified voting or equity ownership thresholds for each of A/N and Liberty Broadband, and provided that the Nominating and Corporate Governance Committee and the Compensation and Benefit Committee each have at least a majority of directors independent from A/N, Liberty Broadband and the Company (referred to as the "unaffiliated directors"). Each of the Nominating and Corporate Governance Committee and the Compensation and Benefits Committee is currently comprised of three unaffiliated directors and one designee of each of A/N and Liberty Broadband. A/N and Liberty Broadband also have certain other committee designation and other governance rights. Upon the closing of the Bright House Transaction, Mr. Thomas Rutledge, the Company's Chief Executive Officer ("CEO"), became the chairman of the board of Charter.

In December 2016, the Company and A/N entered into the Letter Agreement in which A/N exchanged Charter Holdings common units for shares of Charter Class A common stock and the Company purchased from A/N Charter Holdings common units. The Letter Agreement also requires pro rata participation by A/N and its affiliates in any repurchases of shares of Charter Class A common stock until A/N has sold shares or units totaling \$537 million (\$218 million has already been completed), subject to Liberty Broadband's right of first refusal to purchase shares or units from A/N upon A/N's sale to any third party, excluding the Company. See Note 11 for more information. Pursuant to the TRA between Charter and A/N, Charter must pay to A/N 50% of the tax benefit when realized by Charter from the step-up in tax basis resulting from any future exchange or sale of the preferred and common units. See Note 17 for more information.

The Company is aware that Dr. John Malone may be deemed to have a 36.4% voting interest in Liberty Interactive and is Chairman of the board of directors, an executive officer position, of Liberty Interactive. Liberty Interactive owns 38.3% of the common stock of HSN, Inc. ("HSN") and has the right to elect 20% of the board members of HSN. Liberty Interactive wholly owns QVC, Inc. ("QVC"). The Company has programming relationships with HSN and QVC which pre-date the transaction with Liberty Media. For the years ended December 31, 2016, 2015 and 2014, the Company recorded payments in aggregate of approximately \$53 million, \$17 million and \$14 million, respectively, from HSN and QVC as part of channel carriage fees and revenue sharing arrangements for home shopping sales made to customers in the Company's footprint.

Dr. Malone and Mr. Steven Miron, each a member of Charter's board of directors, also serve on the board of directors of Discovery Communications, Inc., ("Discovery") and the Company is aware that Dr. Malone owns 5.2% in the aggregate of the common stock of Discovery and has a 28.7% voting interest in Discovery for the election of directors. The Company is aware that Advance/Newhouse Programming Partnership ("A/N PP"), an affiliate of A/N and in which Mr. Miron is the CEO, owns 100% of the Series A preferred stock of Discovery and 100% of the Series C preferred stock of Discovery, representing approximately 34.0% of the outstanding equity of Discovery's stock, on an as-converted basis. A/N PP has the right to appoint three directors out of a total of ten directors to Discovery's board to be elected by the holders of Discovery's Series A preferred stock. In addition, Dr. Malone is a member of the board of directors of Lions Gate Entertainment Corp. ("Lions Gate", parent company of Starz, Inc.) and owns approximately 5.9% in the aggregate of the common stock of Lions Gate and has 8.1% of the voting power, pursuant to his ownership of Lions Gate Class A voting shares. The Company purchases programming from both Discovery and Lions Gate pursuant to agreements entered into prior to Dr. Malone and Mr. Miron joining Charter's board of directors. Based on publicly available information, the Company does not believe that either Discovery or Lions Gate would currently be considered related parties. The amounts paid in the aggregate to Discovery and Lions Gate represent less than 3% of total operating costs and expenses for the years ended December 31, 2016, 2015 and 2014.

#### *Equity Investments*

The Company has agreements with certain equity-method investees (see Note 7) pursuant to which the Company has made or received related party transaction payments. The Company recorded payments to equity-method investees totaling \$171 million and \$28 million during the years ended December 31, 2016 and 2015, respectively. The Company recorded advertising revenues



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

from transactions with equity-method investees totaling \$7 million during the year ended December 31, 2016. The Company has loans outstanding to investees of \$5 million as of December 31, 2016.

## 20. Commitments and Contingencies

### Commitments

The following table summarizes the Company's payment obligations as of December 31, 2016 for its contractual obligations.

	Total	2017	2018	2019	2020	2021	Thereafter
Capital and Operating Lease Obligations <sup>(a)</sup>	\$ 1,324	\$ 259	\$ 225	\$ 180	\$ 142	108	\$ 410
Programming Minimum Commitments <sup>(b)</sup>	310	225	37	26	22	—	—
Other <sup>(c)</sup>	13,187	1,334	810	704	664	539	9,136
	<u>\$ 14,821</u>	<u>\$ 1,818</u>	<u>\$ 1,072</u>	<u>\$ 910</u>	<u>\$ 828</u>	<u>\$ 647</u>	<u>\$ 9,546</u>

<sup>(a)</sup> The Company leases certain facilities and equipment under non-cancelable capital and operating leases. Leases and rental costs charged to expense for the years ended December 31, 2016, 2015 and 2014 were \$215 million, \$49 million, \$43 million, respectively.

<sup>(b)</sup> The Company pays programming fees under multi-year contracts ranging from three to ten years, typically based on a flat fee per customer, which may be fixed for the term, or may in some cases escalate over the term. Programming costs included in the statement of operations were \$7.0 billion, \$2.7 billion and \$2.5 billion for the years ended December 31, 2016, 2015 and 2014 respectively. Certain of the Company's programming agreements are based on a flat fee per month or have guaranteed minimum payments. The table sets forth the aggregate guaranteed minimum commitments under the Company's programming contracts.

<sup>(c)</sup> "Other" represents other guaranteed minimum commitments, including rights negotiated directly with content owners for distribution on Company-owned channels or networks and commitments related to the Company's role as an advertising and distribution sales agent for third party-owned channels or networks as well as commitments to the Company's customer premise equipment vendors.

The following items are not included in the contractual obligation table due to various factors discussed below. However, the Company incurs these costs as part of its operations:

- The Company rents utility poles used in its operations. Generally, pole rentals are cancelable on short notice, but the Company anticipates that such rentals will recur. Rent expense incurred for pole rental attachments for the years ended December 31, 2016, 2015 and 2014 was \$115 million, \$53 million and \$49 million, respectively.
- The Company pays franchise fees under multi-year franchise agreements based on a percentage of revenues generated from video service per year. The Company also pays other franchise related costs, such as public education grants, under multi-year agreements. Franchise fees and other franchise-related costs included in the accompanying statement of operations were \$534 million, \$212 million and \$208 million for the years ended December 31, 2016, 2015 and 2014 respectively.
- The Company also has \$278 million in letters of credit, of which \$220 million is secured under the Charter Operating credit facility, primarily to its various casualty carriers as collateral for reimbursement of workers' compensation, auto liability and general liability claims.
- Minimum pension funding requirements have not been presented in the table above as such amounts have not been determined beyond 2016. The Company made no cash contributions to the qualified pension plans in 2016; however, the Company is permitted to make discretionary cash contributions to the qualified pension plans in 2017. For the nonqualified pension plan, the Company contributed \$5 million during 2016 and will continue to make contributions in 2017 to the extent benefits are paid.

### Legal Proceedings

In 2014, following an announcement by Comcast and Legacy TWC of their intent to merge, Breffni Barrett and others filed suit in the Supreme Court of the State of New York for the County of New York against Comcast, Legacy TWC and their respective officers and directors. Later five similar class actions were consolidated with this matter (the "NY Actions"). The NY Actions



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
**(dollars in millions, except share or per share data or where indicated)**

were settled in July 2014, however, such settlement was terminated following the termination of the Comcast and TWC merger in April 2015. In May 2015, Charter and TWC announced their intent to merge. Subsequently, the parties in the NY Actions filed a Second Consolidated Class Action Complaint (the "Second Amended Complaint"), removing Comcast as a defendant and naming TWC, the members of the TWC board of directors, Charter and the merger subsidiaries as defendants. The Second Amended Complaint generally alleges, among other things, that the members of the TWC board of directors breached their fiduciary duties to TWC stockholders during the Charter merger negotiations and by entering into the merger agreement and approving the mergers, and that Charter aided and abetted such breaches of fiduciary duties. The complaint sought, among other relief, injunctive relief enjoining the stockholder vote on the mergers, unspecified declaratory and equitable relief, compensatory damages in an unspecified amount, and costs and attorneys' fees.

In September 2015, the parties entered into a memorandum of understanding ("MOU") to settle the action. Pursuant to the MOU, the defendants issued certain supplemental disclosures relating to the mergers on a Form 8-K, and plaintiffs agreed to release with prejudice all claims that could have been asserted against defendants in connection with the mergers. The settlement is conditioned on, among other things, approval by the New York Supreme Court. That court gave preliminary approval to the settlement in October 2016. A hearing to consider final approval of this settlement is set for March 2017. In the event that the New York Supreme Court does not approve the settlement, Charter intends to vigorously defend this case.

In August 2015, a purported stockholder of Charter, Matthew Sciabacucchi, filed a lawsuit in the Delaware Court of Chancery, on behalf of a putative class of Charter stockholders, challenging the transactions between Charter, TWC, A/N, and Liberty Broadband announced by Charter on May 26, 2015 (collectively, the "Transactions"). The lawsuit names as defendants Liberty Broadband, Charter, the board of directors of Charter, and New Charter. Plaintiff alleged that the Transactions improperly benefit Liberty Broadband at the expense of other Charter shareholders, and that Charter issued a false and misleading proxy statement in connection with the Transactions. Plaintiff requested, among other things, that the Delaware Court of Chancery enjoin the September 21, 2015 special meeting of Charter stockholders at which Charter stockholders were asked to vote on the Transactions until the defendants disclosed certain information relating to Charter and the Transactions. The disclosures demanded by the plaintiff included (i) certain unlevered free cash flow projections for Charter and (ii) a Form of Proxy and Right of First Refusal Agreement ("Proxy") by and among Liberty Broadband, A/N, Charter and New Charter, which was referenced in the description of the Second Amended and Restated Stockholders Agreement, dated May 23, 2015, among Charter, New Charter, Liberty Broadband and A/N. On September 9, 2015, Charter issued supplemental disclosures containing unlevered free cash flow projections for Charter. In return, the plaintiff agreed its disclosure claims were moot and withdrew its application to enjoin the Charter stockholder vote on the Transactions. Charter has filed a motion to dismiss this litigation but the court has not yet ruled upon it. Charter denies any liability, believes that it has substantial defenses, and intends to vigorously defend this suit.

The California Attorney General and the Alameda County, California District Attorney are investigating whether certain of Legacy Charter's waste disposal policies, procedures and practices are in violation of the California Business and Professions Code and the California Health and Safety Code. That investigation was commenced in January 2014. A similar investigation involving Legacy TWC was initiated in February 2012. Charter is cooperating with these investigations. While the Company is unable to predict the outcome of these investigations, it does not expect that the outcome will have a material effect on its operations, financial condition, or cash flows.

On December 19, 2011, Sprint Communications Company L.P. ("Sprint") filed a complaint in the U.S. District Court for the District of Kansas alleging that Legacy TWC infringes 12 U.S. patents purportedly relating to Voice over Internet Protocol ("VoIP") services. Over the course of the litigation Sprint dismissed its claims relating to five of the asserted patents, and shortly before trial Sprint dropped its claims with respect to two additional patents. A trial on the remaining five patents is scheduled to begin on February 13, 2017. The plaintiff is seeking monetary damages of approximately \$150 million. The plaintiff is also claiming that TWC willfully infringed the patents, and may seek up to treble damages as well as attorneys' fees and costs. Charter intends to vigorously defend against this lawsuit. However, no assurances can be made that such defenses would ultimately be successful. At this time, the Company does not expect that the outcome of this litigation will have a material adverse effect on its operations, financial condition or cash flows although the ultimate outcome of the litigation cannot be predicted.

On October 23, 2015, the New York Office of the Attorney General (the "NY AG") began an investigation of Legacy TWC's advertised Internet speeds and other Internet product advertising. On February 1, 2017, the NY AG filed suit in the Supreme Court for the State of New York alleging that Legacy TWC's advertising of Internet speeds was false and misleading. The suit seeks restitution and injunctive relief. The Company denies that Legacy TWC engaged in any wrongdoing and the Company intends to defend itself vigorously. However, no assurances can be made that such defenses would ultimately be successful. At this time,



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

the Company does not expect that the outcome of this litigation will have a material adverse effect on its operations, financial condition or cash flows.

The Company is a defendant or co-defendant in several lawsuits involving alleged infringement of various patents relating to various aspects of its businesses. Other industry participants are also defendants in certain of these cases. In the event that a court ultimately determines that the Company infringes on any intellectual property rights, the Company may be subject to substantial damages and/or an injunction that could require the Company or its vendors to modify certain products and services the Company offers to its subscribers, as well as negotiate royalty or license agreements with respect to the patents at issue. While the Company believes the lawsuits are without merit and intends to defend the actions vigorously, no assurance can be given that any adverse outcome would not be material to the Company's consolidated financial condition, results of operations, or liquidity. The Company cannot predict the outcome of any such claims nor can it reasonably estimate a range of possible loss.

The Company is party to lawsuits, claims and regulatory inquiries that arise in the ordinary course of conducting its business, including lawsuits claiming violation of wage and hour laws and breach of contract by vendors, including by three programmers. The ultimate outcome of these other legal matters pending against the Company cannot be predicted, and although such lawsuits and claims are not expected individually to have a material adverse effect on the Company's consolidated financial condition, results of operations or liquidity, such lawsuits could have, in the aggregate, a material adverse effect on the Company's consolidated financial condition, results of operations or liquidity. Whether or not the Company ultimately prevails in any particular lawsuit or claim, litigation can be time consuming and costly and injure the Company's reputation.

## **21. Employee Benefit Plans**

### *Pension Plans*

Upon completion of the TWC Transaction, Charter assumed sponsorship of Legacy TWC's pension plans. The Company sponsors two qualified defined benefit pension plans, the TWC Pension Plan and the TWC Union Pension Plan, that provide pension benefits to a majority of Legacy TWC employees. The Company also provides a nonqualified defined benefit pension plan for certain employees under the TWC Excess Pension Plan.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Changes in the projected benefit obligation, fair value of plan assets and funded status of the pension plans from January 1, 2016 through December 31, 2016 are presented below:

	<u>2016</u>
Projected benefit obligation at beginning of year	\$ —
Benefit obligation assumed in the TWC Transaction	4,009
Service cost	86
Interest cost	87
Curtailement amendment	(675)
Actuarial gain	(149)
Benefits paid	(98)
Projected benefit obligation at end of year	<u>\$ 3,260</u>
Accumulated benefit obligation at end of year	<u>\$ 3,260</u>
Fair value of plan assets at beginning of year	\$ —
Fair value of plan assets acquired in the TWC Transaction	2,877
Actual return on plan assets	162
Employer contributions	5
Benefits paid	(98)
Fair value of plan assets at end of year	<u>\$ 2,946</u>
Funded status	<u>\$ (314)</u>

The projected benefit obligation, accumulated benefit obligation and fair value of plan assets for the qualified pension plans and the nonqualified pension plan as of December 31, 2016 consisted of the following:

	<u>Qualified Pension Plans</u>	<u>Nonqualified Pension Plan</u>
	<u>December 31, 2016</u>	
Projected benefit obligation	\$ 3,204	\$ 56
Accumulated benefit obligation	\$ 3,204	\$ 56
Fair value of plan assets	\$ 2,946	\$ —

Pretax amounts recognized in the consolidated balance sheet as of December 31, 2016 consisted of the following:

	<u>December 31, 2016</u>
Noncurrent asset	\$ 1
Current liability	(6)
Long-term liability	(309)
Net amounts recognized in consolidated balance sheet	<u>\$ (314)</u>

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

The components of net periodic benefit costs for the year ended December 31, 2016 consisted of the following:

	<u>Year Ended December 31, 2016</u>
Service cost	\$ 86
Interest cost	87
Expected return on plan assets	(116)
Pension curtailment gain	(675)
Remeasurement gain	(195)
Net periodic pension benefit	<u>\$ (813)</u>

The \$195 million remeasurement gain recorded during the year ended December 31, 2016 was primarily driven by the effects of an increase of the discount rate from 3.99% at the closing date of the TWC Transaction to 4.20% at December 31, 2016 and a gain to record pension assets at December 31, 2016 fair values.

Weighted average assumptions used to determine benefit obligations as of December 31, 2016 consisted of the following:

	<u>December 31, 2016</u>
Discount rate	4.20%
Rate of compensation increase	—%

The weighted average of discount rates used to measure the projected benefit obligation at the closing date of the TWC Transaction was 3.99%. The rate of compensation increase used to measure the projected benefit obligation as of the closing of the TWC Transaction was an age-graded average increase of 4.25%. The Company utilized the RP 2015/MP2015 mortality tables published by the Society of Actuaries to measure the benefit obligations as of December 31, 2016 and the closing date of the TWC Transaction.

Weighted average assumptions used to determine net periodic benefit costs for the year ended December 31, 2016 consisted of the following:

	<u>Year Ended December 31, 2016</u>
Expected long-term rate of return on plan assets	6.50%
Discount rate <sup>(a)</sup>	3.72%
Rate of compensation increase <sup>(b)</sup>	—%

(a) The discount rate used to determine net periodic pension benefit was 3.99% from the closing date of the TWC Transaction through remeasurement date (June 30, 2016), and was 3.72% from remeasurement date through December 31, 2016.

(b) The rate of compensation increase used to determine net periodic pension benefit was 4.25% from the closing date of the TWC Transaction through remeasurement date (June 30, 2016), and 0% thereafter. See "Pension Plan Curtailment Amendment" below for further discussion.

In developing the expected long-term rate of return on plan assets, the Company considered the pension portfolio's composition, past average rate of earnings and the Company's future asset allocation targets. The weighted average expected long-term rate of return on plan assets used to determine net periodic pension benefit for the year ended December 31, 2017 is expected to be 6.50%. The Company determined the discount rates used to determine benefit obligations and net periodic pension benefit based on the yield of a large population of high quality corporate bonds with cash flows sufficient in timing and amount to settle projected future defined benefit payments.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

*Pension Plan Curtailment Amendment*

Following the closing of the TWC Transaction, Charter amended the pension plans to freeze future benefit accruals to current active plan participants as of August 31, 2016. Effective September 1, 2016, no future compensation increases or future service will be credited to participants of the pension plans and new hires are not eligible to participate in the plans. Upon announcement and approval of the plan amendment, the assumptions underlying the pension liability and pension asset values were reassessed utilizing remeasurement date assumptions in accordance with Charter's mark-to-market pension accounting policy to record gains and losses in the period in which a remeasurement event occurs. The \$675 million curtailment gain recorded during the year ended December 31, 2016 was primarily driven by the reduction of the compensation rate assumption to 0% in accordance with the terms of the plan amendment, reflecting the pension liability at its accumulated benefit obligation instead of its projected benefit obligation at the remeasurement date.

*Pension Plan Assets*

The assets of the qualified pension plans are held in a master trust in which the qualified pension plans are the only participating plans (the "Master Trust"). The investment policy for the qualified pension plans is to achieve a reasonable long-term rate of return on plan assets with an acceptable level of risk in order to maintain adequate funding levels. The investment portfolio is a mix of fixed-income and equity securities with the objective of matching plan liability performance, diversifying risk and achieving a target investment return. The pension plan's Investment Committee establishes risk mitigation policies and regularly monitors investment performance, investment allocation policies, and the execution of these strategies. The Investment Committee engages a third-party investment firm with responsibility of executing the directives of the Investment Committee, monitoring the performance of individual investment managers of the Master Trust, and making adjustments and changes within defined parameters when necessary. On a periodic basis, the Investment Committee conducts a broad strategic review of its portfolio construction and investment allocation policies. Neither the Company, the Investment Committee, nor the third-party investment firm manages any assets internally or directly utilizes derivative instruments or hedging; however, the investment mandate of some investment managers allows the use of derivatives as components of their standard portfolio management strategies. Pension assets are managed in a balanced portfolio comprised of two major components: a return-seeking portion and a liability-matching portion. The expected role of return-seeking investments is to achieve a reasonable long-term growth of pension assets with a prudent level of risk, while the role of liability-matching investments is to provide a partial hedge against liability performance associated with changes in interest rates. The objective within return-seeking investments is to achieve asset diversity in order to balance return and volatility.

The Company adopted an investment strategy referred to as a de-risking glide path to increase the fixed income allocation as the funded status of the qualified pension plans improves. As the qualified pension plans reach set funded status milestones, the assets will be rebalanced to shift more assets from equity to fixed income. Based on the progress with this strategy, the target investment allocation for pension fund assets is permitted to vary within specified ranges subject to Investment Committee approval for return-seeking securities and liability-matching securities. The target and actual investment allocation of the qualified pension plans by asset category as of December 31, 2016 consisted of the following:

	<u>Target Allocation</u>	<u>Actual Allocation December 31, 2016</u>
Return-seeking securities	75.0%	64.4%
Liability-matching securities	25.0%	35.4%
Other investments	—%	0.2%

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
**(dollars in millions, except share or per share data or where indicated)**

The following table sets forth the investment assets of the qualified pension plans, which exclude accrued investment income and other receivables, accrued liabilities, and investments with a fair value measured at net asset value per share as a practical expedient, by level within the fair value hierarchy as of December 31, 2016:

	December 31, 2016			
	Fair Value	Level 1	Level 2	Level 3
Cash	\$ 2	\$ 2	\$ —	\$ —
Common stocks:				
Domestic <sup>(a)</sup>	1,065	1,065	—	—
International <sup>(a)</sup>	391	391	—	—
Commingled equity funds <sup>(b)</sup>	348	—	348	—
Other equity securities <sup>(c)</sup>	3	3	—	—
Corporate debt securities <sup>(d)</sup>	394	—	394	—
Commingled bond funds <sup>(b)</sup>	273	—	273	—
U.S. Treasury debt securities <sup>(a)</sup>	260	260	—	—
Collective trust funds <sup>(c)</sup>	75	—	75	—
U.S. government agency asset-backed debt securities <sup>(f)</sup>	53	—	53	—
Corporate asset-backed debt securities <sup>(g)</sup>	2	—	2	—
Other fixed-income securities <sup>(h)</sup>	89	—	89	—
Total investment assets	2,955	<u>\$ 1,721</u>	<u>\$ 1,234</u>	<u>\$ —</u>
Accrued investment income and other receivables <sup>(i)</sup>	107			
Accrued liabilities <sup>(i)</sup>	(120)			
Investments measured at net asset value <sup>(j)</sup>	4			
Fair value of plan assets	<u>\$ 2,946</u>			

(a) Common stocks, mutual funds and U.S. Treasury debt securities are valued at the closing price reported on the active market on which the individual securities are traded. No single industry comprised a significant portion of common stock held by the qualified pension plan as of December 31, 2016.

(b) Commingled equity funds and commingled bond funds are valued using the net asset value provided by the administrator of the fund. The net asset value is based on the readily determinable value of the underlying assets owned by the fund, less liabilities, and then divided by the number of units outstanding.

(c) Other equity securities consist of preferred stocks, which are valued at the closing price reported on the active market on which the individual securities are traded.

(d) Corporate debt securities are valued based on observable prices from the new issue market, benchmark quotes, secondary trading and dealer quotes. An option adjusted spread model is incorporated to adjust spreads of issues that have early redemption features and final spreads are added to the U.S. Treasury curve.

(e) Collective trust funds primarily consist of short-term investment strategies comprised of instruments issued or fully guaranteed by the U.S. government and/or its agencies and are valued using the net asset value provided by the administrator of the fund. The net asset value is based on the readily determinable value of the underlying assets owned by the fund, less liabilities, and then divided by the number of units outstanding.

(f) U.S. government agency asset-backed debt securities consist of pass-through mortgage-backed securities issued by the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association valued using available trade information, dealer quotes, market indices and research reports, spreads, bids and offers.

(g) Corporate asset-backed debt securities primarily consist of pass-through mortgage-backed securities issued by U.S. and foreign corporations valued using available trade information, dealer quotes, market indices and research reports, spreads, bids and offers.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

- (b) Other fixed-income securities consist of foreign government debt securities, municipal bonds and U.S. government agency debt securities, which are valued based on observable prices from the new issue market, benchmark quotes, secondary trading and dealer quotes. An option adjusted spread model is incorporated to adjust spreads of issues that have early redemption features and final spreads are added to the U.S. Treasury curve.
- (c) Accrued investment income and other receivables includes amounts receivable under foreign exchange contracts of \$70 million as of December 31, 2016. Accrued liabilities includes amounts accrued under foreign exchange contracts of \$71 million as of December 31, 2016. The fair value of the assets and liabilities associated with these foreign exchange contracts are presented on a gross basis and are valued using the exchange rates in effect for the applicable currencies as of the valuation date (a Level 1 fair value measurement).
- (d) Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. These investments primarily consist of hedge funds valued utilizing net asset value provided by the administrator of the fund, which is based on the value of the underlying assets owned by the fund, less liabilities, and then divided by the number of units outstanding. Shares of the fund are not redeemable and the underlying assets are anticipated to be liquidated and distributed to investors in the near term. There are no material unfunded commitments with respect to these investments. The fair value amounts presented in this table are intended to permit the reconciliation of the fair value hierarchy to the total fair value of plan assets discussed throughout this footnote.

#### ***Pension Plan Contributions***

The Company made no cash contributions to the qualified pension plans during the year ended December 31, 2016; however, the Company may make discretionary cash contributions to the qualified pension plans in the future. Such contributions will be dependent on a variety of factors, including current and expected interest rates, asset performance, the funded status of the qualified pension plans and management's judgment. For the nonqualified unfunded pension plan, the Company will continue to make contributions during 2017 to the extent benefits are paid.

Benefit payments for the pension plans are expected to be \$170 million in 2017, \$174 million in 2018, \$177 million in 2019, \$180 million in 2020, \$182 million in 2021 and \$911 million in 2022 to 2026.

#### ***Multiemployer Plans***

Upon completion of the TWC Transaction, Charter assumed Legacy TWC's multiemployer plans. The Company contributes to a number of multiemployer plans under the terms of collective-bargaining agreements that cover its union-represented employees. Such multiemployer plans provide medical, pension and retirement savings benefits to active employees and retirees. The Company made contributions to multiemployer plans of \$31 million for the year ended December 31, 2016.

The risks of participating in multiemployer pension plans are different from single-employer pension plans in the following aspects: (a) assets contributed to a multiemployer pension plan by one employer may be used to provide benefits to employees of other participating employers, (b) if a participating employer stops contributing to the multiemployer pension plan, the unfunded obligations of the plan may be borne by the remaining participating employers and (c) if the Company chooses to stop participating in any of the multiemployer pension plans, it may be required to pay those plans an amount based on the underfunded status of the plan, referred to as a withdrawal liability.

The multiemployer pension plans to which the Company contributes each received a Pension Protection Act "green" zone status in 2015. The zone status is based on the most recent information the Company received from the plan and is certified by the plan's actuary. Among other factors, plans in the green zone are at least 80% funded.

#### ***Defined Contribution Benefit Plans***

The Company's employees may participate in the Charter Communications, Inc. 401(k) Plan (the "401(k) Plan"). Upon completion of the TWC Transaction, Charter assumed Legacy TWC's defined contribution plan, the TWC Savings Plan. In June 2016, the Company announced changes to both the 401(k) Plan and the TWC Savings Plan that were effective September 1, 2016 and effective January 1, 2017, the 401(k) Plan and TWC Savings Plan merged into one plan. Employees that qualify for participation can contribute up to 50% of their salary, on a pre-tax basis, subject to a maximum contribution limit as determined by the Internal Revenue Service. The Company's matching contribution is discretionary and is equal to 100% of the amount of the salary reduction the participant elects to defer (up to 6% of the participant's eligible compensation), excluding any catch-up contributions and is



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
**(dollars in millions, except share or per share data or where indicated)**

paid by the Company on a per pay period basis. The Company made contributions to the 401(k) plans totaling \$147 million, \$23 million and \$19 million for the years ended December 31, 2016, 2015 and 2014, respectively.

For employees who are not eligible to participate in the Company's long-term incentive plan and who are not covered by a collective bargaining agreement, the Company offers a contribution to the new Retirement Accumulation Plan ("RAP"), equal to 3% of eligible pay. The Company made contributions to the RAP totaling \$48 million for the year ended December 31, 2016.

## **22. Recently Issued Accounting Standards**

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"), which is a comprehensive revenue recognition standard that will supersede nearly all existing revenue recognition guidance under U.S. GAAP. The new standard provides a single principles-based, five-step model to be applied to all contracts with customers, which steps are to (1) identify the contract(s) with the customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations in the contract and (5) recognize revenue when each performance obligation is satisfied. More specifically, revenue will be recognized when promised goods or services are transferred to the customer in an amount that reflects the consideration expected in exchange for those goods or services. ASU 2014-09 will be effective, reflecting the one-year deferral, for interim and annual periods beginning after December 15, 2017 (January 1, 2018 for the Company). Early adoption of the standard is permitted but not before the original effective date. Companies can transition to the standard either retrospectively or as a cumulative-effect adjustment as of the date of adoption. The Company is currently in the process of evaluating which method of transition will be utilized. The Company is continuing to assess all potential impacts that the adoption of ASU 2014-09 will have on its consolidated financial statements, including developing new accounting policies, internal controls and processes to facilitate the adoption of the standard. The most significant impacts upon adoption are anticipated to result from the deferral over a period of time instead of recognized immediately of (1) the residential installation revenues which represent nonrefundable up-front fees that convey a material right to the customer and (2) the internal and external commission expenses which represent costs of obtaining a contract.

In April 2015, the FASB issued ASU No. 2015-05, *Customer's Accounting for Fees Paid in a Cloud Computing Arrangement* ("ASU 2015-05"), which provides guidance in determining whether fees for purchasing cloud computing services (or hosted software solutions) are considered internal-use software or should be considered a service contract. The cloud computing agreement that includes a software license should be accounted for in the same manner as internal-use software if customer has contractual right to take possession of the software during the hosting period without significant penalty and it is feasible to either run the software on customer's hardware or contract with another vendor to host the software. Arrangements that don't meet the requirements for internal-use software should be accounted for as a service contract. ASU 2015-05 was effective for interim and annual periods beginning after December 15, 2015 (January 1, 2016 for the Company). The adoption of ASU 2015-05 did not have a material impact on the Company's financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases* ("ASU 2016-02"), which requires lessees to recognize almost all leases on their balance sheet as a right-of-use asset and a lease liability. Lessees are allowed to account for short-term leases (i.e., leases with a term of 12 months or less) off-balance sheet, consistent with current operating lease accounting. For income statement purposes, the FASB retained a dual model, requiring leases to be classified as either operating or finance. Classification will be based on criteria that are largely similar to those applied in current lease accounting, but without explicit bright lines. ASU 2016-02 will be effective for interim and annual periods beginning after December 15, 2018 (January 1, 2019 for the Company). Early adoption is permitted. The new standard requires a modified retrospective transition through a cumulative-effect adjustment as of the beginning of the earliest period presented in the financial statements. The Company is currently in the process of evaluating the impact that the adoption of ASU 2016-02 will have on its consolidated financial statements including identifying the population of leases, evaluating technology solutions and collecting lease data.

In March 2016, the FASB issued ASU No. 2016-09, *Improvements to Employee Share-Based Payment Accounting* ("ASU 2016-09"), which includes multiple provisions intended to simplify various aspects of the accounting for share-based payments. The new standard (1) requires all excess tax benefits and deficiencies to be recognized as income tax expense or benefit in the income statement in the period in which they occur regardless of whether the benefit reduces taxes payable in the current period, (2) requires classification of excess tax benefits as an operating activity on the statements of cash flows, (3) allows an entity to make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur and (4) causes the threshold under which employee share-based awards partially settled in cash can



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

qualify for equity classification to increase to the maximum statutory tax rates in the applicable jurisdiction. ASU 2016-09 will be effective for interim and annual periods after December 15, 2016 (January 1, 2017 for the Company). The new standard generally requires a modified retrospective transition through a cumulative-effect adjustment as of the beginning of the period of adoption, with certain provisions requiring either a prospective or retrospective transition. The Company adopted ASU 2016-09 on January 1, 2017. Upon adoption of ASU 2016-09, the Company will recognize excess tax benefits of approximately \$136 million in deferred tax assets that were previously not recognized in a cumulative-effect adjustment to retained earnings. The Company will prospectively record a deferred tax benefit or expense associated with the difference between book and tax for stock compensation expense. On January 1, 2017, the Company will also establish an accounting policy election to assume zero forfeitures for stock award grants and account for forfeitures when they occur which will prospectively impact stock compensation expense. Other aspects of adoption ASU 2016-09 are not anticipated to have a material impact to the Company's consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, *Classification of Certain Cash Receipts and Cash Payments* ("ASU 2016-15"), which clarifies how entities should classify cash receipts and cash payments related to eight specific cash flow matters on the statement of cash flows, with the objective of reducing existing diversity in practice. ASU 2016-15 will be effective for interim and annual periods beginning after December 15, 2017 (January 1, 2018 for the Company). Early adoption is permitted. The Company is currently in the process of evaluating the impact that the adoption of ASU 2016-15 will have on its consolidated financial statements.

### 23. Unaudited Quarterly Financial Data

The following table presents quarterly data for the periods presented in the consolidated statement of operations:

	Year Ended December 31, 2016			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenues	\$ 2,530	\$ 6,161	\$ 10,037	\$ 10,275
Income from operations	\$ 302	\$ 690	\$ 924	\$ 1,439
Net income (loss) attributable to Charter shareholders	\$ (188)	\$ 3,067	\$ 189	\$ 454
Earnings (loss) per common share attributable to Charter shareholders:				
Basic	\$ (1.86)	\$ 16.73	\$ 0.70	\$ 1.69
Diluted	\$ (1.86)	\$ 15.17	\$ 0.69	\$ 1.67
Weighted average common share outstanding:				
Basic	101,552,093	183,362,776	271,263,259	268,584,368
Diluted	101,552,093	205,214,266	275,373,202	272,624,270

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

	Year Ended December 31, 2015			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenues	\$ 2,362	\$ 2,430	\$ 2,450	\$ 2,512
Income from operations	\$ 249	\$ 269	\$ 273	\$ 323
Net income (loss) attributable to Charter shareholders	\$ (81)	\$ (122)	\$ 54	\$ (122)
Earnings (loss) per common share attributable to Charter shareholders:				
Basic	\$ (0.81)	\$ (1.21)	\$ 0.54	\$ (1.21)
Diluted	\$ (0.81)	\$ (1.21)	\$ 0.53	\$ (1.21)
Weighted average common share outstanding:				
Basic	100,959,008	101,074,644	101,205,400	101,366,476
Diluted	100,959,008	101,074,644	102,481,924	101,366,476

#### 24. Consolidating Schedules

Each of Charter Operating, TWC, LLC, TWCE, CCO Holdings and certain subsidiaries jointly, severally, fully and unconditionally guarantee the outstanding debt securities of the others (other than the CCO Holdings notes) on an unsecured senior basis and the condensed consolidating financial information has been prepared and presented pursuant to SEC Regulation S-X Rule 3-10, *Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered*. Certain Charter Operating subsidiaries that are regulated telephone entities only become guarantor subsidiaries upon approval by regulators. This information is not intended to present the financial position, results of operations and cash flows of the individual companies or groups of companies in accordance with generally accepted accounting principles.

The "Charter Operating and Restricted Subsidiaries" column is presented to comply with the terms of the Credit Agreement.

The "Safari Escrow Entities" column included in the condensed consolidating financial statements as of December 31, 2015 and for the years ended December 31, 2015 and 2014 consists of CCOH Safari, CCO Safari II and CCO Safari III. CCOH Safari, CCO Safari II and CCO Safari III issued the CCOH Safari notes, CCO Safari II notes and the CCO Safari III credit facilities, respectively. Upon closing of the TWC Transaction, the CCOH Safari notes became obligations of CCO Holdings and CCO Holdings Capital and the CCO Safari II notes and CCO Safari III credit facilities became obligations of Charter Operating and Charter Communications Operating Capital Corp. CCOH Safari merged into CCO Holdings and CCO Safari II and CCO Safari III merged into Charter Operating.

The "Unrestricted Subsidiary" column included in the condensed consolidating financial statements for the years ended December 31, 2016 and 2015 consists of CCO Safari which was a non-recourse subsidiary under the Credit Agreement and held the CCO Safari Term G Loans that were repaid in April 2015.

Condensed consolidating financial statements as of December 31, 2016 and 2015 and for the years ended December 31, 2016, 2015 and 2014 follow.

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Charter Communications, Inc.  
Condensed Consolidating Balance Sheet  
As of December 31, 2016

	Non-Guarantor Subsidiaries		Guarantor Subsidiaries		Eliminations	Charter Consolidated
	Charter	Intermediate Holding Companies	CCO Holdings	Charter Operating and Restricted Subsidiaries		
<b>ASSETS</b>						
<b>CURRENT ASSETS:</b>						
Cash and cash equivalents	\$ 57	\$ 154	\$ —	\$ 1,324	\$ —	\$ 1,535
Accounts receivable, net	34	11	—	1,387	—	1,432
Receivables from related party	170	451	62	—	(683)	—
Prepaid expenses and other current assets	—	33	—	300	—	333
Total current assets	261	649	62	3,011	(683)	3,300
<b>INVESTMENT IN CABLE PROPERTIES:</b>						
Property, plant and equipment, net	—	245	—	32,718	—	32,963
Customer relationships, net	—	—	—	14,608	—	14,608
Franchises	—	—	—	67,316	—	67,316
Goodwill	—	—	—	29,509	—	29,509
Total investment in cable properties, net	—	245	—	144,151	—	144,396
INVESTMENT IN SUBSIDIARIES	66,692	75,838	88,760	—	(231,290)	—
LOANS RECEIVABLE – RELATED PARTY	—	640	494	—	(1,134)	—
OTHER NONCURRENT ASSETS	—	214	—	1,157	—	1,371
Total assets	\$ 66,953	\$ 77,586	\$ 89,316	\$ 148,319	\$ (233,107)	\$ 149,067
<b>LIABILITIES AND SHAREHOLDERS'/MEMBER'S EQUITY</b>						
<b>CURRENT LIABILITIES:</b>						
Accounts payable and accrued liabilities	\$ 22	\$ 625	\$ 219	\$ 6,678	\$ —	\$ 7,544
Payables to related party	—	—	—	683	(683)	—
Current portion of long-term debt	—	—	—	2,028	—	2,028
Total current liabilities	22	625	219	9,389	(683)	9,572
LONG-TERM DEBT	—	—	13,259	46,460	—	59,719
LOANS PAYABLE – RELATED PARTY	—	—	—	1,134	(1,134)	—
DEFERRED INCOME TAXES	26,637	3	—	25	—	26,665
OTHER LONG-TERM LIABILITIES	155	64	—	2,526	—	2,745
<b>SHAREHOLDERS'/MEMBER'S EQUITY</b>						
Controlling interest	40,139	66,692	75,838	88,760	(231,290)	40,139
Noncontrolling interests	—	10,202	—	25	—	10,227
Total shareholders'/member's equity	40,139	76,894	75,838	88,785	(231,290)	50,366
Total liabilities and shareholders'/member's equity	\$ 66,953	\$ 77,586	\$ 89,316	\$ 148,319	\$ (233,107)	\$ 149,067



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Charter Communications, Inc.  
Condensed Consolidating Balance Sheet  
As of December 31, 2015

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries			Charter Consolidated
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Eliminations	
<b>ASSETS</b>							
<b>CURRENT ASSETS:</b>							
Cash and cash equivalents	\$ —	\$ —	\$ —	\$ —	\$ 5	\$ —	\$ 5
Accounts receivable, net	8	7	—	—	264	—	279
Receivables from related party	51	297	—	14	—	(362)	—
Prepaid expenses and other current assets	—	6	—	—	55	—	61
Total current assets	59	310	—	14	324	(362)	345
RESTRICTED CASH AND CASH EQUIVALENTS	—	—	22,264	—	—	—	22,264
<b>INVESTMENT IN CABLE PROPERTIES:</b>							
Property, plant and equipment, net	—	28	—	—	8,317	—	8,345
Customer relationships, net	—	—	—	—	856	—	856
Franchises	—	—	—	—	6,006	—	6,006
Goodwill	—	—	—	—	1,168	—	1,168
Total investment in cable properties, net	—	28	—	—	16,347	—	16,375
INVESTMENT IN SUBSIDIARIES	1,468	816	—	11,303	—	(13,587)	—
LOANS RECEIVABLE – RELATED PARTY	—	333	—	613	563	(1,509)	—
OTHER NONCURRENT ASSETS	—	216	—	—	116	—	332
Total assets	\$ 1,527	\$ 1,703	\$ 22,264	\$ 11,930	\$ 17,350	\$ (15,458)	\$ 39,316
<b>LIABILITIES AND SHAREHOLDERS'/MEMBER'S EQUITY (DEFICIT)</b>							
<b>CURRENT LIABILITIES:</b>							
Accounts payable and accrued liabilities	\$ 11	\$ 203	\$ 282	\$ 165	\$ 1,311	\$ —	\$ 1,972
Payables to related party	—	—	17	—	345	(362)	—
Total current liabilities	11	203	299	165	1,656	(362)	1,972
LONG-TERM DEBT	—	—	21,778	10,443	3,502	—	35,723
LOANS PAYABLE – RELATED PARTY	—	—	693	—	816	(1,509)	—
DEFERRED INCOME TAXES	1,562	—	—	—	28	—	1,590
OTHER LONG-TERM LIABILITIES	—	32	—	—	45	—	77
SHAREHOLDERS'/MEMBER'S EQUITY (DEFICIT)	(46)	1,468	(506)	1,322	11,303	(13,587)	(46)
Total liabilities and shareholders'/member's equity (deficit)	\$ 1,527	\$ 1,703	\$ 22,264	\$ 11,930	\$ 17,350	\$ (15,458)	\$ 39,316



**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Charter Communications, Inc.  
Condensed Consolidating Statement of Operations  
For the year ended December 31, 2016

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries			Charter Consolidated
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Eliminations	
REVENUES	\$ 251	\$ 1,004	\$ —	\$ —	\$ 29,003	\$ (1,255)	\$ 29,003
COSTS AND EXPENSES:							
Operating costs and expenses (exclusive of items shown separately below)	251	989	—	—	18,670	(1,255)	18,655
Depreciation and amortization	—	5	—	—	6,902	—	6,907
Other operating (income) expenses, net	262	1	—	—	(177)	—	86
	513	995	—	—	25,395	(1,255)	25,648
Income (loss) from operations	(262)	9	—	—	3,608	—	3,355
OTHER INCOME (EXPENSES):							
Interest income (expense), net	—	14	(390)	(727)	(1,396)	—	(2,499)
Loss on extinguishment of debt	—	—	—	(110)	(1)	—	(111)
Gain on financial instruments, net	—	—	—	—	89	—	89
Other expense, net	—	(11)	—	—	(3)	—	(14)
Equity in income of subsidiaries	851	1,066	—	2,293	—	(4,210)	—
	851	1,069	(390)	1,456	(1,311)	(4,210)	(2,535)
Income (loss) before income taxes	589	1,078	(390)	1,456	2,297	(4,210)	820
INCOME TAX BENEFIT (EXPENSE)	2,933	(5)	—	—	(3)	—	2,925
Consolidated net income (loss)	3,522	1,073	(390)	1,456	2,294	(4,210)	3,745
Less: Net income – noncontrolling interests	—	(222)	—	—	(1)	—	(223)
Net income (loss)	\$ 3,522	\$ 851	\$ (390)	\$ 1,456	\$ 2,293	\$ (4,210)	\$ 3,522

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Charter Communications, Inc.  
Condensed Consolidating Statement of Operations  
For the year ended December 31, 2015

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries			Eliminations	Charter Consolidated
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Unrestricted Subsidiary		
REVENUES	\$ 25	\$ 299	\$ —	\$ —	\$ 9,754	\$ —	\$ (324)	\$ 9,754
COSTS AND EXPENSES:								
Operating costs and expenses (exclusive of items shown separately below)	25	299	—	—	6,426	—	(324)	6,426
Depreciation and amortization	—	—	—	—	2,125	—	—	2,125
Other operating expenses, net	—	—	—	—	89	—	—	89
	25	299	—	—	8,640	—	(324)	8,640
Income from operations	—	—	—	—	1,114	—	—	1,114
OTHER INCOME (EXPENSES):								
Interest income (expense), net	—	8	(474)	(642)	(151)	(47)	—	(1,306)
Loss on extinguishment of debt	—	—	(2)	(123)	—	(3)	—	(128)
Loss on financial instruments, net	—	—	—	—	(4)	—	—	(4)
Other expense, net	—	(7)	—	—	—	—	—	(7)
Equity in income (loss) of subsidiaries	(121)	(168)	—	1,073	(50)	—	(734)	—
	(121)	(167)	(476)	308	(205)	(50)	(734)	(1,445)
Income (loss) before income taxes	(121)	(167)	(476)	308	909	(50)	(734)	(331)
INCOME TAX BENEFIT (EXPENSE)	(150)	—	—	—	210	—	—	60
Consolidated net income (loss)	(271)	(167)	(476)	308	1,119	(50)	(734)	(271)
Less: Net (income) loss – noncontrolling interest	—	46	—	—	(46)	—	—	—
Net income (loss)	\$ (271)	\$ (121)	\$ (476)	\$ 308	\$ 1,073	\$ (50)	\$ (734)	\$ (271)

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Charter Communications, Inc.  
Condensed Consolidating Statement of Operations  
For the year ended December 31, 2014

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries				Charter Consolidated
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Unrestricted Subsidiary	Eliminations	
REVENUES	\$ 22	\$ 235	\$ —	\$ —	\$ 9,108	\$ —	\$ (257)	\$ 9,108
COSTS AND EXPENSES:								
Operating costs and expenses (exclusive of items shown separately below)	22	235	—	—	5,973	—	(257)	5,973
Depreciation and amortization	—	—	—	—	2,102	—	—	2,102
Other operating expenses, net	—	—	—	—	62	—	—	62
	22	235	—	—	8,137	—	(257)	8,137
Income from operations	—	—	—	—	971	—	—	971
OTHER INCOME AND (EXPENSES):								
Interest income (expense), net	—	8	(30)	(679)	(165)	(45)	—	(911)
Loss on financial instruments, net	—	—	—	—	(7)	—	—	(7)
Equity in income (loss) of subsidiaries	40	(12)	—	697	(45)	—	(680)	—
	40	(4)	(30)	18	(217)	(45)	(680)	(918)
Income (loss) before income taxes	40	(4)	(30)	18	754	(45)	(680)	53
INCOME TAX EXPENSE	(223)	—	—	—	(13)	—	—	(236)
Consolidated net income (loss)	(183)	(4)	(30)	18	741	(45)	(680)	(183)
Less Net (income) loss – noncontrolling interest	—	44	—	—	(44)	—	—	—
Net income (loss)	\$ (183)	\$ 40	\$ (30)	\$ 18	\$ 697	\$ (45)	\$ (680)	\$ (183)

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

**Charter Communications, Inc.**  
**Condensed Consolidating Statement of Comprehensive Income (Loss)**  
**For the year ended December 31, 2016**

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries			Charter Consolidated
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Eliminations	
Consolidated net income (loss)	\$ 3,522	\$ 1,073	\$ (390)	\$ 1,456	\$ 2,294	\$ (4,210)	\$ 3,745
Net impact of interest rate derivative instruments	8	8	8	8	8	(32)	8
Foreign currency translation adjustment	(2)	(2)	(2)	(2)	(2)	8	(2)
Consolidated comprehensive income (loss)	3,528	1,079	(384)	1,462	2,300	(4,234)	3,751
Less: Comprehensive income attributable to noncontrolling interests	—	(222)	—	—	(1)	—	(223)
Comprehensive income (loss)	<u>\$ 3,528</u>	<u>\$ 857</u>	<u>\$ (384)</u>	<u>\$ 1,462</u>	<u>\$ 2,299</u>	<u>\$ (4,234)</u>	<u>\$ 3,528</u>

**Charter Communications, Inc.**  
**Condensed Consolidating Statement of Comprehensive Income (Loss)**  
**For the year ended December 31, 2015**

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries			Charter Consolidated
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Unrestricted Subsidiary	
Consolidated net income (loss)	\$ (271)	\$ (167)	\$ (476)	\$ 308	\$ 1,119	\$ (50)	\$ (271)
Net impact of interest rate derivative instruments	9	9	9	9	9	—	9
Consolidated comprehensive income (loss)	(262)	(158)	(467)	317	1,128	(50)	(262)
Less: Comprehensive (income) loss attributable to noncontrolling interests	—	46	—	—	(46)	—	—
Comprehensive income (loss)	<u>\$ (262)</u>	<u>\$ (112)</u>	<u>\$ (467)</u>	<u>\$ 317</u>	<u>\$ 1,082</u>	<u>\$ (50)</u>	<u>\$ (262)</u>

**Charter Communications, Inc.**  
**Condensed Consolidating Statement of Comprehensive Income (Loss)**  
**For the year ended December 31, 2014**

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries			Charter Consolidated
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Unrestricted Subsidiary	
Consolidated net income (loss)	\$ (183)	\$ (4)	\$ (30)	\$ 18	\$ 741	\$ (45)	\$ (183)
Net impact of interest rate derivative instruments	19	19	19	19	19	—	19
Consolidated comprehensive income (loss)	(164)	15	(11)	37	760	(45)	(164)
Less: Comprehensive (income) loss attributable to noncontrolling interests	—	44	—	—	(44)	—	—
Comprehensive income (loss)	<u>\$ (164)</u>	<u>\$ 59</u>	<u>\$ (11)</u>	<u>\$ 37</u>	<u>\$ 716</u>	<u>\$ (45)</u>	<u>\$ (164)</u>

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Charter Communications, Inc.  
Condensed Consolidating Statement of Cash Flows  
For the year ended December 31, 2016

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries			Charter Consolidated
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Eliminations	
NET CASH FLOWS FROM OPERATING ACTIVITIES	\$ (225)	\$ (36)	\$ (463)	\$ (711)	\$ 9,476	\$ —	\$ 8,041
CASH FLOWS FROM INVESTING ACTIVITIES:							
Purchases of property, plant and equipment	—	—	—	—	(5,325)	—	(5,325)
Change in accrued expenses related to capital expenditures	—	—	—	—	603	—	603
Purchases of cable systems, net	(26,781)	(2,022)	—	—	(7)	—	(28,810)
Contribution to subsidiaries	(1,013)	(478)	—	(437)	—	1,928	—
Distributions from subsidiaries	24,552	26,899	—	5,096	—	(56,547)	—
Change in restricted cash and cash equivalents	—	—	22,264	—	—	—	22,264
Other, net	—	—	—	—	(22)	—	(22)
Net cash flows from investing activities	(3,242)	24,399	22,264	4,659	(4,751)	(54,619)	(11,290)
CASH FLOWS FROM FINANCING ACTIVITIES:							
Borrowings of long-term debt	—	—	—	3,201	9,143	—	12,344
Repayments of long-term debt	—	—	—	(2,937)	(7,584)	—	(10,521)
Borrowings (payments) loans payable - related parties	—	(300)	553	(71)	(182)	—	—
Payment for debt issuance costs	—	—	—	(73)	(211)	—	(284)
Issuance of equity	5,000	—	—	—	—	—	5,000
Purchase of treasury stock	(1,562)	—	—	—	—	—	(1,562)
Proceeds from exercise of stock options	86	—	—	—	—	—	86
Settlement of restricted stock units	—	(59)	—	—	—	—	(59)
Purchase of noncontrolling interest	—	(218)	—	—	—	—	(218)
Distributions to noncontrolling interest	—	(96)	—	—	—	—	(96)
Proceeds from termination of interest rate derivatives	—	—	—	—	88	—	88
Contributions from parent	—	1,013	—	478	437	(1,928)	—
Distributions to parent	—	(24,552)	(22,353)	(4,546)	(5,096)	56,547	—
Other, net	—	3	(1)	—	(1)	—	1
Net cash flows from financing activities	3,524	(24,209)	(21,801)	(3,948)	(3,406)	54,619	4,779
NET INCREASE IN CASH AND CASH EQUIVALENTS	57	154	—	—	1,319	—	1,530
CASH AND CASH EQUIVALENTS, beginning of period	—	—	—	—	5	—	5
CASH AND CASH EQUIVALENTS, end of period	\$ 57	\$ 154	\$ —	\$ —	\$ 1,324	\$ —	\$ 1,535

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Charter Communications, Inc.  
Condensed Consolidating Statement of Cash Flows  
For the year ended December 31, 2015

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries				Charter Consolidated
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Unrestricted Subsidiary	Eliminations	
NET CASH FLOWS FROM OPERATING ACTIVITIES	\$ (1)	\$ (5)	\$ (192)	\$ (663)	\$ 3,275	\$ (55)	\$ —	\$ 2,359
CASH FLOWS FROM INVESTING ACTIVITIES:								
Purchases of property, plant and equipment	—	—	—	—	(1,840)	—	—	(1,840)
Change in accrued expenses related to capital expenditures	—	—	—	—	28	—	—	28
Contribution to subsidiaries	(20)	(90)	—	(46)	(24)	—	180	—
Distributions from subsidiaries	26	376	—	715	—	—	(1,117)	—
Change in restricted cash and cash equivalents	—	—	(18,667)	—	—	3,514	—	(15,153)
Other, net	—	(55)	—	—	(12)	—	—	(67)
Net cash flows from investing activities	6	231	(18,667)	669	(1,848)	3,514	(937)	(17,032)
CASH FLOWS FROM FINANCING ACTIVITIES:								
Borrowings of long-term debt	—	—	21,790	2,700	1,555	—	—	26,045
Repayments of long-term debt	—	—	(3,500)	(2,598)	(1,745)	(3,483)	—	(11,326)
Borrowings (payments) loans payable - related parties	—	—	581	(18)	(563)	—	—	—
Payment for debt issuance costs	—	—	(12)	(24)	—	—	—	(36)
Purchase of treasury stock	(38)	—	—	—	—	—	—	(38)
Proceeds from exercise of stock options	30	—	—	—	—	—	—	30
Contributions from parent	—	95	—	15	46	24	(180)	—
Distributions to parent	—	(321)	—	(81)	(715)	—	1,117	—
Net cash flows from financing activities	(8)	(226)	18,859	(6)	(1,422)	(3,459)	937	14,675
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(3)	—	—	—	5	—	—	2
CASH AND CASH EQUIVALENTS, beginning of period	3	—	—	—	—	—	—	3
CASH AND CASH EQUIVALENTS, end of period	\$ —	\$ —	\$ —	\$ —	\$ 5	\$ —	\$ —	\$ 5

**CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2016, 2015 AND 2014**  
(dollars in millions, except share or per share data or where indicated)

Charter Communications, Inc.  
Condensed Consolidating Statement of Cash Flows  
For the year ended December 31, 2014

	Non-Guarantor Subsidiaries			Guarantor Subsidiaries				
	Charter	Intermediate Holding Companies	Safari Escrow Entities	CCO Holdings	Charter Operating and Restricted Subsidiaries	Unrestricted Subsidiary	Eliminations	
NET CASH FLOWS FROM OPERATING ACTIVITIES:	\$ —	\$ (13)	\$ (12)	\$ (665)	\$ 3,086	\$ (37)	\$ —	\$ 2,359
CASH FLOWS FROM INVESTING ACTIVITIES:								
Purchases of property, plant and equipment	—	—	—	—	(2,221)	—	—	(2,221)
Change in accrued expenses related to capital expenditures	—	—	—	—	33	—	—	33
Sales of cable systems, net	—	—	—	—	11	—	—	11
Contribution to subsidiaries	(106)	(600)	—	(100)	(71)	—	877	—
Distributions from subsidiaries	5	30	—	1,132	—	—	(1,167)	—
Change in restricted cash and cash equivalents	—	—	(3,598)	—	—	(3,513)	—	(7,111)
Other, net	—	(5)	—	—	(11)	—	—	(16)
Net cash flows from investing activities	(101)	(575)	(3,598)	1,032	(2,259)	(3,513)	(290)	(9,304)
CASH FLOWS FROM FINANCING ACTIVITIES:								
Borrowings of long-term debt	—	—	3,500	—	1,823	3,483	—	8,806
Repayments of long-term debt	—	—	—	(350)	(1,630)	—	—	(1,980)
Borrowings (payments) loans payable - related parties	—	—	112	(112)	—	—	—	—
Payment for debt issuance costs	—	—	(2)	—	—	(4)	—	(6)
Purchase of treasury stock	(19)	—	—	—	—	—	—	(19)
Proceeds from exercise of options and warrants	123	—	—	—	—	—	—	123
Contributions from parent	—	606	—	100	100	71	(877)	—
Distributions to parent	—	(30)	—	(5)	(1,132)	—	1,167	—
Other, net	—	7	—	—	(4)	—	—	3
Net cash flows from financing activities	104	583	3,610	(367)	(843)	3,550	290	6,927
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	3	(5)	—	—	(16)	—	—	(18)
CASH AND CASH EQUIVALENTS, beginning of period	—	5	—	—	16	—	—	21
CASH AND CASH EQUIVALENTS, end of period	<u>\$ 3</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 3</u>

## 25. Subsequent Events

In January 2017, Charter Operating entered into an amendment to its Credit Agreement decreasing the applicable LIBOR margin on both the term loan E and term loan F to 2.00% and eliminating the LIBOR floor.

In February 2017, CCO Holdings and CCO Holdings Capital Corp. closed on transactions in which they issued \$1.0 billion aggregate principal amount of 5.125% senior notes due May 1, 2027. The net proceeds will be used to redeem CCO Holdings' 6.625% senior notes due 2022, pay related fees and expenses and for general corporate purposes.



10-K 1 d290430d10k.htm 10-K

Table of Contents

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 10-K**

**(Mark One)**

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2016  
OR  
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE TRANSITION PERIOD FROM TO



**COMCAST**

Commission File Number	Registrant; State of Incorporation; Address and Telephone Number	I.R.S. Employer Identification No.
001-32871	<b>COMCAST CORPORATION</b> PENNSYLVANIA One Comcast Center Philadelphia, PA 19103-2838 (215) 286-1700	27-0000798
001-36438	<b>NBCUniversal Media, LLC</b> DELAWARE 30 Rockefeller Plaza New York, NY 10112-0015 (212) 664-4444	14-1682529

**SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:**

Comcast Corporation –

Title of Each Class	Name of Each Exchange on Which Registered
Class A Common Stock, \$0.01 par value	NASDAQ Global Select Market
2.0% Exchangeable Subordinated Debentures due 2029	New York Stock Exchange
5.00% Notes due 2061	New York Stock Exchange
5.50% Notes due 2029	New York Stock Exchange
9.455% Guaranteed Notes due 2022	New York Stock Exchange

NBCUniversal Media, LLC – NONE

**SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:**

Comcast Corporation – NONE  
NBCUniversal Media, LLC – NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Comcast Corporation Yes  No   
NBCUniversal Media, LLC Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Comcast Corporation Yes  No   
NBCUniversal Media, LLC Yes  No

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

Comcast Corporation Yes  No   
NBCUniversal Media, LLC Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, 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).

Comcast Corporation Yes  No   
NBCUniversal Media, LLC Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendments to this Form 10-K.

Comcast Corporation   
NBCUniversal Media, LLC N/A

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

Comcast Corporation Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
NBCUniversal Media, LLC Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

Comcast Corporation  
NBCUniversal Media, LLC

Yes  No   
Yes  No

As of June 30, 2016, the aggregate market value of the Comcast Corporation common stock held by non-affiliates of the registrant was \$155.940 billion. Indicate the number of shares outstanding of each of the registrant's classes of stock, as of the latest practicable date:

As of December 31, 2016, there were 2,366,357,318 shares of Comcast Corporation Class A common stock and 9,444,375 shares of Class B common stock outstanding.

Not applicable for NBCUniversal Media, LLC.

NBCUniversal Media, LLC meets the conditions set forth in General Instruction I(1)(a), (b) and (d) of Form 10-K and is therefore filing this form with the reduced disclosure format.

**DOCUMENTS INCORPORATED BY REFERENCE**

Comcast Corporation – Part III – The registrant's definitive Proxy Statement for its annual meeting of shareholders presently scheduled to be held in June 2017.  
NBCUniversal Media, LLC – NONE

---

Table of ContentsComcast Corporation  
2016 Annual Report on Form 10-K

## Table of Contents

<b>PART I</b>		
Item 1	<u>Business</u>	1
Item 1A	<u>Risk Factors</u>	25
Item 1B	<u>Unresolved Staff Comments</u>	34
Item 2	<u>Properties</u>	34
Item 3	<u>Legal Proceedings</u>	35
Item 4	<u>Mine Safety Disclosures</u>	35
<b>PART II</b>		
Item 5	<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	36
Item 6	<u>Selected Financial Data</u>	39
Item 7	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	40
Item 7A	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	69
Item 8	<u>Comcast Corporation Financial Statements and Supplementary Data</u>	72
Item 9	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	121
Item 9A	<u>Controls and Procedures</u>	121
Item 9B	<u>Other Information</u>	122
<b>PART III</b>		
Item 10	<u>Directors, Executive Officers and Corporate Governance</u>	123
Item 11	<u>Executive Compensation</u>	124
Item 12	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	124
Item 13	<u>Certain Relationships and Related Transactions, and Director Independence</u>	125
Item 14	<u>Principal Accountant Fees and Services</u>	125
<b>PART IV</b>		
Item 15	<u>Exhibits and Financial Statement Schedules</u>	126
	<u>Signatures</u>	135
	<u>NBCUniversal Media, LLC Financial Statements and Supplementary Data</u>	137

**Explanatory Note**

This Annual Report on Form 10-K is a combined report being filed separately by Comcast Corporation ("Comcast") and NBCUniversal Media, LLC ("NBCUniversal"). Comcast owns all of the common equity interests in NBCUniversal, and NBCUniversal meets the conditions set forth in General Instruction I(1)(a), (b) and (d) of Form 10-K and is therefore filing its information within this Form 10-K with the reduced disclosure format. Each of Comcast and NBCUniversal is filing on its own behalf the information contained in this report that relates to itself, and neither company makes any representation as to information relating to the other company. Where information or an explanation is provided that is substantially the same for each company, such information or explanation has been combined in this report. Where information or an explanation is not substantially the same for each company, separate information and explanation has been provided. In addition, separate consolidated financial statements for each company, along with notes to the consolidated financial statements, are included in this report. Unless indicated otherwise, throughout this Annual Report on Form 10-K, we refer to Comcast and its consolidated subsidiaries, including NBCUniversal and its consolidated subsidiaries, as "we," "us" and "our;" Comcast Cable Communications, LLC and its subsidiaries as

**Table of Contents**

"Comcast Cable;" Comcast Holdings Corporation as "Comcast Holdings;" and NBCUniversal, LLC as "NBCUniversal Holdings."

This Annual Report on Form 10-K is for the year ended December 31, 2016. This Annual Report on Form 10-K modifies and supersedes documents filed before it.

The Securities and Exchange Commission ("SEC") allows us to "incorporate by reference" information that we file with it, which means that we can disclose important information to you by referring you directly to those documents. Information incorporated by reference is considered to be part of this Annual Report on Form 10-K. In addition, information that we file with the SEC in the future will automatically update and supersede information contained in this Annual Report on Form 10-K.

Our registered trademarks include Comcast, NBCUniversal and the Comcast and NBCUniversal logos. This Annual Report on Form 10-K also contains other trademarks, service marks and trade names owned by us, as well as those owned by others.

## Table of Contents

### Part I

#### Item 1: Business

We are a global media and technology company with two primary businesses, Comcast Cable and NBCUniversal. We were incorporated under the laws of Pennsylvania in December 2001. Through our predecessors, we have developed, managed and operated cable systems since 1963. In 2011, we acquired control of NBCUniversal from General Electric Company (the "NBCUniversal transaction"), and in 2013, we acquired General Electric Company's remaining interest in NBCUniversal.

We present our operations for Comcast Cable in one reportable business segment, referred to as Cable Communications, and our operations for NBCUniversal in four reportable business segments: Cable Networks, Broadcast Television, Filmed Entertainment and Theme Parks (collectively, the "NBCUniversal segments").

- **Cable Communications:** Consists of the operations of Comcast Cable, which is one of the nation's largest providers of video, high-speed Internet and voice services ("cable services") to residential customers under the XFINITY brand; we also provide these and other services to business customers and sell advertising.
- **Cable Networks:** Consists primarily of our national cable networks, our regional sports and news networks, our international cable networks, and our cable television studio production operations.
- **Broadcast Television:** Consists primarily of the NBC and Telemundo broadcast networks, our NBC and Telemundo owned local broadcast television stations, and our broadcast television studio production operations.
- **Filmed Entertainment:** Consists primarily of the operations of Universal Pictures, which produces, acquires, markets and distributes filmed entertainment worldwide, as well as DreamWorks Animation, which we acquired in August 2016; our films are also produced under the Illumination and Focus Features names.
- **Theme Parks:** Consists primarily of our Universal theme parks in Orlando, Florida and Hollywood, California and our 51% interest in the Universal Studios theme park in Osaka, Japan ("Universal Studios Japan"), which we acquired in November 2015.

Our other business interests consist primarily of Comcast Spectacor, which owns the Philadelphia Flyers and the Wells Fargo Center arena in Philadelphia, Pennsylvania and operates arena management-related businesses. We are also pursuing other business initiatives, such as a wireless phone service that we expect to launch in 2017 using our virtual network operator rights to provide the service over a third party's wireless network.

For financial and other information about our reportable business segments, refer to Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations, Note 17 to Comcast's consolidated financial statements, and Note 16 to NBCUniversal's consolidated financial statements included in this Annual Report on Form 10-K.

#### Available Information and Websites

Comcast's phone number is (215) 286-1700, and its principal executive offices are located at One Comcast Center, Philadelphia, PA 19103-2838. NBCUniversal's phone number is (212) 664-4444, and its principal executive offices are located at 30 Rockefeller Plaza, New York, NY 10112-0015. Comcast and NBCUniversal's

## Table of Contents

Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and any amendments to such reports filed with or furnished to the SEC under Sections 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), are available free of charge on the SEC's website at [www.sec.gov](http://www.sec.gov) and on Comcast's website at [www.comcastcorporation.com](http://www.comcastcorporation.com) as soon as reasonably practicable after such reports are electronically filed with the SEC. The information posted on our websites is not incorporated into our SEC filings. The public may read and copy any materials filed with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

## Description of Our Businesses

### Cable Communications Segment

The table below summarizes certain customer and penetration data for our cable system operations.

December 31 (in millions)	2016	2015	2014
Homes and businesses passed <sup>(a)</sup>	56.4	55.7	54.7
Total customer relationships <sup>(b)</sup>	28.6	27.7	27.0
Single product customers <sup>(b)</sup>	8.5	8.4	8.4
Double product customers <sup>(b)</sup>	9.7	9.2	8.8
Triple product customers <sup>(b)</sup>	10.3	10.1	9.9
Video			
Video customers <sup>(c)</sup>	22.5	22.3	22.4
Video penetration <sup>(d)</sup>	39.9%	40.1%	40.9%
High-speed Internet			
High-speed Internet customers	24.7	23.3	22.0
High-speed Internet penetration <sup>(d)</sup>	43.8%	41.9%	40.2%
Voice			
Voice customers	11.7	11.5	11.2
Voice penetration <sup>(d)</sup>	20.7%	20.6%	20.5%

Basis of Presentation: Customer metrics include our residential and business customers. All percentages are calculated based on actual amounts. Minor differences may exist due to rounding.

- (a) Homes and businesses are considered passed if we can connect them to our distribution system without further extending the transmission lines. Homes and businesses passed is estimated based on the best available information.
- (b) Customer relationships represent the number of residential and business customers that subscribe to at least one of our cable services. Single product, double product and triple product customers represent customers that subscribe to one, two or three of our cable services, respectively. As of December 31, 2016, we had 26.5 million residential customer relationships.
- (c) Generally, a home or business receiving video programming from our distribution system counts as one video customer. For multiple dwelling units ("MDUs") whose residents have the ability to receive additional cable services, such as additional programming choices or our high-definition video ("HD") or digital video recorder ("DVR") advanced services, we count and report customers based on the number of potential billable relationships within each MDU. For MDUs whose residents are not able to receive additional cable services, the MDU is counted as a single customer.
- (d) Penetration is calculated by dividing the number of customers by the number of homes and businesses passed.

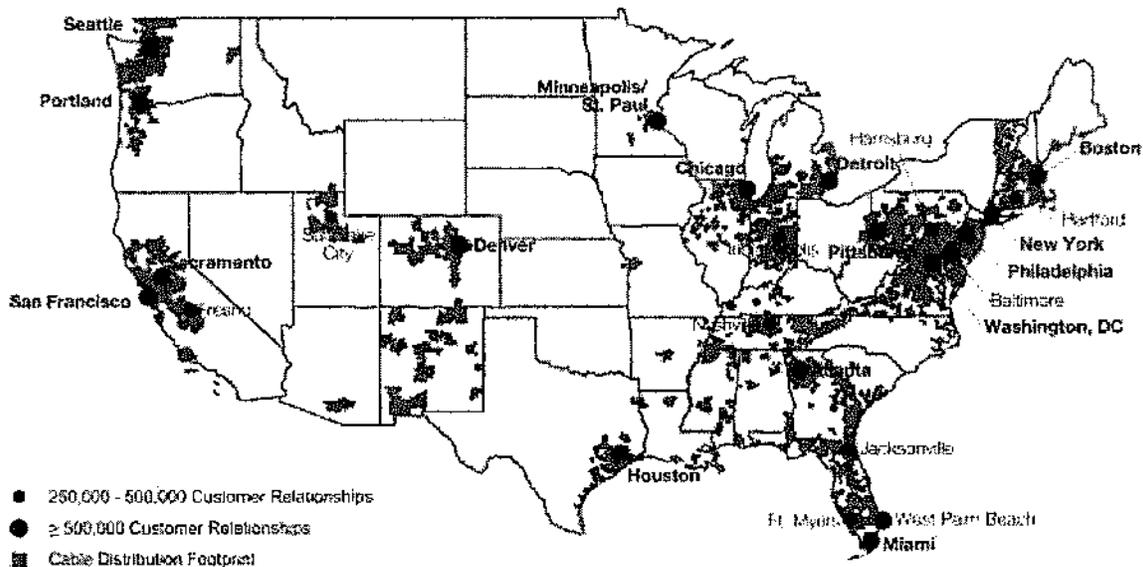
## Table of Contents

### **Cable Services**

We offer our video, high-speed Internet and voice services individually and as bundled services over our cable distribution system to residential and business customers. Our bundled service offerings aim to meet the needs of the various segments of our customer base, ranging from high-speed Internet services packaged with video or streaming services that include a limited number of channels, to a triple product bundle, consisting of our video, high-speed Internet and voice services. We also offer our home security and automation services as a component of our bundled service offerings. Subscription rates and related charges vary according to the services and features customers receive and the type of equipment they use, and customers are typically billed in advance on a monthly basis. The majority of our residential cable services customers are not subject to minimum-term contracts for their services, while substantially all of our business customers are. Minimum-term contracts are typically 2 years in length for residential customers and typically range from 2 to 5 years for business services customers. Customers with minimum-term contracts may only discontinue service in accordance with the terms of their contracts, which typically include an early termination fee.

### **The Areas We Serve**

The map below highlights our footprint as of December 31, 2016 and the designated market areas ("DMAs") in which we offer cable services that have 250,000 or more customer relationships. The locations that are bolded represent the DMAs in which we operate that were also included in the top 25 U.S. television DMAs as of December 31, 2016.



### **Video Services**

We offer a broad variety of video services under the XFINITY brand that provide access to hundreds of channels depending on the customer's level of service. Our levels of service typically range from a limited basic service with access to between 20 and 40 channels to a full service with access to more than 300 channels. Our video services generally include programming provided by national broadcast networks, local broadcast stations, and national and regional cable networks, as well as government and public access programming. We also offer packages that include extensive amounts of foreign-language programming and other specialty tiers of programming with sports, family and international themes. We tailor our video services for a particular geographic area according to applicable local and federal regulatory requirements, programming preferences and demographics.

## Table of Contents

Our video customers may also subscribe to premium networks. Premium networks include networks such as HBO, Showtime, Starz and Cinemax that generally provide, without commercial interruption, movies, original programming, live and taped sporting events and concerts, and other features.

Our video services generally include access to our video on demand service ("On Demand") and an interactive, on-screen program guide. Our On Demand service provides video customers with over 100,000 programming choices over the course of a month, including approximately 40,000 in high definition. A substantial portion of our On Demand content is available at no additional charge; other content, primarily movies and special-events programming, such as sporting events and concerts, can be rented or in some cases purchased to own digitally. We continue to increase the number of On Demand choices we offer.

Our HD service provides customers with high-resolution picture quality, improved audio quality and a wide-screen format through an HD set-top box. Our HD service includes a broad selection of HD programming choices, including major broadcast networks, national cable networks, premium networks and regional sports networks. Our DVR service allows video customers to record and store programs and play them at whatever time is convenient. Our DVR service also provides the ability to pause and rewind live television. We refer to our HD and DVR services as "advanced services."

We are actively deploying set-top boxes for our Internet Protocol ("IP") and cloud-enabled video platform, referred to as our X1 platform. Our X1 platform provides customers with integrated search functionality, personalized recommendations and access to certain third-party Internet applications, such as Netflix. We also offer our cloud DVR technology in substantially all of our markets. Cloud DVR technology allows our video customers to record programming using cloud-based servers and also view those recordings on mobile devices via our mobile apps.

Through our mobile apps and online portal, we offer streaming services that allow our video customers to view certain live programming and On Demand content, browse program listings, and schedule and manage DVR recordings. Depending on the customer's level of service, these services may require an additional monthly fee.

### High-Speed Internet Services

We offer high-speed Internet services with downstream speeds from a range of up to 10 Mbps to fiber-based speeds up to 2 Gbps. These services include access to our online portal and mobile apps, which provide email, an address book, calendars and online security features. We are actively deploying wireless gateways throughout our footprint, which combine a customer's wireless router, cable modem and voice adapter, to improve the performance of multiple IP-enabled devices used at the same time within the home, provide faster Internet speeds and create an in-home Wi-Fi network. We are continuing to expand our network of residential, outdoor and business Wi-Fi hotspots to allow most of our high-speed Internet customers to access our high-speed Internet services inside and outside the home. As of December 31, 2016, there were approximately 15.8 million of these hotspots.

### Voice Services

We offer voice services using an interconnected Voice over Internet Protocol ("VoIP") technology. Our voice services provide either unlimited or usage-based local and domestic long-distance calling and include options for international calling plans, voicemail, voicemail transcriptions, text messaging, caller ID and call waiting. For customers with our high-speed Internet services, our voice services also include the ability to access and manage voicemail, text messaging and other account features through our online portal or mobile apps.

## Table of Contents

### **Business Services**

We offer our cable services to small and medium-sized businesses and to large enterprises with multiple locations. Our large enterprise business services are designed for Fortune 1000 companies and other large enterprises with multiple locations both within and outside of our cable distribution footprint. We service these multiple locations through agreements with other cable companies to use their networks to provide coverage outside of our service areas. In addition to the features available to our residential cable services customers, our services for business customers include an interactive tool that allows customers to store, share, and collaborate on files online, hosted voice services that use cloud network servers, a business directory listing, and additional capacity for multiple phone lines.

We offer Ethernet network services that connect multiple locations and provide higher downstream and upstream speed options to medium-sized businesses and large enterprises. We also provide cellular backhaul services to mobile network operators to help those customers manage network bandwidth.

### **Advertising**

As part of our distribution agreements with cable networks, we generally receive an allocation of scheduled advertising time on cable networks that we sell through our advertising business, Spotlight, to local, regional and national advertisers. In most cases, the available advertising units are sold by our sales force. In some cases, we work with representation firms as an extension of our sales force to sell a portion of the advertising units allocated to us. We also represent the advertising sales efforts of other multichannel video providers in some markets. In addition, we generate revenue from the sale of advertising online and on our On Demand service.

### **Other**

We also offer home security and automation services that provide home monitoring services and the ability to manage other functions within the home, such as lighting and room temperature, through our online portal or our mobile apps.

### **Technology**

Our cable distribution system uses a hybrid fiber-optic and coaxial cable network that we believe is sufficiently flexible and scalable to support our future technology requirements. This network provides the two-way transmissions that are essential to providing high-speed Internet services, interactive video services, such as On Demand, and voice services.

We continue to focus on technology initiatives, including:

- developing and deploying next-generation media and content delivery platforms, such as our X1 platform and related cloud DVR technology, that use IP technology and our own cloud network servers to deliver video and advanced search capabilities, including through a voice-activated remote control, and allow access to certain third-party Internet applications
- deploying wireless gateways to improve the performance of multiple IP-enabled devices used at the same time within the home, provide faster Internet speeds and create an in-home Wi-Fi network
- expanding our network of residential, outdoor and business Wi-Fi hotspots
- developing multiple tools to recapture bandwidth and optimize our network to allow for faster Internet speeds and capacity, including using advanced video encoding and digital compression technologies and DOCSIS innovations, such as DOCSIS 3.1

## Table of Contents

- developing and deploying various technology and software tools to improve the customer experience

### **Sources of Supply**

To offer our video services, we license a substantial portion of our programming from cable networks and broadcast networks, as well as from local broadcast television stations. We attempt to secure long-term programming distribution agreements with these programming providers. We seek to include in our distribution agreements the rights to offer such programming through multiple delivery platforms that may be used in a variety of locations, such as through On Demand, our online portal, our mobile apps, and our streaming services.

For our high-speed Internet services, we license software products, such as email and security software, and content, such as news feeds for our online portal, from a variety of suppliers. Under our contracts with these suppliers, we generally pay on a fixed-fee basis, on a per subscriber basis in the case of software product licenses or on a video advertising revenue share basis in the case of content licenses.

For our voice services, we license software products such as voicemail and text messaging from a variety of suppliers under multiyear contracts. The fees we pay are generally based on the consumption of the related services.

We purchase from a limited number of suppliers a significant number of set-top boxes and certain other customer premise equipment, network equipment and services to provide our cable services and our home security and automation services to residential and business customers.

We use two primary vendors to provide customer billing for our cable services to our residential and business customers.

### **Customer and Technical Services**

Our customer service call centers provide 24/7 call-answering capability, telemarketing and other services. Our technical services group performs various tasks, including installations, plant maintenance and upgrades to our cable distribution system.

### **Sales and Marketing**

We offer our services directly to residential and business customers through customer service call centers, customer service centers, our website, door-to-door selling, telemarketing and retail outlets, as well as through advertising via direct mail, television and the Internet.

## **NBCUniversal Segments**

---

### **Cable Networks**

Our Cable Networks segment consists of a diversified portfolio of national cable networks that provide a variety of entertainment, news and information, and sports content, our regional sports and news networks, our international cable networks, and our cable television studio production operations. We also own related digital media properties, which primarily include brand-aligned websites.

## Table of Contents

The table below presents a summary of our national cable networks and their advertising reach to U.S. households.

Cable Network	Approximate U.S. Households as of December 31 (in millions) <sup>(a)</sup>			Description of Programming
	2016	2015	2014	
USA Network	92	94	96	General entertainment
MSNBC	91	92	95	News and information
E!	90	92	94	Entertainment and pop culture
Syfy	90	92	95	Imagination-based entertainment
CNBC	89	91	94	Business and financial news
Bravo	88	90	92	Entertainment, culture and arts
NBC Sports Network	83	83	81	Sports
Golf Channel	78	77	79	Golf competition and golf entertainment
Oxygen	76	77	78	Women's interests
Sprout	59	56	58	Children's entertainment
Esquire Network <sup>(b)</sup>	58	68	70	Men's lifestyle and entertainment
Chiller	37	38	39	Horror and suspense
CNBC World	36	36	38	Global financial news
Universal HD	30	29	31	General entertainment HD programming
Cloo <sup>(b)</sup>	24	25	26	Crime, mystery and suspense

(a) Household data is based on The Nielsen Company's January reports, except for Universal HD, which is derived from information provided by multichannel video providers. Household data for 2016 is derived from information available during the period from November 28, 2016 through December 25, 2016.

(b) In January 2017, we announced plans to convert the Esquire Network to an online-only format in 2017 and we ceased operations of the Cloo network.

Our regional sports and news networks together serve more than 27 million households across the United States, including key markets such as Baltimore/Washington, Boston, Chicago, Philadelphia, Portland, Sacramento and San Francisco.

We market and distribute our cable network programming in the United States and internationally to traditional and virtual multichannel video providers, as well as to subscription video on demand services, such as those offered by Amazon, Hulu and Netflix. These distributors may provide our content on television, including via video on demand services, online and through mobile apps.

Our cable networks produce their own programs or acquire the rights to programming from third parties, including sports programming rights that are discussed below under the heading "Broadcast Television." Our cable television studio production operations identify, develop and produce original content for our cable networks and third parties. We license this content to cable networks, broadcast networks and subscription video on demand services and it is sold on standard-definition DVDs and Blu-ray discs (together, "DVDs") and through digital distribution services such as iTunes.

### **Broadcast Television**

Our Broadcast Television segment operates the NBC and Telemundo broadcast networks, which together serve viewers and advertisers in all 50 states. Our Broadcast Television segment also includes our owned NBC and Telemundo local broadcast television stations, the NBC Universo national cable network, our broadcast television studio production operations, and related digital media properties.

## Table of Contents

### NBC Network

The NBC network distributes entertainment, news and sports programming that reaches viewers in virtually all U.S. television households through more than 200 affiliated stations across the United States, including our 10 owned NBC-affiliated local broadcast television stations. The NBC network's programming library consists of rights of varying nature to more than 100,000 episodes of popular television content, including current and classic titles, unscripted programming, sports, news, long-form and short-form programming, and locally produced programming from around the world. In addition, the NBC network owns related digital media properties, which primarily include brand-aligned websites.

The NBC network produces its own programs or acquires the rights to programming from third parties. NBCUniversal has various contractual commitments for the licensing of rights to multiyear programming, primarily sports programming. Our most significant sports programming commitments include the U.S. broadcast rights for the summer and winter Olympic Games through 2032 and agreements with the NFL to produce and broadcast a specified number of regular season and playoff games, including *Thursday Night Football* through the 2017-18 season, *Sunday Night Football* through the 2022-23 season and the 2018 and 2021 Super Bowl games. We also have U.S. broadcast rights to a specified number of NHL games through the 2020-21 season, English Premier League soccer through the 2021-22 season, certain NASCAR events through 2024 and certain PGA TOUR and other golf events through 2030. NBCUniversal's sports programming agreements also include the rights to distribute content on our national cable networks, including the NBC Sports Network and Golf Channel, on our regional sports networks, and online, including through our mobile apps.

Our broadcast television studio production operations develop and produce original content, including scripted and unscripted programming series and talk shows. This original content is licensed to broadcast networks, cable networks and local broadcast television stations owned by us and third parties, as well as to subscription video on demand services, and it is sold on DVDs and through digital distribution services both in the United States and internationally. We also produce first-run syndicated shows for local markets that are broadcast on local broadcast television stations in the United States on a market-by-market basis. We currently distribute some of our television programs after their initial broadcast, as well as older television programs from our library, to local broadcast television stations and cable networks in the off-network syndication market.

## Table of Contents

### *NBC Local Broadcast Television Stations*

As of December 31, 2016, we owned and operated 10 NBC-affiliated local broadcast television stations that collectively reached approximately 31 million U.S. television households, which represent approximately 27% of U.S. television households. In addition to broadcasting the NBC network's national programming, our local broadcast television stations produce news, sports, public affairs and other programming that addresses local needs and acquire syndicated programming from other sources. The table below presents a summary of the NBC-affiliated local broadcast television stations that we owned and operated as of December 31, 2016.

DMA Served <sup>(a)(b)</sup>	Station	General Market Rank <sup>(c)</sup>	Percentage of U.S. Television Households <sup>(d)</sup>
New York, NY	WNBC	1	6%
Los Angeles, CA	KNBC	2	5%
Chicago, IL	WMAQ	3	3%
Philadelphia, PA	WCAU	4	3%
Dallas-Fort Worth, TX	KXAS	5	2%
San Francisco-Oakland-San Jose, CA	KNTV	6	2%
Washington, D.C.	WRC	7	2%
Miami-Ft. Lauderdale, FL	WTVJ	16	1%
San Diego, CA	KNSD	28	1%
Hartford, CT	WVIT	30	1%

(a) DMA served is defined by Nielsen Media Research as a geographic market for the sale of national spot and local advertising time.

(b) On January 1, 2017, we launched a new owned and operated NBC-affiliated local broadcast television station in the Boston market that reaches approximately 2 million U.S. television households. Boston's general market rank is No. 9, which represents approximately 2% of U.S. television households.

(c) General market rank is based on the relative size of the DMA among the 210 generally recognized DMAs in the United States based on Nielsen estimates for the 2016-17 season.

(d) Based on Nielsen estimates for the 2016-17 season. The percentage of U.S. television households does not reflect the calculation of national audience reach under the Federal Communications Commission's ("FCC") national television ownership cap limits. See "Legislation and Regulation — Broadcast Television — Ownership Limits — National Television Ownership."

### *Telemundo*

Telemundo is a leading Hispanic media company that produces, acquires and distributes Spanish-language content in the United States and internationally. Telemundo's operations include the Telemundo network, its 17 owned local broadcast television stations and the NBC Universo national cable network.

The Telemundo network is a leading Spanish-language broadcast network featuring original telenovelas, movies, news, specials and sporting events. Telemundo develops original programming primarily through its production studio and also acquires the rights to programming from third parties. It holds the Spanish-language U.S. broadcast rights to FIFA World Cup soccer through 2026 and the Spanish-language U.S. broadcast rights for certain NFL games that the NBC network will broadcast through the 2022-23 season.

## Table of Contents

### Telemundo Local Broadcast Television Stations

As of December 31, 2016, Telemundo owned 17 local broadcast television stations, including 16 local broadcast television stations affiliated with the Telemundo network, which collectively reached approximately 59% of U.S. Hispanic television households as of December 31, 2016, and an independent television station in Puerto Rico. The table below presents a summary of these local broadcast television stations.

DMA Served <sup>(a)</sup>	Station	Hispanic Market Rank <sup>(b)</sup>	Percentage of U.S. Hispanic Television Households <sup>(c)</sup>
Los Angeles, CA	KVEA	1	13%
New York, NY	WNJU	2	10%
Miami, FL	WSCV	3	5%
Houston, TX	KTMD	4	5%
Dallas-Fort Worth, TX	KXTX	5	4%
Chicago, IL	WSNS	6	4%
San Antonio, TX	KVDA	7	3%
San Francisco-Oakland-San Jose, CA	KSTS	8	3%
Phoenix, AZ	KTAZ	9	3%
Harlingen-Brownsville-McAllen, TX	KTLM	10	2%
Fresno, CA	KNSO <sup>(d)</sup>	14	2%
Philadelphia, PA	WWSI	16	2%
Denver, CO	KDEN	17	2%
Boston, MA	WNEU	21	1%
Las Vegas, NV	KBLR	24	1%
Tucson, AZ	KHRR	26	1%
Puerto Rico	WKAQ	N/A	N/A

(a) DMA served is defined by Nielsen Media Research as a geographic market for the sale of national spot and local advertising time.

(b) Hispanic market rank is based on the relative size of the DMA among approximately 15.1 million U.S. Hispanic households based on Nielsen estimates for the 2016-17 season.

(c) Based on Nielsen estimates for the 2016-17 season. The percentage of U.S. Hispanic television households does not reflect the calculation of national audience reach under the FCC's national television ownership cap limits. See "Legislation and Regulation — Broadcast Television — Ownership Limits — National Television Ownership."

(d) Operated by a third party that provides certain non-network programming and operations services under a time brokerage agreement.

### Filmed Entertainment

Our Filmed Entertainment segment primarily produces, acquires, markets and distributes filmed entertainment worldwide, and it also develops, produces and licenses live stage plays.

We produce films both on our own and jointly with other studios or production companies, as well as with other entities. Our films are produced primarily under the Universal Pictures, Illumination and Focus Features names, and in August 2016, we acquired DreamWorks Animation. Our films are marketed and distributed worldwide primarily through our own marketing and distribution operations. We also acquire distribution rights to films produced by others, which may be limited to particular geographic regions, specific forms of media or certain periods of time. Our content includes theatrical films, direct-to-video movies and our film library, which is comprised of more than 5,000 movies in a variety of genres.

We have entered into, and may continue to enter into, film cofinancing arrangements with third parties, including both studio and nonstudio entities, to jointly finance or distribute certain of our film productions. These arrangements can take various forms, but in most cases involve the grant of an economic interest in a film to an investor. Investors generally assume the full risks and rewards of ownership proportionate to their ownership in the film.

## Table of Contents

The majority of our produced and acquired films are initially distributed for exhibition in movie theaters. After their release in movie theaters, we sell and license our films through various methods. We distribute our films globally by selling them on DVDs to retail stores, rental kiosks and subscription by mail services and by selling them through digital distribution services and video on demand services provided by multichannel video providers, including our Cable Communications segment. We also license our films, including selections from our film library, to cable, broadcast and premium networks, to subscription video on demand services, and to video on demand and pay-per-view services. The number of films that we license through subscription video on demand services is increasing as consumers continue to seek additional ways to view our content.

### **Theme Parks**

Our Theme Parks segment consists primarily of our Universal theme parks in Orlando, Florida and Hollywood, California and our 51% interest in Universal Studios Japan, which we acquired in November 2015. Universal Orlando includes two theme parks, Universal Studios Florida and Universal's Islands of Adventure, as well as Universal CityWalk Orlando, a dining, retail and entertainment complex. Universal Orlando also features on-site themed hotels in which we own a noncontrolling interest. Our Universal theme park in Hollywood, California consists primarily of Universal Studios Hollywood, as well as Universal CityWalk Hollywood. We continue to expand our theme park business internationally, such as through our plans to develop a Universal Studios theme park in Beijing, China along with a consortium of Chinese state-owned companies. In addition, we license the right to use the Universal Studios brand name and other intellectual property, and also provide other services, to third parties that own and operate the Universal Studios Singapore theme park on Sentosa Island, Singapore. We also owned a water park, Wet 'n Wild in Orlando, Florida, which closed on December 31, 2016, and are developing a new water park, Volcano Bay, in Orlando, Florida, that we plan to open in mid-2017.

Our Theme Parks segment licenses the right to use a substantial amount of intellectual property from third parties for its themed elements in rides, attractions and merchandising.

### **Competition**

All of our businesses operate in intensely competitive, consumer-driven and rapidly changing environments and compete with a growing number of companies that provide a broad range of communications products and services, and entertainment, news and information products and services, to consumers. Technological changes are further intensifying and complicating the competitive landscape for all of our businesses by challenging existing business models and affecting consumer behavior.

### **Cable Communications**

Competition for our cable services consists primarily of direct broadcast satellite ("DBS") providers, which have a national footprint and compete in all of our service areas, and phone companies with fiber-based networks, which overlap approximately 60% of our service areas and are continuing to expand the areas they serve. Many of these competitors offer features, pricing and packaging for these services, individually and in bundles, comparable to what we offer, and some of these traditional competitors also offer smaller online-only video packages. In 2015, AT&T, one of our largest phone company competitors, acquired DIRECTV, the nation's largest DBS provider, which created an even larger competitor to our cable services and has enabled it to enhance its bundled offerings with video, high-speed Internet, and wireline and wireless phone services. AT&T also announced in 2016 a proposed merger with Time Warner Inc., a media and entertainment company, which competes with our NBCUniversal businesses.

Current and future wireless Internet services, such as 3G, 4G and 5G wireless broadband services and Wi-Fi networks, may compete with our high-speed Internet services, and our voice services are facing increased competition as customers replace wireline phones with wireless phones and Internet-based phone services such as Skype.

## Table of Contents

There also continue to be new companies, some with significant financial resources, that offer or are seeking to offer services that potentially may compete with some or all of our cable services. For example, Google has launched high-speed Internet and video services in a limited number of areas in which we operate and other companies continue to emerge that provide Internet streaming and downloading of video programming, some of which charge a nominal or no fee.

### Video Services

We compete with a number of different sources that provide news, sports, information and entertainment programming to consumers, including:

- DBS providers, including AT&T's DIRECTV and DISH Network, that transmit satellite signals to substantially all U.S. households to provide video programming and other information similar to our video services
- phone companies, including AT&T and Verizon, that have built and continue to build fiber-based networks that provide cable services similar to ours, which overlap a substantial portion of our service areas, and that in some cases offer bundled offerings that include wireless phone services
- online video distributors that offer online services and devices that enable Internet streaming and downloading of movies, television shows and other video programming, including linear and video on demand programming, and generally involve the offering of smaller packages of programming networks at prices lower than our traditional video service package offerings
- other providers that build and operate wireline communications systems in the same communities that we serve, including those operating as franchised cable operators
- satellite master antenna television systems that offer to their subscribers both improved reception of local broadcast television stations and much of the programming offered by our cable systems and generally serve MDUs, office complexes and residential developments
- other companies, such as local broadcast television stations, that provide multiple channels of free over-the-air programming, as well as video rental services and home entertainment and gaming products

### High-Speed Internet Services

We compete with a number of companies offering Internet services, including:

- wireline phone companies
- Internet service providers
- wireless phone companies and other providers of wireless Internet service
- satellite broadband providers
- power companies
- municipal broadband networks

Some phone companies, such as AT&T, CenturyLink, Frontier and Verizon, have built and are continuing to build fiber-based network infrastructure farther into their networks, which allows them to provide data trans-

## Table of Contents

mission speeds that exceed those that can be provided with traditional digital subscriber line ("DSL") technology, and are now offering these higher-speed services in many of our service areas. Certain companies that offer DSL service have increased data transmission speeds, lowered prices or created bundled services to compete with our high-speed Internet services.

Google has launched a fiber-to-the-home network that provides high-speed Internet services in a limited number of areas in which we operate, and certain municipalities in our service areas are also building fiber-based networks.

Various wireless companies are offering Internet services using a variety of network types, including 3G and 4G, and in the future 5G, wireless broadband services and Wi-Fi networks. These networks work with devices such as smartphones, laptops, tablets and mobile wireless routers, as well as wireless data cards. A growing number of commercial venues, such as retail malls, restaurants and airports, also offer Wi-Fi service. Numerous local governments are also considering or actively pursuing publicly subsidized Wi-Fi and other Internet access networks. The availability of these wireless offerings could negatively impact the demand for our high-speed Internet services.

### Voice Services

Our voice services compete with wireline and wireless phone companies, including incumbent local exchange carriers ("ILECs") and competitive local exchange carriers ("CLECs"), and other Internet-based and VoIP service providers. Certain phone companies, such as the ILECs AT&T and Verizon, have substantial capital and other resources, longstanding customer relationships, and extensive existing facilities and network rights-of-way. A few CLECs also have existing local networks and significant financial resources. In addition, we are increasingly competing with other phone service providers as customers replace traditional wireline phone services with wireless and Internet-based phone services.

### Business Services

Our business services primarily compete with a variety of phone companies, including ILECs and CLECs. These companies either operate their own network infrastructure or rely on reselling all or part of another carrier's network. We also compete with satellite operators who offer video services to businesses.

## **NBCUniversal Segments**

### Cable Networks and Broadcast Television

Our cable networks, broadcast networks and owned local broadcast television stations compete for viewers' attention and audience share with all forms of programming provided to viewers, including cable, broadcast and premium networks; subscription video on demand services; local broadcast television stations; home entertainment products; pay-per-view and video on demand services; online activities, such as social networking and viewing user-generated content; gaming products; and other forms of entertainment, news and information.

Our cable networks, broadcast networks and owned local broadcast television stations compete for the acquisition of programming and for on-air and creative talent with other cable and broadcast networks, local television stations and subscription video on demand services. The market for programming is very competitive, particularly for sports programming, where the cost for such programming is significant.

Our cable networks compete with other cable networks and programming providers for carriage of their programming by multichannel video providers and subscription video on demand services. Our broadcast networks compete with the other broadcast networks in markets across the United States to secure affiliations with independently owned television stations, which are necessary to ensure the effective distribution of broadcast network programming to a nationwide audience.

## Table of Contents

In addition, our cable television and broadcast television studio production operations compete with other production companies and creators of content for the acquisition of story properties, for creative, performing and technical personnel, and for distribution of, and consumer interest in, their content.

### Filmed Entertainment

Our filmed entertainment business competes for audiences for its films and other entertainment content with other major studios and, to a lesser extent, with independent film producers, as well as with alternative forms of entertainment. Our competitive position primarily depends on the number of films we produce, their distribution and marketing success, and consumer response. Our filmed entertainment business also competes to obtain creative, performing and technical talent, including writers, actors, directors and producers, as well as scripts for films. Our filmed entertainment business also competes with the other major studios and other producers of entertainment content for the exhibition of its films in theaters and for premium network and digital distribution of its films.

### Theme Parks

Our theme parks business competes with other multi-park entertainment companies. We also compete with other providers of entertainment, lodging, tourism and recreational activities. To help maintain the competitiveness of our theme parks, we have invested and continue to invest in existing and new theme park attractions, hotels and infrastructure.

### Advertising

Our cable communications business, cable networks, broadcast networks, and owned local broadcast television stations compete for the sale of advertising with other television networks and stations, as well as with all other advertising platforms, such as digital, radio and print media. The willingness of advertisers to purchase advertising from us may be adversely affected by lower audience ratings at our cable networks, broadcast networks and owned local broadcast television stations. Declines in advertising revenue also can be caused by increased competition for the leisure time of viewers and audience fragmentation and from the growing use of technologies such as DVRs and video on demand services, which give consumers greater flexibility to watch programming on a time-delayed or on-demand basis or to fast-forward or skip advertisements within programming; from subscription video on demand services; and from other online programming.

### Seasonality and Cyclicity

---

Each of our businesses is subject to seasonal and cyclical variations. See Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations and refer to the "Seasonality and Cyclicity" discussion within that section for additional information.

## Legislation and Regulation

The Communications Act of 1934, as amended (the "Communications Act"), and FCC regulations and policies affect significant aspects of our businesses. Our businesses are also subject to other regulation by federal, state, local and foreign authorities and to agreements we enter into with local cable franchising authorities. In addition, we must comply with the terms, conditions and commitments of the FCC Order that approved the NBCUniversal transaction in January 2011 (the "NBCUniversal Order") and a consent decree entered into between us, the Department of Justice ("DOJ") and five states (the "NBCUniversal Consent Decree") in September 2011, which contain conditions and commitments of varying duration, ranging from three to seven years thereafter.

Legislators and regulators at all levels of government frequently consider changing, and sometimes do change, existing statutes, rules or regulations, or interpretations of existing statutes, rules or regulations, or

## Table of Contents

prescribe new ones, any of which may significantly affect our businesses. In addition, in recent years, the FCC and certain states have been more active in considering rulemakings and legislation, as well as in conducting inquiries and reviews, regarding our services. Any future legislative, judicial, regulatory or administrative actions may increase our costs or impose additional restrictions on our businesses, some of which may be significant. Congress may consider proposals to address communications issues, including whether it should rewrite the entire Communications Act to account for changes in the communications marketplace, whether it should address the FCC's authority to implement or enforce open Internet regulations, and whether it should fund new broadband infrastructure. We are unable to predict the effects of any of these or any other further legislative requirements on our businesses. In addition, with the new Administration in place, the FCC and other agencies may pursue new regulations or seek changes to, or the elimination of, existing regulations, such as the classification of broadband Internet service and requirements relating to the Internet and privacy. We cannot predict what changes will be sought and, if adopted, how they will affect our businesses.

The following paragraphs summarize material existing and potential future legal and regulatory requirements affecting our businesses, although reference should be made to the Communications Act, FCC regulations, the NBCUniversal Order, the NBCUniversal Consent Decree, and other legislation and regulations for further information.

### **Cable Communications Segment**

---

#### **Video Services**

##### **Program Carriage**

Cable operators and other multichannel video providers are prohibited from requiring as a condition of carriage a financial interest in, or exclusive distribution rights for, a video programming network. In addition, FCC regulations, as well as the NBCUniversal Order, prohibit us from unreasonably restraining the ability of an unaffiliated video programming network to compete fairly by discriminating against the network on the basis of its non-affiliation in the selection, terms or conditions for its carriage. We have been involved in program carriage disputes at the FCC and may be subject to new complaints in the future.

##### **Must-Carry/Retransmission Consent**

Cable operators are required to carry, without compensation, programming transmitted by most local commercial and noncommercial broadcast television stations. As an alternative to this "must-carry" requirement, local broadcast television stations may choose to negotiate with the cable operator for "retransmission consent," under which the station gives up its must-carry rights and instead seeks to negotiate a carriage agreement with the cable operator, which frequently will involve payments to the station. We currently pay certain local broadcast television stations in exchange for their required consent for the retransmission of the stations' broadcast programming to our video services customers and expect to continue to be subject to demands for increased payment and other concessions from local broadcast television stations. For information on must-carry and retransmission consent issues relating to our broadcast television business, see "NBCUniversal Segments — Broadcast Television" below and refer to the "Must-Carry/Retransmission Consent" discussion within that section.

##### **Pricing and Packaging**

In 2015, the FCC revised its rate regulations to create a presumption that all local communities are subject to effective competition and should no longer be subject to rate regulation that limits prices cable operators may charge for basic video service, equipment and installation. That decision has been appealed in federal court. While the FCC has accepted a certification from a Massachusetts franchising authority that demonstrated an absence of effective competition in a number of the communities we serve in Massachusetts that will allow for

## Table of Contents

continued rate regulation in those communities, all of the other areas we serve are unregulated. In addition to the FCC's rate regulation rules, certain state entities monitor and may challenge the marketing and advertising of our services. For example, in 2016, the Washington State Attorney General filed suit in state court alleging our service protection plan, an optional plan that protects customers from incurring charges for service visits to diagnose and repair installed in-home wiring for residential cable services, violates state consumer protection laws.

### Cable Equipment

The Communications Act includes provisions aimed at promoting the retail availability of set-top boxes and other equipment that can be used to receive digital video services. In 2016, the FCC launched a rulemaking to consider proposed technology mandates on multichannel video providers aimed at enabling third-party retail video devices to access a provider's video service without the need for a provider-supplied set-top box. If implemented, these mandates would impose substantial costs on us, impair our ability to innovate and have other adverse effects on our business. It is unclear whether the FCC under the new Administration will pursue this proceeding or adopt these rules.

### Pole Attachments

The FCC regulates the rates, terms and conditions that most pole-owning utility companies charge cable operators and telecommunications carriers, including broadband Internet access service providers such as us, for allowing attachments to their poles. States are permitted to preempt FCC jurisdiction and regulate the rates, terms and conditions of attachments themselves, and many states in which we operate have done so. Most of these states have generally followed the FCC's pole attachment rate standards, which set rates for telecommunications service pole attachments to levels at or near the rates for cable service attachments. In 2015, the FCC eliminated the ability of utility companies to justify higher rates for telecommunication service pole attachments. Cable operators had requested this FCC action because the FCC's new open Internet regulations, as described below under the heading "Open Internet Regulations", reclassified Internet access service as a telecommunications service, which could have allowed for higher rental rates to be applied to a majority of our pole attachments. The FCC's order ensuring that pole rates for telecommunications service attachments approximate the cable service pole rate has been appealed in federal court by the utility companies. Some municipalities have enacted "one-touch" make ready pole attachment ordinances, which permit third parties to alter components of our network attached to utility poles in ways that could adversely affect our businesses. We and other providers have filed complaints in federal court challenging these ordinances.

### Franchising

Cable operators generally operate their cable systems under nonexclusive franchises granted by local or state franchising authorities. While the terms and conditions of franchises vary materially from jurisdiction to jurisdiction, franchises typically last for a fixed term, obligate the franchisee to pay franchise fees and meet service quality, customer service and other requirements, and are terminable if the franchisee fails to comply with material provisions. Franchising authorities also may establish reasonable requirements for public, educational and governmental access programming, and some of our franchises require substantial channel capacity and financial support for this programming. The Communications Act also contains provisions governing the franchising process, including renewal procedures designed to protect incumbent franchisees against arbitrary denials of renewal. We believe that our franchise renewal prospects are generally favorable but cannot guarantee the future renewal of any individual franchise.

Approximately half of the states in which we operate provide for statewide franchising or have simplified local franchising requirements for new entrants. Some allow new entrants to operate on more favorable terms than our current operations, for instance by not requiring that the new entrant provide service to all parts of the franchise area or permitting the new entrant to designate only those portions it wishes to serve. Certain states allow incumbent cable operators such as us to opt in to the new state franchise immediately or later.

## Table of Contents

when a competing state franchise has been issued, although even in those states, incumbent cable operators may be required to retain certain franchise obligations that are more burdensome than the new entrant's state franchise.

### **High-Speed Internet Services**

We provide high-speed Internet services to our customers. Many of these services are subject to a number of regulatory obligations described below, including open Internet regulations prescribed by the FCC and certain common carrier regulations under Title II of the Communications Act. As an Internet service provider ("ISP"), we are also subject to a requirement to implement certain network capabilities to assist law enforcement in conducting surveillance of persons suspected of criminal activity. From time to time, the FCC considers imposing new regulatory obligations on ISPs, including, for example, proposals to require broadband network outage reporting. New broadband regulations, if adopted, may have adverse effects on our businesses.

#### Open Internet Regulations

In 2015, the FCC reclassified broadband Internet access service as a "telecommunications service" subject to new open Internet regulations and certain common carrier regulations under Title II of the Communications Act, including requirements that charges and practices of ISPs for and in connection with broadband Internet access service be just, reasonable and not unjustly or unreasonably discriminatory. However, the FCC refrained from implementing a number of utility-style regulations that might otherwise apply under Title II, such as rate regulation, tariffs and unbundling requirements.

The new open Internet regulations bar ISPs from blocking access to lawful content, applications, services or non-harmful devices; prohibit ISPs from impairing or degrading lawful Internet traffic on the basis of content, applications or services, or impairing or degrading the use of non-harmful devices; prohibit ISPs from favoring lawful traffic from one provider of Internet content, applications or services (called an "edge provider") over lawful traffic of another edge provider in exchange for consideration ("paid prioritization"); establish a new "general conduct standard" that prohibits ISPs from unreasonably interfering with or unreasonably disadvantaging the ability of consumers to select, access and use the lawful Internet content, applications, services or devices of their choosing or of edge providers to make lawful content, applications, services or devices available to consumers; and require ISPs to disclose information regarding network management, performance and commercial terms of the service. In addition, interconnection arrangements, which govern how Internet traffic is exchanged between high-speed Internet networks and provide direct, dedicated interconnection capacity to edge providers, are now subject to FCC oversight under Title II of the Communications Act. All of these regulations are subject to FCC enforcement and could give rise to third-party claims for damages or equitable relief. These requirements could adversely affect our business, although the extent to which they do so will depend upon the manner in which the FCC interprets and enforces them.

In June 2016, a panel of the United States Court of Appeals for the District of Columbia affirmed the FCC's new open Internet regulations on appeal. Petitions have been filed requesting a rehearing of the decision. In addition, Congress may consider legislation addressing these regulations, and the FCC under the new Administration may also revisit the rules. We cannot predict whether or how the rules might be changed. States have attempted, and may continue to attempt, to use the FCC's open Internet decision to justify imposing new regulations and taxes and fees on ISPs that could adversely affect our business.

Separate and apart from the FCC's new open Internet regulations, we committed to be bound by the FCC's original "open Internet" regulations adopted in 2010 as a condition of the NBCUniversal Order and the NBCUniversal Consent Decree until 2018, although we did not agree to be bound by any future open Internet regulations. As a result, among other things, we cannot block access to lawful Internet content, applications, services or non-harmful devices or unreasonably discriminate in transmitting lawful Internet network traffic, although we may engage in reasonable network management.

## **Table of Contents**

### **Business Data Services**

In April 2016, the FCC proposed new regulations for "business data services" (formerly "special access" services), which provide dedicated point-to-point transmission of data at certain guaranteed speeds and service levels using high-capacity connections. The FCC proposed new rate regulation and other regulatory mandates that could apply to business data services offered by cable companies. The proposed rules or any variation of the proposed rules, if implemented, could impose substantial costs on us and have other significant adverse effects on our business. It is uncertain whether the FCC under the new Administration will pursue this proceeding or adopt these rules.

### **NBCUniversal Order/Consent Decree Conditions**

The NBCUniversal Order and NBCUniversal Consent Decree include various conditions and commitments requiring us to offer all of our broadband Internet access service speed tiers on a stand-alone basis at reasonable market-based prices, to maintain a broadband Internet access service of at least 12 Mbps downstream across most of our footprint, and to avoid discrimination in how we treat "specialized services" (defined as services we provide over the same last-mile facilities as our broadband Internet access service, but not including our broadband Internet access service, video services or voice services).

### **Municipally Owned Broadband Networks**

A number of local municipalities operate municipally-owned broadband networks. Certain states have enacted laws that restrict or prohibit local municipalities from operating municipally owned broadband networks. The FCC's efforts to preempt such laws in Tennessee and North Carolina were overturned in 2016 by the United States Court of Appeals for the Sixth Circuit. However, there may be further efforts by local governments to expand or create government-owned networks and there may also be efforts in state legislatures to restrict the development of government-owned networks or to ease or facilitate such networks. In addition, as part of any federal infrastructure program, governmental subsidies or funding of additional Internet broadband networks may be encouraged. We cannot predict how successful those efforts will be and how they might affect our business.

### **Voice Services**

We provide voice services using VoIP technology. The FCC has adopted a number of regulations for providers of nontraditional voice services such as ours, including regulations relating to privacy of customer proprietary network information, local number portability duties and benefits, disability access, E911, law enforcement assistance, outage reporting, Universal Service Fund contribution obligations and certain regulatory filing requirements. The FCC has not yet ruled on whether VoIP services such as ours should be classified as an "information service" or a "telecommunications service" under the Communications Act. The classification determination is important because telecommunications services are regulated more extensively than information services. State regulatory commissions and legislatures may continue to investigate imposing regulatory requirements on our voice services, and the FCC's open Internet regulations reclassifying Internet access as a telecommunications service may further encourage state-level regulatory actions.

### **Voice Interconnection**

Because the FCC has not determined the appropriate classification of our voice services, providers of VoIP services typically either secure CLEC authorization or obtain interconnection to traditional wireline phone company networks by contracting with an existing CLEC, which has the right, as a telecommunications carrier, to request and obtain interconnection with the traditional wireline phone companies. We have arranged for such interconnection rights through affiliated CLECs. If a regulatory or judicial authority were to deny our ability to interconnect through one of our affiliated CLECs, our ability to provide voice services and compete in the area in question would be negatively impacted. The FCC regulates the arrangements by which telecommunications carriers compensate one another for exchanged traffic and has affirmed the right of CLECs to collect intercarrier compensation when providing interconnection for VoIP providers.

## Table of Contents

### Universal Service

The federal Universal Service program generally requires us and other phone service providers to pay a fee based on revenue from their services into a fund used to subsidize the provision of telecommunications services in high-cost areas and to low-income consumers and the provision of Internet and telecommunications services to schools, libraries and certain health care providers. Some states also have analogous programs that support service in high-cost areas or to low-income consumers. The FCC has long considered implementing changes to the Universal Service program, such as changing the fee calculation from a revenue-based formula to a per-user fee or per-connection fee, adopting a fee based on bandwidth, and expanding the services subject to the fee to include broadband Internet access services. We are unable to predict if or how the FCC may change the Universal Service program, or the effects any such changes would have on our businesses.

The FCC recently has shifted its focus away from supporting traditional telephone service, and toward subsidizing broadband deployment. This shift could assist some of our competitors. For example, in 2014, the FCC substantially revised the program that provides Universal Service support for services to schools and libraries to shift support from voice services to broadband services and the deployment of Wi-Fi networks. Similarly, the FCC has expanded its Lifeline subsidy program for low-income consumers to include broadband services in addition to voice services. The FCC under the new Administration or Congress may revisit these subsidy programs and how they are funded. We cannot predict whether or how these programs will be changed.

### NBCUniversal Segments

---

#### Cable Networks

##### Program Access

The Communications Act and FCC regulations (the "program access rules") generally prevent cable networks affiliated with cable operators from favoring cable operators over competing multichannel video programming distributors ("MVPDs").

The FCC and Congress have considered proposals that would require companies that own multiple cable networks to make each of their networks available individually when negotiating distribution agreements with MVPDs and potentially with online video distributors ("OVDs"). We currently offer our cable networks both on a bundled basis and, when requested, individually.

Under the terms of the NBCUniversal Order, MVPDs in certain circumstances can invoke commercial arbitration for access to our cable networks and broadcast television networks, including our regional sports networks. In addition, under the NBCUniversal Order and NBCUniversal Consent Decree, we are required to make certain of our cable network, broadcast television and filmed entertainment programming available to bona fide OVDs in certain circumstances. For further discussion of these conditions, see "Broadcast Television" below and refer to the "Must-Carry/Retransmission Consent" and "Internet Distribution" discussions within that section.

##### Children's Programming

Under federal regulations, the amount of commercial content that may be shown on cable networks, broadcast networks and broadcast television stations during programming originally produced and broadcast primarily for an audience of children under 13 years of age is limited, and certain television station programming must serve the educational and informational needs of children under 17 years of age. In addition, the NBCUniversal Order includes certain commitments and conditions related to children's television and advertising directed at children.

## Table of Contents

### **Broadcast Television**

#### **Licensing**

Local broadcast television stations may be operated only in accordance with a license issued by the FCC upon a finding that the grant of the license will serve the public interest, convenience and necessity. The FCC grants broadcast television station licenses for specific periods of time, which may be renewed with or without conditions. Substantially all of our broadcast television station licenses have pending applications for renewal, although our stations' authority to operate is automatically extended while a renewal application is under review. Several of these applications have been opposed by third parties. Although our licenses have been renewed in the past, there can be no assurance that we will always obtain renewal grants.

#### **Ownership Limits**

FCC regulations limit the ability of individuals and entities to have "attributable interests" above specific ownership levels in local television stations and place limitations on ownership of other specified mass media entities, such as limits on the cross-ownership of broadcast television stations and newspapers in the same market. The FCC is in the process of reviewing these ownership regulations.

#### *Local Television Ownership*

Under FCC regulations, a licensee generally may own up to two broadcast television stations in the same DMA, as long as at least one of the stations is not among the top four-ranked stations in the market based on audience share and there are at least eight independently owned and operating full-power broadcast television stations in the market. Without regard to the number of remaining independently owned television stations, ownership of more than one television station within the same DMA is permitted so long as certain signal contours of the stations involved do not overlap.

#### *National Television Ownership*

The Communications Act and FCC regulations limit the number of broadcast television stations one entity may own or control nationally. No entity may have an attributable interest in broadcast television stations that reach, in the aggregate, more than 39% of all U.S. television households. The FCC also has adopted a rule that eliminates a 50% discount formerly afforded to UHF stations (channels 14 and above) in calculating the extent of an individual station owner's holdings under the national cap. Our owned broadcast television station reach does not exceed this limit, but the elimination of this discount places us closer to the national cap and limits our flexibility to acquire stations in the future.

#### *Foreign Ownership*

The Communications Act generally limits foreign ownership in a broadcast television station to 20% direct ownership and 25% indirect ownership, although the limit on indirect ownership can be waived if the FCC finds it to be in the public interest.

#### *Dual Network Rule*

Each of the four major broadcast television networks — ABC, CBS, Fox and NBC — is prohibited from being under common ownership or control with another of the four.

#### **Must-Carry/Retransmission Consent**

Every three years, each commercial television station must elect for each cable system in its DMA either must-carry or retransmission consent. A similar regulatory scheme applies to satellite providers. For the current period, which ends on December 31, 2017, all of our owned NBC broadcast television stations and our owned Telemundo broadcast television stations elected retransmission consent.

In enacting the STELA Reauthorization Act of 2014, Congress modified certain aspects of the compulsory copyright licenses under which satellite providers and cable operators retransmit broadcast television sta-

## **Table of Contents**

tions. Congress also is considering legislation that would modify the must-carry and retransmission consent regime. Under conditions imposed in the NBCUniversal Order, MVPDs may invoke commercial arbitration to resolve disputes regarding carriage of our owned local broadcast television stations.

### **Internet Distribution**

The NBCUniversal Order and NBCUniversal Consent Decree establish certain obligations and restraints concerning distribution of our content online. We must make available certain of our cable network, broadcast television and filmed entertainment programming to bona fide OVDs in certain circumstances, and they may invoke commercial arbitration to resolve disputes over access to such programming. We also must distribute programming via nbc.com that is generally equivalent to the programming that we distributed via nbc.com as of January 1, 2011, on generally equivalent prices, terms and conditions, so long as at least one of the other major broadcast networks continues to distribute its programming in a similar fashion. We are one of three broadcast network owners of Hulu, but we have no voting rights or board representation. We have entered into renewal license agreements with Hulu on substantially the same terms as its other broadcast network owners.

### **Indecency**

A federal statute and FCC regulations prohibit the broadcast of obscene material on television stations at any time and indecent or profane material between the hours of 6 a.m. and 10 p.m. From time to time, we have received and may receive in the future letters of inquiry from the FCC prompted by complaints alleging that certain programming on our owned local broadcast television stations included indecent or profane material.

### **Filmed Entertainment**

Our filmed entertainment business is subject to "trade practice laws" in effect in 25 states and Puerto Rico relating to theatrical distribution of motion pictures. In countries outside the United States, a variety of existing or contemplated laws and regulations may affect our ability to distribute and license motion picture and television products, as well as consumer merchandise products. The ability of countries to deny market access or refuse national treatment to products originating outside their territories is regulated under various international agreements.

### **Theme Parks**

Our theme parks are subject to various regulations, including laws and regulations regarding environmental protection, privacy and data protection, consumer product safety and theme park operations, such as health, sanitation, safety and fire standards, as well as liquor licenses.

## **Other Areas of Regulation**

---

### **Intellectual Property**

Copyright, trademark, unfair competition, patent, trade secret and other proprietary-rights laws of the United States and other countries help protect our intellectual property rights. In particular, piracy of programming and films through unauthorized distribution of counterfeit DVDs, peer-to-peer file sharing and other platforms presents challenges for our cable networks, broadcast television and filmed entertainment businesses. The unauthorized reproduction, distribution or display of copyrighted material over the Internet or through other methods of distribution, such as through devices, software or websites that allow the reproduction, viewing, sharing and/or downloading of content by either ignoring or interfering with the content's security features and copyrighted status, interferes with the market for copyrighted works and disrupts our ability to exploit our content. The extent of copyright protection and the use of technological protections, such as encryption, are controversial. Modifications to existing laws that weaken these protections could have an adverse effect on our ability to license and sell our programming.

## **Table of Contents**

While many legal protections exist to combat piracy, laws in the United States and internationally continue to evolve, as do technologies used to evade these laws. We have actively engaged in the enforcement of our intellectual property rights and likely will continue to expend substantial resources to protect our content. The repeal of laws intended to combat piracy and protect intellectual property or weakening of such laws or enforcement in the United States or internationally, or a failure of existing laws to adapt to new technologies, could make it more difficult for us to adequately protect our intellectual property rights, which could negatively affect their value and further increase the costs of enforcing our rights.

Copyright laws also require that we contribute a percentage of revenue to a federal copyright royalty pool in exchange for retransmitting copyrighted material in broadcast signals under a compulsory license and that we pay standard industry licensing fees for the public performance of music in the programs we distribute, such as local advertising and local origination programming on our cable systems, as well as in the content we create. The fees we pay to music performance rights organizations are typically renegotiated when we renew licenses with those organizations, while the royalties we contribute to the copyright royalty pool for broadcast signals can be challenged by copyright owners in annual audits, and we cannot predict what those fees will be in the future or if disputes will arise over them. In addition, in response to a 2014 FCC decision eliminating the FCC's "sports blackout" rule, which previously enabled sports teams to insist that cable operators black out sports events not available on local broadcast signals, the leading sports leagues petitioned the Copyright Royalty Board to impose a copyright surcharge on cable operators to compensate sports teams for the loss of programming exclusivity, and that proceeding is now pending.

There has been litigation related to a number of online entities that stream our broadcast television content online without the consent of, or compensation to, NBC or its affiliates. In 2014, the U.S. Supreme Court ruled that one such entity, Aereo, violated the broadcasters' exclusive right to perform their copyrighted works publicly. Subsequently, Aereo sought to operate as a cable system under the Copyright Act. Although the U.S. Copyright Office rejected its application for a compulsory copyright license, other companies continue to seek legislation or court rulings to obtain a compulsory license to stream broadcast programming online.

### **Privacy and Data Security Regulation**

The Communications Act generally restricts the nonconsensual collection and disclosure to third parties of cable customers' personally identifiable information by cable operators, except for rendering service, conducting legitimate business activities related to the service, and responding to legal requests. We are also subject to various state and federal regulations that provide privacy protections for customer proprietary network information related to our voice services.

As a result of the FCC's 2015 decision to reclassify broadband Internet access service as a "telecommunications service" subject to Title II of the Communications Act, the FCC has concluded that ISPs are subject to FCC regulations regarding the use and disclosure of certain customer information. Specifically, in October 2016, the FCC adopted new privacy and data security regulations governing the use of certain customer information by telecommunications carriers, including ISPs and providers of VoIP services such as ours. Under these new regulations, we may use, disclose or permit access to any customer non-sensitive proprietary information subject to the customer's ability to opt out, but must obtain opt-in approval from the customer to use, disclose or permit access to customer sensitive proprietary information, with certain exceptions. The new regulations also impose breach notification obligations and data security requirements. These new rules are more stringent than the FTC's privacy rules that previously applied to ISPs and could have adverse effects on our ability to compete in the highly concentrated online advertising market. The FCC under the new Administration or Congress may revisit and revise these new rules, although we cannot predict whether or how the rules might be changed.

## Table of Contents

In addition to FCC privacy regulations governing ISPs, the FTC generally exercises authority over privacy protections applicable to some of our other businesses by using its existing authority over unfair and deceptive acts or practices to apply greater restrictions on the collection and use of personally identifiable and other information relating to consumers. It also has undertaken numerous enforcement actions against parties that do not provide sufficient security protections against the loss or unauthorized disclosure of this type of information. However, a recent court decision has raised questions regarding the extent of FTC jurisdiction over companies like us, whose service offerings include some common carrier services. The FTC has appealed this decision. We cannot predict the outcome of the litigation or the impact of the decision on our business. We also are subject to stringent data security and data retention requirements that apply to website operators and online services directed to children under 13 years of age, or that knowingly collect or post personal information from children under 13 years of age. Other privacy-oriented laws have been extended by courts to online video providers and are increasingly being used in privacy lawsuits, including class actions, against providers of video materials online.

We are also subject to state and federal "do not call" laws regarding telemarketing and state and federal laws regarding unsolicited commercial emails, as well as FCC regulations relating to automated telemarketing calls, texts and SMS messages. The FTC and state attorneys general also have initiated efforts to increase and enforce transparency requirements about the collection and use of consumer information, even in an aggregated, non-customer-identifiable form, which may require ongoing review of new and rapidly evolving technologies and methods for delivering content and advertising to ensure that appropriate notice is given to consumers and consent is obtained where required.

We are also subject to state and federal laws and regulations regarding data security that primarily apply to sensitive personal information that could be used to commit identity theft. Most states have security breach notification laws that generally require a business to give notice to consumers and government agencies when certain information has been disclosed due to a security breach, and the FCC has adopted security breach rules for voice services and broadband Internet access services. Several states have also enacted general data security requirements to safeguard consumer information, including the proper disposal of consumer information.

The National Institute of Standards and Technology ("NIST"), in cooperation with other federal agencies and owners and operators of U.S. critical infrastructure, including us, have developed a voluntary framework that provides a prioritized, flexible, repeatable, performance-based and cost-effective approach to cybersecurity risk. It is a compendium of existing cross-sector cyber-defense processes, practices and protocols that can help companies identify, assess and manage their cyber risks and vulnerabilities, and several government agencies have encouraged compliance with this framework. NIST recently proposed draft updates to this voluntary framework and is collecting feedback on the draft. In June 2016, the Department of Homeland Security and the Department of Justice, in collaboration with other federal agencies, released final guidance regarding the sharing of cyber threat indicators and defensive measures between and among Federal and Non-Federal entities under the Cybersecurity Act of 2015. Finally, there are pending legislative proposals that could impose new requirements on owners and operators of critical infrastructure, including us, and the FCC is considering expanding its cybersecurity guidelines or adopting new cybersecurity requirements.

### **FCC Spectrum Auction**

Congress has authorized the FCC to conduct an auction to repurpose some broadcast spectrum to mobile broadband use. In this auction, licensees of full-power and Class A television stations have the opportunity to sell some or all of their spectrum rights in exchange for cash. TV stations that do not voluntarily sell their spectrum rights may be assigned new channels on which to operate, but the FCC must make "all reasonable efforts" to preserve those stations' over-the-air coverage areas and populations served, and to reimburse them for reasonable relocation costs (subject to an aggregate limit of \$1.75 billion).

## Table of Contents

NBCUniversal has submitted applications with the FCC indicating its potential interest in selling broadcast spectrum rights, and we have filed an application to bid on new mobile broadband licenses. Filing an application in the auction does not create any obligation to sell, bid on or buy spectrum.

Bidding in the auction began in May 2016 and is still ongoing. We cannot predict the outcome of the auction or the impact the outcome may have on our business.

### **State and Local Taxes**

Some states and localities have imposed or are considering imposing, through both legislative and administrative channels, new or additional taxes or fees on, or limiting or eliminating incentives or credits earned or monetized by, the businesses operated by our Cable Communications and NBCUniversal segments, or imposing adverse methodologies by which taxes, fees, incentives or credits are computed, earned or monetized. These include combined reporting or other changes to general business taxes, central assessments for property tax, and taxes and fees on the businesses operated or services provided by our Cable Communications and NBCUniversal segments. In some situations, DBS providers and other competitors that deliver their services over a high-speed Internet connection do not face the same state tax and fee burdens. Congress has also considered, and may consider again, proposals to bar or limit states from imposing taxes on these DBS providers or other competitors that are equivalent to the taxes or fees that we pay. The Internet Tax Freedom Act, which prohibits most states and localities from imposing sales and other taxes on our Internet access charges, has now been made permanent by 2016 legislation; however, some jurisdictions have or may assert that certain taxes akin to right-of-way fees are not preempted by Internet Tax Freedom Act. The FCC's reclassification of broadband Internet access services as Title II telecommunications services may cause or allow, directly or indirectly, some states and localities to impose various other taxes and fees on our high-speed Internet business.

### **Environmental Matters**

Certain of our business operations are subject to environmental laws and regulations since they involve air emissions, wastewater discharges, and the use, disposal and cleanup of toxic and hazardous substances. Any failure to comply with environmental requirements could result in monetary fines, civil or criminal sanctions, third-party claims, or other costs or liabilities.

Environmental requirements have become more stringent over time, and pending or proposed new regulations could impact our operations or costs. For example, climate change regulation, such as proposed greenhouse gas emissions limits or cap and trade programs, could result in an increase in the cost of electricity, which is a significant component of our operational costs for some aspects of our businesses.

### **Other Regulations**

Federal regulators actively regulate other aspects of our businesses, including accessibility to our video and voice services and broadcast television programming for people with disabilities, customer service standards, inside wiring, leased access, loudness of commercial advertisements, advertising, Emergency Alert System, equal employment opportunity, lottery programming, recordkeeping and public file access requirements, regulatory fees and technical standards relating to the operation of cable systems and television stations. We are occasionally subject to enforcement actions at the FCC, which can result in us having to pay fines to the agency or being subject to other sanctions. We also are subject to various international regulations, including those that cover television broadcasting, programming and advertising.

## Table of Contents

### Employees

As of December 31, 2016, we had approximately 159,000 full-time and part-time employees calculated on a full-time equivalent basis. Of these employees, approximately 91,000 and 58,000 were associated with our cable communications business and our NBCUniversal businesses, respectively. We also use freelance and temporary employees in the normal course of our business.

### Caution Concerning Forward-Looking Statements

The SEC encourages companies to disclose forward-looking information so that investors can better understand a company's future prospects and make informed investment decisions. In this Annual Report on Form 10-K, we state our beliefs of future events and of our future financial performance. In some cases, you can identify these so-called "forward-looking statements" by words such as "may," "will," "should," "expects," "believes," "estimates," "potential," or "continue," or the negative of these words, and other comparable words. You should be aware that these statements are only our predictions. In evaluating these statements, you should consider various factors, including the risks and uncertainties listed in "Risk Factors" and in other reports we file with the SEC.

Additionally, we operate in a highly competitive, consumer-driven and rapidly changing environment. This environment is affected by government regulation; economic, strategic, political and social conditions; consumer response to new and existing products and services; technological developments; and, particularly in view of new technologies, the ability to develop and protect intellectual property rights. Our actual results could differ materially from our forward-looking statements as a result of any of such factors, which could adversely affect our businesses, results of operations or financial condition. We undertake no obligation to update any forward-looking statements.

### Item 1A: Risk Factors

**Our businesses currently face a wide range of competition, and our businesses and results of operations could be adversely affected if we do not compete effectively.**

All of our businesses operate in intensely competitive, consumer-driven and rapidly changing environments and compete with a growing number of companies that provide a broad range of communications products and services and entertainment, news and information content to consumers. Technological changes are further intensifying and complicating the competitive landscape and influencing consumer behavior, which is discussed in the risk factor immediately below under the heading "Changes in consumer behavior driven by new technologies and distribution platforms for viewing content may adversely affect our businesses and challenge existing business models."

Competition for our cable services consists primarily of DBS providers and phone companies with fiber-based networks that typically offer features, pricing and packaging for services comparable to ours. In 2015, AT&T, our largest phone company competitor, acquired DirecTV, the nation's largest DBS provider to create an even larger competitor that also has its own wireless phone facilities, which we do not, and in 2016, announced a proposed merger with Time Warner, a media and entertainment company. Some of these competitors have begun offering smaller packages of channels at price points lower than our standard packages, both through traditional and online distribution platforms, which could cause us to offer more customized programming packages that may be less profitable. In addition, if consolidation between wireless distributors and content providers occurs, some of our competitors may offer free or lower cost streaming services for viewing their content through unlimited data-usage plans for their Internet or wireless phone serv-

## Table of Contents

ices. Additional companies, some with significant financial resources, continue to enter or are seeking to enter the video distribution market, primarily by offering online video programming services that can be viewed live, through streaming services or by downloading.

Current and future wireless Internet services, such as 3G, 4G and 5G wireless broadband services and Wi-Fi networks, and devices such as wireless data cards, tablets and smartphones, and mobile wireless routers that connect to such devices, may compete with our high-speed Internet services. Our voice services are facing increased competition as customers replace wireline phones with wireless and Internet-based phone services.

Our cable communications business continues to seek ways to enhance the value of our cable services network, such as by growing our high-speed Internet and business services businesses and by launching additional services, such as our home security and automation services. There can be no assurance that we can execute on these and other initiatives in a manner sufficient to grow or maintain our Cable Communications segment revenue, maintain our Cable Communications segment operating margin, or to compete successfully in the future.

Each of NBCUniversal's businesses also faces substantial and increasing competition from providers of similar types of content, as well as from other forms of entertainment and recreational activities. NBCUniversal must compete to obtain talent, programming and other resources required in operating these businesses.

The ability of all of our businesses to compete effectively depends on our perceived image and reputation among our various constituencies, including our customers, consumers, advertisers, investors and government authorities. Our ability to compete may be negatively affected if we do not provide our customers with a satisfactory customer experience.

There can be no assurance that we will be able to compete effectively against existing or new competitors or that competition will not have an adverse effect on our businesses. For a more detailed description of the competition facing our businesses, see Item 1: Business and refer to the "Competition" discussion within that section.

### **Changes in consumer behavior driven by new technologies and distribution platforms for viewing content may adversely affect our businesses and challenge existing business models.**

New technologies and platforms for the distribution, sale and viewing of content have been, and will likely continue to be, developed that further increase the number of competitors that all our businesses face and challenge existing business models. These technologies and distribution platforms are driving changes in consumer behavior as consumers seek more control over when, where and how they consume content and access communications services.

While our cable communications business is attempting to adapt to changing consumer behaviors, for example, by deploying our X1 platform, cloud DVR technology and apps such as Netflix on our X1 set top boxes, new and traditional competitors, as well as some programming networks, continue to launch subscription video on demand services, live online broadcast and cable television streaming services and downloading services that can be viewed on television sets, computers, smartphones and tablets. Many of these service offerings charge no fee or a lower fee than our traditional video packages for access to their content, which could have an adverse effect on demand for our video services, including for expanded digital video packages, premium networks, and our DVR and On Demand services.

New technologies and distribution platforms, together with an increasing number of companies offering their content directly to consumers over the Internet, including some that also offer exclusive high-quality original

## Table of Contents

video programming, have increased the number of entertainment choices available to consumers, which has intensified audience fragmentation. The increase in entertainment choices has and may continue to reduce the number of subscribers to our cable networks. Time-shifting technologies, such as DVRs and cloud-based recording services and video on demand services, reduce the viewing of content through traditional linear television distribution outlets. Reduced viewing of our content through traditional linear television distribution outlets has caused and will likely continue to cause audience ratings declines for NBCUniversal's linear television content and may adversely affect the price and amount of advertising that advertisers are willing to purchase from us and the amount NBCUniversal receives for distribution of its content.

The success of any of these ongoing or future developments or our failure to effectively anticipate or adapt to emerging competitors or changes in consumer behavior, including among younger consumers, could have an adverse effect on our competitive position, businesses and results of operations.

### **A decline in advertisers' expenditures or changes in advertising markets could negatively impact our businesses.**

Our cable communications, cable networks and broadcast television businesses compete for the sale of advertising time with other television networks and stations, as well as with all other advertising platforms, such as digital media, as well as radio and print. We derive substantial revenue from the sale of advertising, and a decline in expenditures by advertisers, including through traditional linear television distribution models, could negatively impact our results of operations. Declines can be caused by the economic prospects of specific advertisers or industries, increased competition for the leisure time of viewers and audience fragmentation, the growing use of new technologies, or the economy in general. In addition, advertisers' willingness to purchase advertising from us may be adversely affected by lower audience ratings, which many of our networks have experienced and likely will continue to experience. Advertising sales and rates also are dependent on the methodology used for audience measurement and could be negatively affected if methodologies do not accurately reflect actual viewership levels. For example, certain methods of viewing content, such as delayed viewing on DVRs or viewing content online, might not be counted in audience measurements or may generate less, if any, revenue than traditional distribution methods, which could have an adverse effect on our advertising revenue. Reductions in advertisers' expenditures could adversely affect our revenue and businesses.

### **Our businesses depend on keeping pace with technological developments.**

Our success is, to a large extent, dependent on our ability to acquire, develop, adopt and leverage new and existing technologies, and our competitors' use of certain types of technology and equipment may provide them with a competitive advantage. For example, current and new wireless Internet technologies such as 4G and 5G wireless broadband services continue to evolve rapidly to allow for greater speed and reliability, and some companies and municipalities are building advanced fiber-based networks that provide very fast Internet access speeds. We expect other advances in communications technology to occur in the future. If we choose technology or equipment that is not as effective or attractive to consumers as that employed by our competitors, if we fail to employ technologies desired by consumers before our competitors do so, or if we fail to execute effectively on our technology initiatives, our businesses and results of operations could be adversely affected. We also will continue to incur additional costs as we execute our technology initiatives, such as the deployment of DOCSIS 3.1, X1 set-top boxes, wireless gateways and cloud DVR technology, and there can be no assurance that we can execute on these and other initiatives in a manner sufficient to grow or maintain our revenue or to compete successfully in the future. We also may incur increased costs if changes in our competitors' product offerings require that we offer certain of our existing services or enhancements at a lower or no cost to our customers or that we make additional research and development expenditures.

## Table of Contents

### **We are subject to regulation by federal, state, local and foreign authorities, which may impose additional costs and restrictions on our businesses.**

Federal, state and local governments extensively regulate the video, high-speed Internet and voice services industries. Our broadcast television business is also highly regulated by federal laws and regulations. Our cable networks, filmed entertainment and theme parks businesses are also subject to various other laws and regulations at the international, federal, state and local levels, including laws and regulations relating to environmental protection, which have become more stringent over time, and the safety of consumer products and theme park operations. In addition, we are subject to the NBCUniversal Order and the NBCUniversal Consent Decree, which have imposed numerous conditions on our businesses relating to the treatment of competitors and other matters. In recent years, the FCC and certain states also have been more active in conducting inquiries and reviews regarding our services, and this trend may continue. Failure to comply with the laws and regulations applicable to our businesses could result in administrative enforcement actions, fines, and civil and criminal liability. For a more extensive discussion of the significant risks associated with the regulation of our businesses, see Item 1: Business and refer to the "Legislation and Regulation" discussion within that section.

### **Changes to existing statutes, rules, regulations, or interpretations thereof, or adoption of new ones, could have an adverse effect on our businesses.**

Legislators and regulators at all levels of government frequently consider changing, and sometimes do change, existing statutes, rules, regulations, or interpretations thereof, or prescribe new ones, which may significantly affect our businesses. In addition, in recent years, the FCC and certain states have been more active in considering rulemakings and legislation regarding our services. Any future legislative, judicial, regulatory or administrative actions may increase our costs or impose additional restrictions on our businesses, some of which may be significant. In addition, Congress is expected to consider proposals to address communications issues, including whether it should rewrite the entire Communications Act to account for changes in the communications marketplace, whether it should address the FCC's authority to implement or enforce open Internet regulations, and whether it should fund new broadband infrastructure. We are unable to predict the effects of any of these or any other further legislative requirements on our businesses, nor can we predict how the FCC or other agencies under the new Administration will address regulatory matters affecting our businesses. Any changes to the legal and regulatory framework applicable to any of our services or businesses could have a negative impact on our businesses and results of operations.

### **Programming expenses for our video services are increasing, which could adversely affect our Cable Communications segment's video business.**

We expect programming expenses for our video services to continue to be our Cable Communications segment's largest single expense item and to increase in the foreseeable future. The multichannel video provider industry has experienced continued increases in the cost of programming, especially sports programming, which we expect will continue for the foreseeable future. Our programming expenses may also increase as we add programming to our video services or distribute existing programming to more of our customers or through additional delivery platforms, such as On Demand or streaming services. Additionally, in the past few years, we have begun paying certain local broadcast television stations in exchange for their required consent for the retransmission of broadcast network programming to our video services customers; we expect to continue to be subject to increasing demands for payment and other concessions from local broadcast television stations. These market factors may be exacerbated by increased consolidation in the media industry, which may further increase our programming expenses. If we are unable to raise our customers' rates or offset programming cost increases through the sale of additional services, the increasing cost of programming could have an adverse effect on our Cable Communications segment's results of operations. Moreover, as our contracts with content providers expire, there can be no assurance that they will be renewed on acceptable terms or that they will be renewed at all, in which case we may be unable to provide such content as part of our video services, and our businesses and results of operations could be adversely affected.

## Table of Contents

**NBCUniversal's success depends on consumer acceptance of its content, and its businesses may be adversely affected if its content fails to achieve sufficient consumer acceptance or the costs to create or acquire content increase.**

Most of NBCUniversal's businesses create and acquire media and entertainment content, the success of which depends substantially on consumer tastes and preferences that change in often unpredictable ways. The success of these businesses depends on our ability to consistently create, acquire, market and distribute cable network and broadcast television programming, filmed entertainment, theme park attractions and other content that meet the changing preferences of the broad domestic and international consumer markets. We have invested, and will continue to invest, substantial funds in our content, including in the production of original content on our cable networks and broadcast television networks, in our films and for theme park attractions, before learning the extent to which it would earn consumer acceptance.

We also obtain a significant portion of our content from third parties, such as movie studios, television production companies, sports organizations and other suppliers. Competition for popular content, particularly for sports programming, is intense, and we may have to increase the price we are willing to pay or be outbid by our competitors for popular content. Entering into or renewing contracts for such programming rights or acquiring additional rights may result in significantly increased costs. Particularly with respect to long-term contracts for sports programming rights, our results of operations and cash flows over the term of a contract depend on a number of factors, including the strength of the advertising market, our audience size, the ability to secure distribution from and impose surcharges or obtain carriage on multichannel video providers for the content, and the timing and amount of our rights payments. There can be no assurance that revenue from these contracts will exceed our costs for the rights, as well as the other costs of producing and distributing the programming. If our content does not achieve sufficient consumer acceptance, or if we cannot obtain or retain rights to popular content on acceptable terms, or at all, our businesses may be adversely affected.

**The loss of NBCUniversal's programming distribution agreements, or the renewal of these agreements on less favorable terms, could adversely affect its businesses.**

Our cable networks depend on their ability to secure and maintain distribution agreements with multichannel video providers, and if a network does not attract sufficient viewers, multichannel video providers may decide not to distribute the network. Our broadcast television networks depend on their ability to secure and maintain network affiliation agreements with third-party local broadcast television stations in the markets where we do not own the affiliated local broadcast television station. In addition, every three years, each of our owned local broadcast television stations must elect, with respect to its retransmission by multichannel video providers within its DMA, either "must-carry" status, in which the distributor's carriage of the station is mandatory and does not generate any compensation for the local station, or "retransmission consent," in which the station gives up its right to mandatory carriage and instead seeks to negotiate the terms and conditions of carriage with the distributor, including the amount of compensation, if any, paid to the station by such distributor. All of our NBC and Telemundo owned local broadcast television stations have elected retransmission consent through December 31, 2017. Increasingly, our cable networks, broadcast television and filmed entertainment businesses have entered into agreements to license their prior season and library content on other distribution platforms, including subscription video on demand services, and some multichannel video providers are offering smaller packages of channels as part of their streaming and linear television programming packages. In addition, certain online entities may stream our broadcast television content online without our consent and without paying any compensation to us. As a result, there can be no assurance that any of our distribution agreements will be renewed in the future on acceptable terms, or at all. The loss of any of these agreements, or the renewal of these agreements on less favorable terms, could reduce our distribution revenue and the reach of our television programming and its attractiveness to advertisers, which in turn could adversely affect our cable networks, broadcast television and filmed entertainment businesses.

## Table of Contents

### **We rely on network and information systems and other technologies, as well as key properties, and a disruption, cyber attack, failure or destruction of such networks, systems, technologies or properties may disrupt our businesses.**

Network and information systems and other technologies, including those related to our network management, customer service operations and programming delivery, are critical to our business activities. Network and information systems-related events, including those caused by us or by third parties, such as computer hackings, cyber attacks, computer viruses, worms or other destructive or disruptive software, process breakdowns, denial of service attacks, malicious social engineering or other malicious activities, or any combination of the foregoing, or power outages, natural disasters, infectious disease outbreaks, terrorist attacks or other similar events, could result in a degradation or disruption of our services, excessive call volume to call centers, a reduction in demand for our theme parks or damage to our equipment, data, properties and reputation. These events also could result in large expenditures to repair or replace the damaged properties, networks or information systems or to protect them from similar events in the future, and any such events could have an adverse effect on our results of operations.

In addition, we may obtain certain confidential, proprietary and personal information about our customers, personnel and vendors, and may provide this information to third parties, in connection with our business. While we obtain assurances that these third parties will protect this information, there is a risk that this information may be compromised. Any security breaches, such as misappropriation, misuse, leakage, falsification or accidental release or loss of information maintained in our information technology systems, including customer, personnel and vendor data, could damage our reputation and require us to expend significant capital and other resources to remedy any such security breach, and could cause regulators to impose fines or other remedies for failure to comply with relevant customer privacy rules.

The risk of these systems-related events and security breaches occurring continues to intensify in many lines of business, and our lines of business may be at a disproportionately heightened risk of these events occurring, due to the nature of our businesses and the fact that we maintain certain information necessary to conduct our business in digital form stored on cloud servers. In the ordinary course of our business, there are frequent attempts to cause such systems-related events and security breaches, and we have experienced minor systems-related events that, to date, have not resulted in any significant degradation or disruption to our network or information systems or our services or operations. While we develop and maintain systems, and operate a comprehensive security program, seeking to prevent systems-related events and security breaches from occurring, the development, maintenance and operation of these systems and programs is costly and requires ongoing monitoring and updating as technologies change and efforts to overcome security measures become more sophisticated. Despite any efforts to prevent these events and security breaches, there can be no assurance that they will not occur in the future or will not have an adverse effect on our businesses. Moreover, the amount and scope of insurance we maintain against losses resulting from any such events or security breaches likely would not be sufficient to cover our losses or otherwise adequately compensate us for any disruptions to our business that may result, and the occurrence of any such events or security breaches could have an adverse effect on our business.

### **We may be unable to obtain necessary hardware, software and operational support.**

We depend on third-party vendors to supply us with a significant amount of the hardware, software and operational support necessary to provide certain of our services. Some of these vendors represent our primary source of supply or grant us the right to incorporate their intellectual property into some of our hardware and software products. While we actively monitor the operations and financial condition of key vendors in an attempt to detect any potential difficulties, there can be no assurance that we would timely identify any operating or financial difficulties associated with these vendors or that we could effectively mitigate our risks with respect to any such difficulties. If any of these vendors experience operating or financial difficulties, if our demand exceeds their capacity or if they are otherwise unable to meet our specifications or provide the

## Table of Contents

equipment or services we need in a timely manner or at reasonable prices, our ability to provide some services may be adversely affected.

### **Weak economic conditions may have a negative impact on our businesses.**

A substantial portion of our revenue comes from customers whose spending patterns may be affected by prevailing economic conditions. Weak economic conditions could adversely affect demand for any of our products and services and have a negative impact on our results of operations. For example, customers may reduce the level of cable services to which they subscribe, or may discontinue subscribing to one or more of our cable services. This risk may be increased by the expanded availability of free or lower cost competitive services, such as subscription video on demand services, or substitute services for our high-speed Internet and voice services, such as mobile phones, smartphones and Wi-Fi networks. Weak economic conditions also may have a negative impact on our advertising revenue, the performance of our films and home entertainment releases, and attendance and spending in our theme parks. Weak economic conditions and turmoil in the global financial markets may also impair the ability of third parties to satisfy their obligations to us, and any disruption in the global financial markets may affect our ability to obtain financing or refinance any existing debt on acceptable terms.

### **Our businesses depend on using and protecting certain intellectual property rights and on not infringing the intellectual property rights of others.**

We rely on our intellectual property, such as patents, copyrights, trademarks and trade secrets, as well as licenses and other agreements with our vendors and other third parties, to use various technologies, conduct our operations and sell our products and services. Legal challenges to our intellectual property rights and claims of intellectual property infringement by third parties could require that we enter into royalty or licensing agreements on unfavorable terms, incur substantial monetary liability, or be enjoined preliminarily or permanently from further use of the intellectual property in question or from the continuation of our businesses as currently conducted. We may need to change our business practices if any of these events occur, which may limit our ability to compete effectively and could have an adverse effect on our results of operations. Even if we believe any such challenges or claims are without merit, they can be time-consuming and costly to defend and divert management's attention and resources away from our businesses. Moreover, if we are unable to obtain or continue to obtain licenses from our vendors and other third parties on reasonable terms, our businesses could be adversely affected.

In addition, intellectual property constitutes a significant part of the value of NBCUniversal's businesses, and its success is highly dependent on protecting the intellectual property rights of the content it creates or acquires against third-party misappropriation, reproduction or infringement. The unauthorized reproduction, distribution or display of copyrighted material negatively affects our ability to generate revenue from the legitimate sale of our content, as well as from the sale of advertising in connection with our content, and increases our costs due to our active enforcement of our intellectual property rights.

Piracy and other unauthorized uses of content are made easier, and the enforcement of intellectual property rights more challenging, by technological advances that allow the conversion of programming, films and other content into digital formats, which facilitates the creation, transmission and sharing of high-quality unauthorized copies. In particular, piracy of programming and films through unauthorized distribution on DVDs, peer-to-peer computer networks and other platforms continues to present challenges for our cable networks, broadcast television and filmed entertainment businesses. While piracy is a challenge in the United States, it is particularly prevalent in many parts of the world that lack developed copyright laws, effective enforcement of copyright laws and technical protective measures like those in effect in the United States. If any U.S. or international laws intended to combat piracy and protect intellectual property rights are repealed or weakened or are not adequately enforced, or if the legal system fails to adapt to new technologies that facilitate piracy, we may be unable to effectively protect our rights, the value of our intellectual property may

## **Table of Contents**

be negatively impacted and our costs of enforcing our rights may increase. See Item 1: Business and refer to the "Legislation and Regulation — Other Areas of Regulation — Intellectual Property" discussion for additional information.

### **Acquisitions and other strategic initiatives present many risks, and we may not realize the financial and strategic goals that we had contemplated.**

From time to time, we make acquisitions and investments and may pursue other strategic initiatives, including, for example, with respect to our wireless strategy. In connection with such acquisitions and strategic initiatives, we may incur unanticipated expenses, fail to realize anticipated benefits, have difficulty incorporating an acquired or new line of business, disrupt relationships with current and new employees, customers and vendors, incur significant debt, or have to delay or not proceed with announced transactions or initiatives. For example, our launch of a wireless phone service in 2017 using virtual network operator rights from a third party will have success-based working capital requirements, primarily associated with the procurement of handsets and other equipment, as we launch the service, which could have negative effects on our cash flows. Additionally, regulatory agencies, such as the FCC or DOJ, may impose restrictions on the operation of our businesses as a result of our seeking regulatory approvals for any significant acquisitions and strategic initiatives, or may dissuade us from pursuing certain transactions. The occurrence of any of these events could have an adverse effect on our businesses.

### **Labor disputes, whether involving employees or sports organizations, may disrupt our operations and adversely affect our businesses.**

Many of NBCUniversal's employees, including writers, directors, actors, technical and production personnel and others, as well as some of our on-air and creative talent employees, are covered by collective bargaining agreements or works councils. Most of NBCUniversal's collective bargaining agreements are industry-wide agreements, and we may lack practical control over the negotiations and terms of the agreements. If we are unable to reach agreement with a labor union before the expiration of a collective bargaining agreement, our employees who were covered by that agreement may have a right to strike or take other actions that could adversely affect us, which could disrupt our operations and reduce our revenue, and the resolution of any disputes may increase our costs. There can be no assurance that we will renew our collective bargaining agreements as they expire or that we can renew them on favorable terms or without any work stoppages.

In addition, our cable networks and broadcast television networks have programming rights agreements of varying scope and duration with various sports organizations to broadcast and produce sporting events, including certain NFL, NHL, NBA and MLB games. Labor disputes in these and other sports organizations could have an adverse effect on our businesses.

### **The loss of key management personnel or popular on-air and creative talent could have an adverse effect on our businesses.**

We rely on certain key management personnel in the operation of our businesses. While we maintain long-term and emergency transition plans for key management personnel and believe we could either identify internal candidates or attract outside candidates to fill any vacancy created by the loss of any key management personnel, the loss of one or more of our key management personnel could have a negative impact on our businesses. In addition, our cable networks, broadcast television and filmed entertainment businesses depend on the abilities and expertise of our on-air and creative talent. If we fail to retain our on-air or creative talent, if the costs to retain such talent increase materially, if we need to make significant termination payments, or if these individuals lose their current appeal, our businesses could be adversely affected.

### **We face risks relating to doing business internationally that could adversely affect our businesses.**

We, primarily through NBCUniversal, operate our businesses worldwide. There are risks inherent in doing business internationally, including global financial market turmoil; economic volatility and the global economic

**Table of Contents**

slowdown; currency exchange rate fluctuations and inflationary pressures; the requirements of local laws and customs relating to the publication and distribution of content and the display and sale of advertising; import or export restrictions and changes in trade regulations; difficulties in developing, staffing and managing foreign operations; issues related to occupational safety and adherence to diverse local labor laws and regulations; and potentially adverse tax developments. In addition, doing business internationally subjects us to risks relating to political or social unrest, corruption and government regulation, including U.S. laws such as the Foreign Corrupt Practices Act, that impose stringent requirements on how we conduct our foreign operations. If any of these events occur, our businesses may be adversely affected.

**Our Class B common stock has substantial voting rights and separate approval rights over several potentially material transactions, and our Chairman and CEO has considerable influence over our company through his beneficial ownership of our Class B common stock.**

Our Class B common stock has a nondilutable 33 1/3% of the combined voting power of our Class A and Class B common stock. This nondilutable voting power is subject to proportional decrease to the extent the number of shares of Class B common stock is reduced below 9,444,375, which was the number of shares of Class B common stock outstanding on the date of our 2002 acquisition of AT&T Corp.'s cable business, subject to adjustment in specified situations. Stock dividends payable on the Class B common stock in the form of Class B or Class A common stock do not decrease the nondilutable voting power of the Class B common stock. The Class B common stock also has separate approval rights over several potentially material transactions, even if they are approved by our Board of Directors or by our other shareholders and even if they might be in the best interests of our other shareholders. These potentially material transactions include mergers or consolidations involving Comcast Corporation, transactions (such as a sale of all or substantially all of our assets) or issuances of securities that require shareholder approval, transactions that result in any person or group owning shares representing more than 10% of the combined voting power of the resulting or surviving corporation, issuances of Class B common stock or securities exercisable or convertible into Class B common stock, and amendments to our articles of incorporation or by-laws that would limit the rights of holders of our Class B common stock. Brian L. Roberts, our chairman and CEO, beneficially owns all of the outstanding shares of our Class B common stock and, accordingly, has considerable influence over our company and the potential ability to transfer effective control by selling the Class B common stock, which could be at a premium.

## Table of Contents

### Item 1B: Unresolved Staff Comments

None.

### Item 2: Properties

We believe that substantially all of our physical assets were in good operating condition as of December 31, 2016. Our corporate headquarters and Cable Communications segment headquarters are located in Philadelphia, Pennsylvania at One Comcast Center. We own an 80% interest in the entity whose primary asset is One Comcast Center. In addition, we own an 80% interest in an entity that is currently constructing the Comcast Technology Center, which is adjacent to One Comcast Center. We also lease locations for numerous business offices, warehouses and properties housing divisional information technology operations throughout the United States.

#### Cable Communications Segment

Our principal physical assets consist of operating plant and equipment, including signal receiving, encoding and decoding devices, headends and distribution networks, and equipment at or near our customers' homes. Our distribution network consists primarily of headends, content distribution servers, coaxial and fiber-optic cables, lasers, routers, switches and related electronic equipment. Our cable plant and related equipment generally are connected to utility poles under pole rental agreements with local public utilities, although in some areas the distribution cable is buried in underground ducts or trenches. Customer premise equipment consists primarily of set-top boxes, cable modems and wireless gateways. The physical components of cable systems require periodic maintenance and replacement.

Our signal reception sites, which consist primarily of antenna towers and headends, and our microwave facilities are located on owned and leased parcels of land, and we own or lease space on the towers on which certain of our equipment is located. We own most of our service vehicles.

Our high-speed Internet network consists of fiber-optic cables owned or leased by us and related equipment. We also operate national and regional data centers with equipment that is used to provide services, such as email and web services, to our high-speed Internet and voice customers, as well as cloud services to our video customers. In addition, we maintain network operations centers with equipment necessary to monitor and manage the status of our services and network.

We own or lease buildings throughout the country that contain customer service call centers, customer service retail centers, warehouses and administrative space. We also own a building that houses our digital media center. The digital media center contains equipment that we own or lease, including equipment related to network origination, video transmission via satellite and terrestrial fiber-optics, broadcast studios, post-production services and interactive television services.

#### NBCUniversal Segments

NBCUniversal's corporate headquarters are located in New York City at 30 Rockefeller Plaza. NBCUniversal owns the space it occupies at 30 Rockefeller Plaza. We also own or lease offices, studios, production facilities, screening rooms, retail operations, warehouse space, satellite transmission receiving facilities and data centers in numerous locations in the United States and around the world, including property for our owned local broadcast television stations. In addition, we own theme parks and related facilities in Orlando, Florida and Hollywood, California, as well as a 51% interest in the theme park and related facilities in Osaka, Japan.

Table of Contents

## NBCUniversal Properties as of December 31, 2016

Location	Principal Use	Principal Segment in Which Used	Owned or Leased
30 Rockefeller Plaza New York, NY	NBCUniversal corporate headquarters, offices and studios	Headquarters and Other, Cable Networks and Broadcast Television	Owned
10 Rockefeller Plaza New York, NY	<i>The Today Show</i> studio, production facilities and offices	Broadcast Television	Leased
Universal City Universal City, CA	Offices, studios, theme park and retail operations	All	Owned
1000 Universal Studios Plaza Orlando, FL	Theme parks, production facilities, parking structures and administrative buildings	Theme Parks	Owned
2 Chome-1-33 Sakurajima, Konohana Ward, Osaka, Osaka Prefecture 554-0031, Japan	Theme park and administrative buildings	Theme Parks	Tangible properties owned on leased parcels of land
2290 W. 8th Ave. Hialeah, FL	Telemundo headquarters and production facilities	Headquarters and Other and Broadcast Television	Leased

Other

The Wells Fargo Center, a large, multipurpose arena in Philadelphia, Pennsylvania that we own, was the principal physical operating asset of our other businesses as of December 31, 2016.

Item 3: Legal Proceedings

Refer to Note 16 to Comcast's consolidated financial statements included in this Annual Report on Form 10-K for a discussion of recent developments related to our legal proceedings.

NBCUniversal is subject to legal proceedings and claims that arise in the ordinary course of its business and it does not expect the final disposition of these matters to have a material adverse effect on its results of operations, cash flows or financial condition, although any such matters could be time-consuming and costly and could injure its reputation.

Item 4: Mine Safety Disclosures

Not applicable.

Table of Contents**Part II****Item 5: Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

Comcast's Class A common stock is listed on the NASDAQ Global Select Market under the symbol CMCSA. There is no established public trading market for Comcast's Class B common stock. The Class B common stock can be converted, on a share for share basis, into Class A common stock.

On January 24, 2017, our Board of Directors approved a two-for-one stock split in the form of a 100% dividend payable on February 17, 2017 to shareholders of record as of the close of business on February 8, 2017. As the common stock is not yet trading on a post-split basis, all share and per-share amounts are presented on a pre-split basis.

## Dividends Declared

2016		2015	
Month Declared:	Dividend Per Share	Month Declared:	Dividend Per Share
February	\$ 0.275	February	\$ 0.25
May	\$ 0.275	May	\$ 0.25
July	\$ 0.275	July	\$ 0.25
October (paid in January 2017)	\$ 0.275	October (paid in January 2016)	\$ 0.25
Total	\$ 1.10	Total	\$ 1.00

We expect to continue to pay quarterly dividends, although each dividend is subject to approval by our Board of Directors. In January 2017, our Board of Directors approved a 15% increase in our dividend to \$1.26 per share on an annualized, pre-split basis, or \$0.63 per share on an annualized, post-split basis. In addition, the Board of Directors approved our first quarter dividend of \$0.1575 a share on a post-split basis to be paid in April 2017.

Holders of Class A common stock in the aggregate hold 66  $\frac{2}{3}$ % of the voting power of our common stock. The number of votes that each share of Class A common stock has at any given time depends on the number of shares of Class A common stock and Class B common stock then outstanding. The Class B common stock has a 33  $\frac{1}{3}$ % nondilutable voting interest, and each share of Class B common stock has 15 votes per share. Mr. Brian L. Roberts beneficially owns all outstanding shares of Class B common stock. Generally, including as to the election of directors, holders of Class A common stock and Class B common stock vote as one class except where class voting is required by law.

Record holders as of December 31, 2016 are presented in the table below.

Stock Class	Record Holders
Class A Common Stock	463,104
Class B Common Stock	3

## Table of Contents

The table below summarizes our repurchases under our Board-authorized share repurchase program during 2016.

Period	Total Number of Shares Purchased	Average Price Per Share	Total Number of Shares Purchased as Part of Publicly Announced Authorization	Total Dollar Amount Purchased Under the Authorization	Maximum Dollar Value of Shares That May Yet Be Purchased Under the Authorization <sup>(a)</sup>
First Quarter 2016	22,025,226	\$ 56.82	21,989,334	\$ 1,249,417,635	\$ 8,750,582,365
Second Quarter 2016	18,418,256	\$ 61.66	18,418,136	\$ 1,135,699,704	\$ 7,614,882,661
Third Quarter 2016	20,836,401	\$ 66.07	20,836,288	\$ 1,376,575,738	\$ 6,238,306,923
October 1-31, 2016	13,294,399	\$ 64.00	13,294,399	\$ 850,819,050	\$ 5,387,487,873
November 1-30, 2016	4,036,116	\$ 61.80	4,036,116	\$ 249,446,256	\$ 5,138,041,617
December 1-31, 2016	1,995,929	\$ 69.18	1,995,464	\$ 138,041,588	\$ 5,000,000,029
<b>Total</b>	<b>80,606,327</b>	<b>\$ 62.06</b>	<b>80,569,737</b>	<b>\$ 4,999,999,971</b>	<b>\$ 5,000,000,029</b>

(a) In December 2015, our Board of Directors increased our share repurchase program authorization to \$10 billion, and in January 2017, it increased the authorization to \$12 billion, which does not have an expiration date.

The total number of shares purchased during 2016 includes 36,590 shares received in the administration of employee share-based compensation plans.

Under our share repurchase program authorization, we may repurchase shares in the open market or in private transactions. We expect to repurchase \$5.0 billion of our Class A common stock during 2017, subject to market conditions.

### Issuance of Equity Securities

In December 2016, we issued 356,635 shares of our Class A common stock to an institutional accredited investor in connection with an advance on future services in a transaction exempt from registration under the Securities Act of 1933, as amended, in accordance with Section 4(a)(2) thereof.

### Comcast Common Stock Sales Price Table

The following table sets forth, for the indicated periods, the high and low sales prices of Comcast's Class A and Class A Special common stock.

	Class A		Class A Special <sup>(a)</sup>	
	High	Low	High	Low
<b>2016</b>				
First Quarter	\$ 61.37	\$ 52.34	\$ —	\$ —
Second Quarter	\$ 65.42	\$ 59.62	\$ —	\$ —
Third Quarter	\$ 68.36	\$ 64.27	\$ —	\$ —
Fourth Quarter	\$ 71.32	\$ 60.04	\$ —	\$ —
<b>2015</b>				
First Quarter	\$ 60.70	\$ 52.45	\$ 60.19	\$ 52.23
Second Quarter	\$ 61.64	\$ 56.05	\$ 61.38	\$ 55.74
Third Quarter	\$ 64.99	\$ 50.00	\$ 64.70	\$ 51.26
Fourth Quarter <sup>(a)</sup>	\$ 63.38	\$ 55.39	\$ 63.48	\$ 56.88

(a) The high and low sales price of Comcast's Class A Special common stock reflects the prices until December 11, 2015, when each issued share of Class A Special common stock was reclassified into one share of Class A common stock (see Note 12 to Comcast's consolidated financial statements).

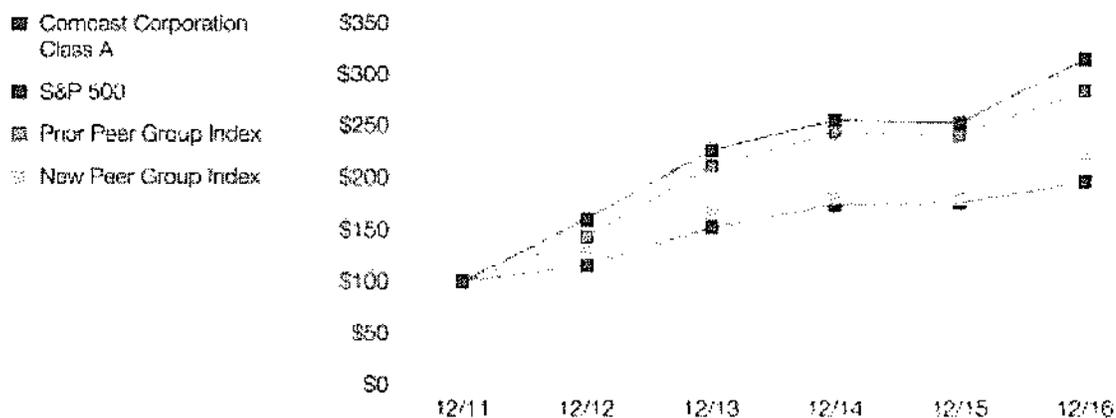
## Table of Contents

### Stock Performance Graph

#### Comcast

The following graph compares the annual percentage change in the cumulative total shareholder return on Comcast's Class A common stock during the five years ended December 31, 2016 with the cumulative total returns on the Standard & Poor's 500 Stock Index and with a select peer group consisting of us and other companies engaged in the cable, communications and media industries. This peer group (the "new peer group index") consists of our common stock, DISH Network Corporation (Class A), Charter Communications, Inc., AT&T Inc., Verizon Communications Inc., CenturyLink, Inc., and Sprint Corporation (the "transmission and distribution subgroup"); and Time Warner Inc., Walt Disney Company, Viacom Inc. (Class B), Twenty-First Century Fox, Inc. (Class A), and CBS Corporation (Class B) (the "media subgroup"). The new peer group index was created as a result of merger and acquisition activity that impacted our prior peer group index, which had consisted of our common stock as well as Cablevision Systems Corporation (Class A) (included through June 21, 2016, the date of acquisition by Altice NV), DISH Network Corporation (Class A), DirecTV Inc. (included through July 24, 2015, the date of acquisition by AT&T Inc.), Time Warner Cable Inc. (included through May 18, 2016, the date of acquisition by Charter Communications, Inc.) (the "cable subgroup"); and Time Warner Inc., Walt Disney Company, Viacom Inc. (Class B), Twenty-First Century Fox, Inc. (Class A), and CBS Corporation (Class B) (the "media subgroup"). The peer groups are constructed as composite peer groups in which the transmission and distribution subgroup and the cable subgroup are weighted 61% and the media subgroup is weighted 39% based on the respective revenue of our Cable Communications and NBCUniversal segments. The comparison assumes \$100 was invested on December 31, 2011 in our Class A common stock and in each of the following indices and assumes the reinvestment of dividends.

#### Comparison of 5 Year Cumulative Total Return



	2012	2013	2014	2015	2016
Comcast Class A	\$ 160	\$ 226	\$ 256	\$ 253	\$ 316
S&P 500 Stock Index	\$ 116	\$ 153	\$ 174	\$ 176	\$ 197
Prior Peer Group Index	\$ 144	\$ 211	\$ 244	\$ 242	\$ 284
New Peer Group Index	\$ 130	\$ 170	\$ 180	\$ 178	\$ 220

#### NBCUniversal

NBCUniversal is a wholly owned subsidiary of NBCUniversal Holdings and there is no market for its equity securities.

Table of Contents

## Item 6: Selected Financial Data

## Comcast

Year ended December 31 (in millions, except per share data)	2016	2015	2014	2013	2012
<b>Statement of Income Data</b>					
Revenue	\$ 80,403	\$ 74,510	\$ 68,775	\$ 64,657	\$ 62,570
Operating income	16,859	15,998	14,904	13,563	12,179
Net income attributable to Comcast Corporation <sup>(a)</sup>	8,695	8,163	8,380	6,816	6,203
Basic earnings per common share attributable to Comcast Corporation shareholders <sup>(b)</sup>	3.61	3.28	3.24	2.60	2.32
Diluted earnings per common share attributable to Comcast Corporation shareholders <sup>(b)</sup>	3.57	3.24	3.20	2.56	2.28
Dividends declared per common share <sup>(b)</sup>	1.10	1.00	0.90	0.78	0.65
<b>Balance Sheet Data (at year end)</b>					
Total assets	\$ 180,500	\$ 166,574	\$ 159,186	\$ 158,672	\$ 164,837
Total debt, including current portion	61,046	52,621	48,081	47,706	40,323
Comcast Corporation shareholders' equity	53,943	52,269	52,711	50,694	49,356
<b>Statement of Cash Flows Data</b>					
Net cash provided by (used in):					
Operating activities	19,240	18,778	16,945	14,160	14,854
Investing activities	(18,385)	(11,964)	(8,733)	(9,514)	(1,486)
Financing activities	151	(8,429)	(6,020)	(13,879)	(4,037)

(a) For 2016, 2015 and 2014, refer to Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations included in this Annual Report on Form 10-K for a discussion of the effects of items impacting net income attributable to Comcast Corporation. In 2016, 2015, 2014, 2013 and 2012, net income attributable to Comcast Corporation is stated after deducting net income attributable to noncontrolling interests of \$350 million, \$250 million, \$212 million, \$319 million and \$1.7 billion, respectively. The reduction in net income attributable to noncontrolling interests in 2013 was primarily due to our acquisition of General Electric Company's remaining interest in NBCUniversal.

(b) Per share amounts are presented on a pre-split basis (see Note 1 to Comcast's consolidated financial statements).

## NBCUniversal

Omitted pursuant to General Instruction I(2)(a) to Form 10-K.

## Table of Contents

# Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations

## Introduction and Overview

We are a global media and technology company with two primary businesses, Comcast Cable and NBCUniversal. We present our operations for Comcast Cable in one reportable business segment, referred to as Cable Communications, and our operations for NBCUniversal in four reportable business segments: Cable Networks, Broadcast Television, Filmed Entertainment and Theme Parks (collectively, the "NBCUniversal segments").

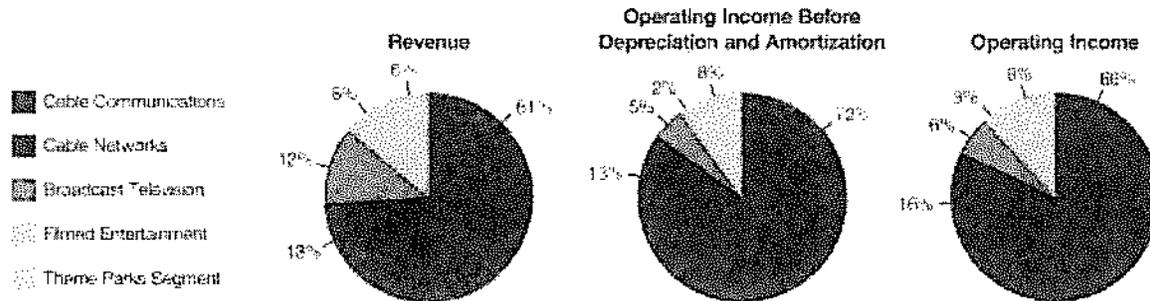
The following provides an overview of our businesses.

### Consolidated Revenue and Operating Income

(in billions)



### 2016 Consolidated Operating Results by Segment<sup>(a)</sup>



(a) Excludes the results of NBCUniversal Headquarters and Other, Corporate and Other, and eliminations.

### Cable Communications Segment

Comcast Cable is one of the nation's largest providers of video, high-speed Internet and voice services ("cable services") to residential customers under the XFINITY brand, and we also provide these and other services to business customers. As of December 31, 2016, our cable systems had 28.6 million total customer relationships, of which 26.5 million were residential customer relationships; served 22.5 million video customers, 24.7 million high-speed Internet customers and 11.7 million voice customers; and passed more than 56 million homes and businesses.

Our Cable Communications segment generates revenue primarily from residential and business customers subscribing to our cable services, which we market individually and as bundled services, and from the sale of advertising. Customers are typically billed in advance on a monthly basis based on the services and features

## Table of Contents

they receive and the type of equipment they use. The majority of our residential cable services customers are not subject to minimum-term contracts for their services, while substantially all of our business customers are. Minimum-term contracts are typically 2 years in length for residential customers and typically range from 2 to 5 years for business services customers. Customers with minimum-term contracts may only discontinue service in accordance with the terms of their contracts, which typically include an early termination fee.

### **NBCUniversal Segments**

NBCUniversal is one of the world's leading media and entertainment companies that develops, produces and distributes entertainment, news and information, sports, and other content for global audiences, and owns and operates theme parks worldwide.

#### Cable Networks

Our Cable Networks segment consists primarily of a diversified portfolio of cable television networks. Our cable networks are comprised of our national cable entertainment networks (USA Network, E!, Syfy, Bravo, Oxygen, Sprout, Esquire Network, Chiller, Universal HD and Cloo), our national cable news and information networks (MSNBC, CNBC and CNBC World), our national cable sports networks (NBC Sports Network and Golf Channel), our regional sports and news networks, our international cable networks, our cable television studio production operations, and related digital media properties.

Our Cable Networks segment generates revenue primarily from the distribution and licensing of its programming and from the sale of advertising on its networks.

#### Broadcast Television

Our Broadcast Television segment consists primarily of the NBC and Telemundo broadcast television networks, our NBC and Telemundo owned local broadcast television stations, the NBC Universo national cable network, our broadcast television studio production operations, and related digital media properties.

Our Broadcast Television segment generates revenue primarily from the sale of advertising on its networks, from the licensing of its programming, and from fees received under retransmission consent agreements and associated fees received from NBC-affiliated local broadcast television stations.

#### Filmed Entertainment

Our Filmed Entertainment segment primarily produces, acquires, markets and distributes filmed entertainment worldwide, and it also develops, produces and licenses live stage plays. Our films are produced primarily under the Universal Pictures, Illumination and Focus Features names, and in August 2016, we acquired DreamWorks Animation. DreamWorks Animation creates animated feature films, television series and specials, live entertainment and related consumer products.

Our Filmed Entertainment segment generates revenue primarily from the worldwide distribution of our owned and acquired films for exhibition in movie theaters and from the licensing and sale of our owned and acquired films.

#### Theme Parks

Our Theme Parks segment consists primarily of our Universal theme parks in Orlando, Florida and Hollywood, California and our 51% interest in the Universal Studios theme park in Osaka, Japan ("Universal Studios Japan"), which we acquired in November 2015. In addition, along with a consortium of Chinese state-owned companies, we are developing a theme park in China.

Our Theme Parks segment generates revenue primarily from ticket sales and guest spending at our theme parks.

## Table of Contents

### **Corporate and Other**

Our other business interests consist primarily of the operations of Comcast Spectacor, which owns the Philadelphia Flyers and the Wells Fargo Center arena in Philadelphia, Pennsylvania and operates arena management-related businesses.

We currently anticipate launching a Comcast-branded wireless phone service in 2017 using our virtual network operator rights to provide the service over a third party's wireless network, although we are still evaluating the parameters of the anticipated offering. A wireless phone service will have success-based working capital requirements, primarily associated with the procurement of handsets and other equipment, as we launch the new service.

### **2016 Developments**

The following are the more significant developments in our businesses during 2016:

#### Cable Communications Segment

- An increase in revenue of 6.6% to \$50.0 billion and an increase in operating income before depreciation and amortization of 5.6% to \$20.1 billion
- A decrease in operating margin to 40.2% primarily due to higher programming expenses, which were partially offset by increases in high-speed Internet, video and business services revenue
- Investments to improve the customer experience, including by hiring additional personnel and developing and deploying various technology and software tools
- An increase in capital expenditures of 7.9% to \$7.6 billion primarily due to:
  - an increased investment in line extensions, primarily for the expansion of our business services
  - an increased investment in scalable infrastructure to increase network capacity
  - the continued deployment of wireless gateways
  - the continued deployment of our X1 platform, which is now available in all of the markets in which we operate, and our cloud DVR technology, which is now available in substantially all of our markets

#### NBCUniversal Segments

- An increase in total NBCUniversal revenue of 11.0% to \$31.6 billion; excluding \$1.6 billion of revenue associated with our broadcast of the Rio Olympics in August 2016, as well as \$376 million of revenue associated with our broadcast of the Super Bowl in February 2015, total NBCUniversal revenue increased 6.7%
- An increase in total NBCUniversal operating income before depreciation and amortization of 13.8% to \$7.2 billion
- An increase in Cable Networks segment revenue of 8.7%, including \$432 million associated with our broadcast of the 2016 Rio Olympics
- An increase in Broadcast Television segment revenue of 19.0%, including \$1.2 billion associated with our broadcast of the 2016 Rio Olympics
- The acquisition of DreamWorks Animation for \$3.8 billion in our Filmed Entertainment segment

## Table of Contents

- An increase in Theme Parks segment revenue of 12.7% on a pro forma combined basis to include Universal Studios Japan

### Corporate and Other

- The announcement that we anticipate launching a Comcast-branded wireless phone service in 2017 using our virtual network operator rights to provide the service over a third party's wireless network

### **Competition**

The results of operations of our reportable business segments are affected by competition, as all of our businesses operate in intensely competitive, consumer-driven and rapidly changing environments and compete with a growing number of companies that provide a broad range of communications products and services and entertainment, news and information content to consumers.

For additional information on the competition our businesses face, see Item 1: Business and refer to the "Competition" discussion within that section and see Item 1A: Risk Factors and refer to the risk factors within that section entitled "Our businesses currently face a wide range of competition, and our businesses and results of operations could be adversely affected if we do not compete effectively" and "Changes in consumer behavior driven by new technologies and distribution platforms for viewing content may adversely affect our businesses and challenge existing business models."

### **Seasonality and Cyclicity**

Each of our businesses is subject to seasonal and cyclical variations. In our Cable Communications segment, our results are impacted by the seasonal nature of customers receiving our cable services in college and vacation markets. This generally results in a reduction in net customer additions in the second quarter and an increase in net customer additions in the third and fourth quarters of each year.

Revenue in our Cable Communications, Cable Networks and Broadcast Television segments is subject to cyclical advertising patterns and changes in viewership levels. Advertising revenue in the U.S. is generally higher in the second and fourth quarters of each year, due in part to increases in consumer advertising in the spring and in the period leading up to and including the holiday season. Advertising revenue in the U.S. is also cyclical, with a benefit in even-numbered years due to advertising related to candidates running for political office and issue-oriented advertising. Revenue in our Cable Networks and Broadcast Television segments fluctuates depending on the timing of when our programming is aired, which typically results in higher advertising revenue in the second and fourth quarters of each year. Our revenue and operating costs and expenses, excluding depreciation and amortization ("operating costs and expenses") are cyclical as a result of our periodic broadcasts of major sporting events, such as the Olympic Games, which affect our Cable Networks and Broadcast Television segments, and the Super Bowl, which affects our Broadcast Television segment. Our advertising revenue increases in the period of these broadcasts due to increased demand for advertising time, and our operating costs and expenses also increase as a result of our production costs and the amortization of the related rights fees.

Revenue in our Filmed Entertainment segment fluctuates due to the timing of the release of films in movie theaters, on standard-definition digital video discs and Blu-ray discs (together, "DVDs") and through various other distribution platforms. Release dates are determined by several factors, including competition and the timing of vacation and holiday periods. As a result, revenue tends to be seasonal, with increases experienced each year during the summer months and around the holiday season. Revenue in our Cable Networks, Broadcast Television and Filmed Entertainment segments also fluctuates due to the timing of when our content is made available to licensees.

## Table of Contents

Revenue in our Theme Parks segment fluctuates with changes in theme park attendance that result from the seasonal nature of vacation travel and weather variations, local entertainment offerings and the opening of new attractions as well as with changes in currency exchange rates. Our theme parks generally experience peak attendance during the spring holiday period, the summer months when schools are closed and the holiday season.

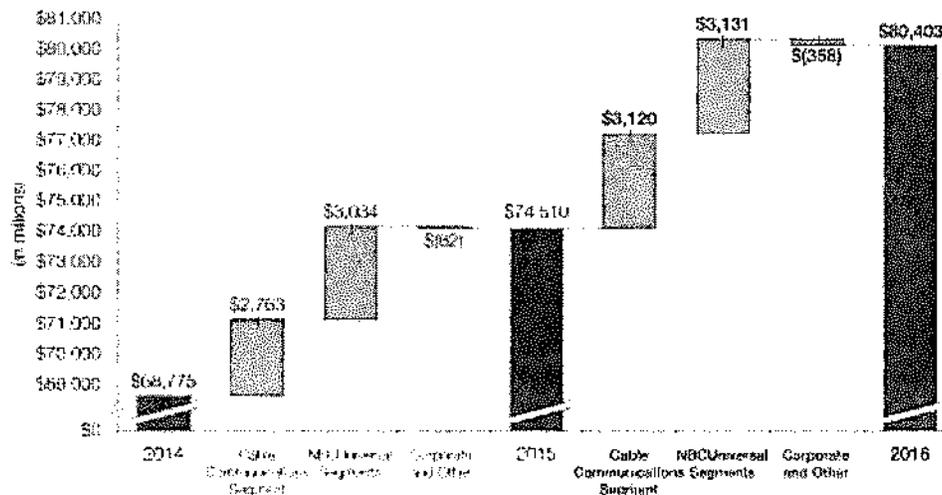
## Consolidated Operating Results

Year ended December 31 (in millions)	2016	2015	2014	% Change 2015 to 2016	% Change 2014 to 2015
<b>Revenue</b>	<b>\$ 80,403</b>	<b>\$ 74,510</b>	<b>\$ 68,775</b>	<b>7.9%</b>	<b>8.3%</b>
Costs and Expenses:					
Programming and production	24,463	22,550	20,912	8.5	7.8
Other operating and administrative	23,409	21,319	19,839	9.8	7.5
Advertising, marketing and promotion	6,114	5,963	5,101	2.5	16.9
Depreciation	7,464	6,781	6,337	10.1	7.0
Amortization	2,094	1,899	1,682	10.3	12.8
<b>Operating income</b>	<b>16,859</b>	<b>15,998</b>	<b>14,904</b>	<b>5.4</b>	<b>7.3</b>
Other income (expense) items, net	(2,506)	(2,626)	(2,439)	(4.6)	7.7
Income before income taxes	14,353	13,372	12,465	7.3	7.3
Income tax expense	(5,308)	(4,959)	(3,873)	7.0	28.0
Net income	9,045	8,413	8,592	7.5	(2.1)
Net (income) loss attributable to noncontrolling interests and redeemable subsidiary preferred stock	(350)	(250)	(212)	39.3	18.1
<b>Net income attributable to Comcast Corporation</b>	<b>\$ 8,695</b>	<b>\$ 8,163</b>	<b>\$ 8,380</b>	<b>6.5%</b>	<b>(2.6)%</b>

All percentages are calculated based on actual amounts. Minor differences may exist due to rounding.

## Consolidated Revenue

The following graph illustrates the contributions to the increases in consolidated revenue made by our Cable Communications and NBCUniversal segments, as well as by Corporate and Other activities including eliminations.



## Table of Contents

The primary drivers of the changes in revenue were as follows:

2016

- Growth in our Cable Communications segment driven by our high-speed Internet, video and business services businesses
- Our broadcast of the 2016 Rio Olympics that generated \$1.6 billion of revenue, which was reported in our NBCUniversal segments

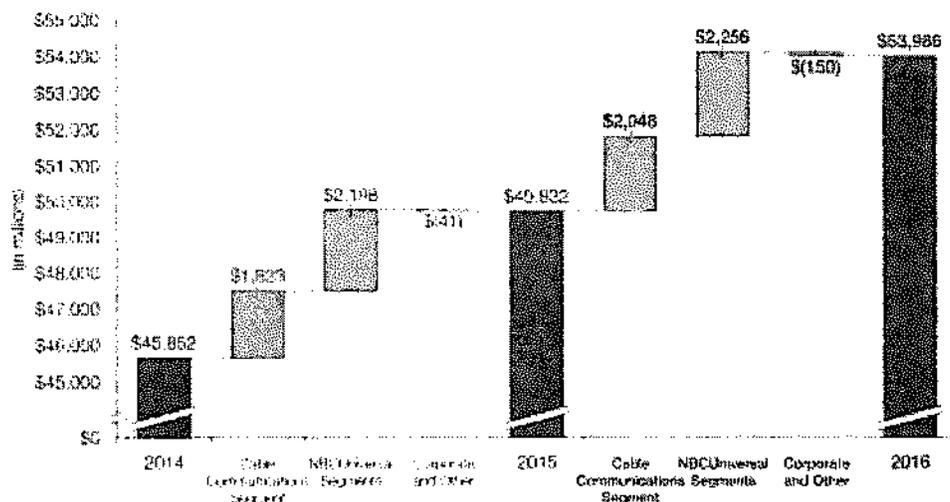
2015

- Growth in our Cable Communications segment driven by our high-speed Internet, business services and video businesses
- Our larger film slate in our Filmed Entertainment segment, which led to an increase in revenue of \$2.3 billion, and our broadcast of the 2015 Super Bowl, which generated \$376 million of revenue, both of which were reported in our NBCUniversal segments

Revenue for our segments is discussed separately below under the heading "Segment Operating Results." Revenue for our other businesses is discussed separately under the heading "Corporate and Other Results of Operations."

### Consolidated Costs and Expenses

The following graph illustrates the contributions to the increases in consolidated operating costs and expenses made by our Cable Communications and NBCUniversal segments, as well as by Corporate and Other activities including eliminations.



The primary drivers of the changes in operating costs and expenses were as follows:

2016

- An increase in programming expenses in our Cable Communications segment
- Our broadcast of the 2016 Rio Olympics, which was reported in our NBCUniversal segments

## Table of Contents

### 2015

- An increase in programming expenses in our Cable Communications segment
- Our larger film slate and our broadcast of the 2015 Super Bowl, both of which were reported in our NBCUniversal segments
- Transaction-related costs associated with the Time Warner Cable merger and the related divestiture transactions of \$178 million, which were reported in Corporate and Other activities. In April 2015, we and Time Warner Cable Inc. terminated our planned merger and, as a result, we terminated our related agreement with Charter Communications, Inc. to spin off, exchange and sell certain cable systems

Operating costs and expenses for our segments is discussed separately below under the heading "Segment Operating Results." Operating costs and expenses for our other businesses is discussed separately below under the heading "Corporate and Other Results of Operations."

### Consolidated Depreciation and Amortization

Year ended December 31 (in millions)	2016	2015	2014	% Change 2015 to 2016	% Change 2014 to 2015
Cable Communications	\$ 7,670	\$ 7,051	\$ 6,436	8.8%	9.6%
NBCUniversal	1,805	1,539	1,495	17.3	2.9
Corporate and Other	83	90	88	(7.3)	1.3
<b>Comcast Consolidated</b>	<b>\$ 9,558</b>	<b>\$ 8,680</b>	<b>\$ 8,019</b>	<b>10.1%</b>	<b>8.2%</b>

Consolidated depreciation and amortization expense increased in 2016 and 2015 primarily due to increases in capital expenditures, as well as expenditures for software, in our Cable Communications segment in recent years. We continue to invest to increase our network capacity and in customer premise equipment, primarily for our X1 platform and cloud DVR technology and for wireless gateways. In addition, because these assets generally have shorter estimated useful lives, our depreciation expenses have increased and we expect this will continue in 2017. NBCUniversal depreciation and amortization expense also increased due to the acquisition of the 51% interest in Universal Studios Japan in November 2015 and our investments in new attractions in the Theme Parks segment.

### Segment Operating Results

Our segment operating results are presented based on how we assess operating performance and internally report financial information. We use operating income (loss) before depreciation and amortization, excluding impairment charges related to fixed and intangible assets and gains or losses from the sale of assets, if any, as the measure of profit or loss for our operating segments. This measure eliminates the significant level of noncash depreciation and amortization expense that results from the capital-intensive nature of certain of our businesses and from intangible assets recognized in business combinations. Additionally, it is unaffected by our capital structure or investment activities. We use this measure to evaluate our consolidated operating performance and the operating performance of our operating segments and to allocate resources and capital to our operating segments. It is also a significant performance measure in our annual incentive compensation programs. We believe that this measure is useful to investors because it is one of the bases for comparing our operating performance with that of other companies in our industries, although our measure may not be directly comparable to similar measures used by other companies. Because we use operating income (loss) before depreciation and amortization to measure our segment profit or loss, we reconcile it to operating income, the most directly comparable financial measure calculated and presented in accordance with generally accepted accounting principles in the United States ("GAAP"), in the business segment footnote to our

**Table of Contents**

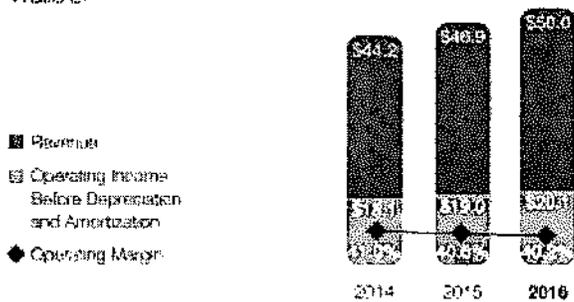
consolidated financial statements (see Note 17 to Comcast's consolidated financial statements and Note 16 to NBCUniversal's consolidated financial statements). This measure should not be considered a substitute for operating income (loss), net income (loss) attributable to Comcast Corporation or NBCUniversal, net cash provided by operating activities, or other measures of performance or liquidity we have reported in accordance with GAAP.

The revenue and operating costs and expenses associated with our broadcasts of the 2016 Rio Olympics and the Sochi Olympics in February 2014 were reported in our Cable Networks and Broadcast Television segments. The revenue and operating costs and expenses associated with our broadcast of the 2015 Super Bowl were reported in our Broadcast Television segment.

We have adjusted prior period segment operating results to reflect certain changes in our management reporting presentation. See Note 17 to Comcast's consolidated financial statements for additional information on these changes.

**Cable Communications Segment Results of Operations**

**Revenue and Operating Income Before Depreciation and Amortization**  
in billions



**Customer Relationships**  
in millions

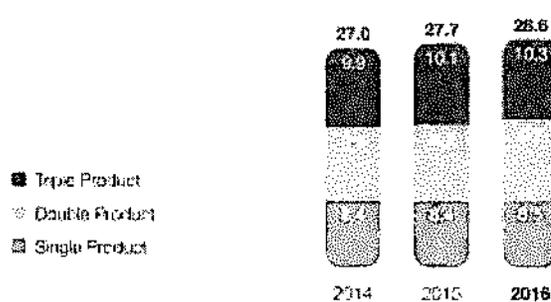


Table of Contents

Year ended December 31 (in millions)	2016	2015	2014	% Change 2015 to 2016	% Change 2014 to 2015
<b>Revenue</b>					
Residential:					
Video	\$ 22,357	\$ 21,526	\$ 20,783	3.9%	3.6%
High-speed Internet	13,532	12,471	11,321	8.5	10.2
Voice	3,540	3,608	3,671	(1.9)	(1.7)
Business services	5,514	4,751	3,960	16.1	20.0
Advertising	2,518	2,298	2,388	9.6	(3.8)
Other	2,587	2,274	2,042	13.8	11.3
<b>Total revenue</b>	<b>50,048</b>	<b>46,928</b>	<b>44,165</b>	<b>6.6</b>	<b>6.3</b>
<b>Operating costs and expenses</b>					
Programming	11,576	10,516	9,819	10.1	7.1
Technical and product support	6,371	5,996	5,594	6.3	7.2
Customer service	2,486	2,396	2,226	3.7	7.7
Franchise and other regulatory fees	1,481	1,382	1,296	7.2	6.7
Advertising, marketing and promotion	3,547	3,369	3,098	5.3	8.7
Other	4,478	4,232	4,035	5.8	4.8
<b>Total operating costs and expenses</b>	<b>29,939</b>	<b>27,891</b>	<b>26,068</b>	<b>7.3</b>	<b>7.0</b>
<b>Operating income before depreciation and amortization</b>	<b>\$ 20,109</b>	<b>\$ 19,037</b>	<b>\$ 18,097</b>	<b>5.6%</b>	<b>5.2%</b>

## Customer Metrics

December 31 (in thousands)	Total Customers			Net Additional Customers		
	2016	2015	2014	2016	2015	2014
Total customer relationships <sup>(a)</sup>	28,559	27,701	27,035	858	666	358
Single product customers <sup>(a)</sup>	8,541	8,366	8,409	175	(43)	(343)
Double product customers <sup>(a)</sup>	9,699	9,221	8,750	477	472	209
Triple product customers <sup>(a)</sup>	10,319	10,114	9,876	205	238	492
Video customers	22,608	22,347	22,383	161	(36)	(194)
High-speed Internet customers	24,701	23,329	21,962	1,373	1,367	1,277
Voice customers	11,687	11,475	11,193	211	282	470
<b>Average monthly total revenue per customer relationship</b>	<b>\$ 148.26</b>	<b>\$ 142.89</b>	<b>\$ 137.04</b>			

Customer metrics include residential and business customers and are presented based on actual amounts. Minor differences may exist due to rounding.

(a) Customer relationships represent the number of residential and business customers that subscribe to at least one of our cable services. Single product, double product and triple product customers represent customers that subscribe to one, two or three of our cable services, respectively.

**Cable Communications Segment – Revenue**

## Video

Our Cable Communications segment offers a broad variety of video service packages that may include premium networks, pay-per-view services and our On Demand service. Our video customers may subscribe for additional fees to our high-definition ("HD") video and digital video recorder ("DVR") advanced services. We are actively deploying set-top boxes for our Internet Protocol ("IP") and cloud-enabled video platform, referred to as our X1 platform, and cloud DVR technology throughout our footprint.

## Table of Contents

Video revenue increased 3.9% and 3.6% in 2016 and 2015, respectively. The increases in revenue in both years were primarily due to rate adjustments and an increase in the number of residential customers subscribing to additional services such as premium channels and advanced services, which accounted for increases in revenue of 3.9% and 4.5% in 2016 and 2015, respectively. As of December 31, 2016, 14.8 million customers subscribed to at least one of our HD or DVR advanced services compared to 13.9 million customers and 13.0 million customers as of December 31, 2015 and 2014, respectively. Net additional video customers increased in 2016 primarily due to reduced customer churn, which we believe is a result of our continued deployment of our X1 platform as well as improvements we have made in the customer experience. The increase in revenue in 2015 was partially offset by a decrease in the number of residential video customers, which was primarily due to competitive pressures and the impact of rate adjustments.

As of December 31, 2016, 39.9% of the homes and businesses in the areas we serve subscribed to our video services, compared to 40.1% and 40.9% as of December 31, 2015 and 2014, respectively. We have in the past, and may in the future, experience declines in the number of residential video customers due to competitive pressures and the impact of rate adjustments.

### High-Speed Internet

We offer high-speed Internet services with downstream speeds from a range of up to 10 Mbps to fiber-based speeds up to 2 Gbps. We are actively deploying wireless gateways throughout our footprint, which combine a customer's wireless router, cable modem and voice adapter, to improve the performance of multiple IP-enabled devices used at the same time within the home, provide faster Internet speeds and create an in-home Wi-Fi network. We are continuing to expand our network of residential, outdoor and business Wi-Fi hotspots to allow most of our high-speed Internet customers to access our high-speed Internet services inside and outside the home. As of December 31, 2016, there were approximately 15.8 million of these hotspots.

High-speed Internet revenue increased 8.5% and 10.2% in 2016 and 2015, respectively. Increases in the number of residential customers receiving our high-speed Internet services accounted for increases in revenue of 5.8% in both 2016 and 2015. The remaining increases in revenue in both 2016 and 2015 were primarily due to increases in the number of customers receiving higher levels of service and the impact of rate adjustments.

As of December 31, 2016, 43.8% of the homes and businesses in the areas we serve subscribed to our high-speed Internet services, compared to 41.9% and 40.2% as of December 31, 2015 and 2014, respectively. Our customer base continues to grow as consumers choose our high-speed Internet service and seek higher-speed offerings.

### Voice

We offer voice services that provide local and long-distance calling and other related features.

Voice revenue decreased 1.9% and 1.7% in 2016 and 2015, respectively. While the number of residential customers receiving voice services through our discounted bundled service offerings increased in both years, revenue was negatively impacted by the allocation of voice revenue for our customers who receive bundled services. The amount allocated to voice revenue in the rate charged for bundled services decreased in both years because video and high-speed Internet rates increased while voice rates remained relatively flat.

As of December 31, 2016, 20.7% of the homes and businesses in the areas we serve subscribed to our voice services, compared to 20.6% and 20.5% as of December 31, 2015 and 2014, respectively.

## Table of Contents

### Business Services

We offer our cable services to small and medium-sized businesses and to large enterprises with multiple locations. We offer Ethernet network services that connect multiple locations and provide higher downstream and upstream speed options to medium-sized businesses and large enterprises. We also provide cellular backhaul services to mobile network operators to help those customers manage network bandwidth.

Business services revenue increased 16.1% and 20.0% in 2016 and 2015, respectively. The increase in 2016 was primarily due to an increase in the number of small business customers, as well as continued growth in our medium-sized business services, including Ethernet network and advanced voice services. The increase in 2015 was primarily due to an increase in the number of small business customers receiving our high-speed Internet and voice services and rate adjustments. In 2016, 2015 and 2014, our small business customers represented more than 70% of total business services revenue. We believe the increases in the number of business customers were primarily the result of our efforts to gain market share from competitors by offering competitive services and pricing, although the rate of growth in the number of our small business customers may slow as the business matures.

### Advertising

Our Cable Communications segment also sells advertising. As part of our distribution agreements with cable networks, we generally receive an allocation of scheduled advertising time on cable networks that we sell through our advertising business, Spotlight, to local, regional and national advertisers. In most cases, the available advertising units are sold by our sales force. In some cases, we work with representation firms as an extension of our sales force to sell a portion of the advertising units allocated to us. We also represent the advertising sales efforts of other multichannel video providers in some markets. In addition, we generate revenue from the sale of advertising online and on our On Demand service. Advertising revenue is affected by the strength of the advertising market and general economic conditions.

Advertising revenue increased 9.6% in 2016 primarily due to an increase in political advertising revenue. Advertising revenue decreased 3.8% in 2015 primarily due to a decrease in political advertising revenue. Excluding the impact of political advertising revenue, advertising revenue increased slightly in 2016 and 3.0% in 2015.

In 2016, 5% of our Cable Communications segment advertising revenue was generated from our NBCUniversal segments, compared to 6% and 5% in 2015 and 2014, respectively. These amounts are eliminated in our consolidated financial statements but are included in the amounts presented above.

### Other

Other revenue primarily includes revenue related to cable franchise and other regulatory fees. We also receive revenue related to fees from other services, such as our home security and automation services. Cable franchise and other regulatory fees represent the fees we are required to pay to federal, state and local authorities that we pass through to our customers. Under the terms of our cable franchise agreements, we are generally required to pay to the cable franchising authority an amount based on our gross video revenue. The changes in franchise and other regulatory fees collected from our cable services customers are generally due to changes in the revenue to which the fees apply.

Other revenue increased 13.8% and 11.3% in 2016 and 2015, respectively, primarily due to increases in cable franchise and other regulatory fees, revenue from our home security and automation services and revenue from other services.

Table of Contents**Cable Communications Segment – Operating Costs and Expenses****Programming Expenses**

Programming expenses, which represent our most significant operating expense, are the fees we incur to provide content to our video customers. These expenses are affected by the programming license fees charged by cable networks, the fees charged for retransmission of the signals from local broadcast television stations, the number of video customers we serve and the amount of content we provide. Programming expenses increased in 2016 and 2015 primarily due to increases in programming license fees, including retransmission consent fees, sports programming costs and fees to secure rights for additional programming for distribution across an increasing number of platforms.

We anticipate that our programming expenses will increase at a higher growth rate in 2017, as the fees we pay will increase primarily due to the timing of contract renewals and increases in retransmission consent fees and sports programming costs; as we provide additional content to our video customers; and as we deliver this content through an increasing number of platforms, including On Demand, online and through our mobile apps. We believe that adding more content and delivering it on various platforms will help us to attract and retain video customers.

**Technical and Product Support Expenses**

Technical and product support expenses include costs to complete service call and installation activities, as well as costs for network operations, product development, fulfillment and provisioning. Technical and product support expenses increased in 2016 and 2015 primarily due to expenses related to the development, delivery and support of our enhanced devices and services, including our X1 platform, cloud DVR technology and wireless gateways, and continued growth in business services and home security and automation services. The increases in both years were also due to expenses related to investments to improve the customer experience.

**Customer Service Expenses**

Customer service expenses include the personnel and other costs associated with handling the sale of services to customers and customer service activity. Customer service expenses increased in 2016 and 2015 primarily due to increased support for improving the customer experience and increases in total labor costs, which reflect sales and support activities associated with the continued deployment of our enhanced devices and services, including our X1 platform and wireless gateways, and continued growth in business services and home security and automation services. The rate of growth of our customer service expenses decreased in 2016 primarily due to reduced call volumes.

**Franchise and Other Regulatory Fees**

Franchise and other regulatory fees increased in 2016 and 2015 primarily due to increases in the revenue to which the fees apply.

**Advertising, Marketing and Promotion Expenses**

Advertising, marketing and promotion expenses increased in 2016 and 2015 primarily due to increases in spending associated with attracting new residential and business services customers and encouraging existing customers to add additional or higher-tier services.

**Other Operating Costs and Expenses**

Other operating costs and expenses increased in 2016 and 2015 primarily due to increases in costs to support our advertising sales business, as well as increases in other administrative costs.

## Table of Contents

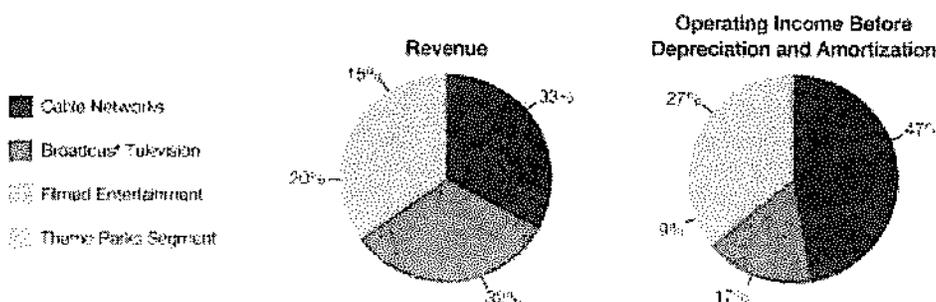
### Cable Communications Segment – Operating Margin

Our Cable Communications segment operating margin is operating income before depreciation and amortization as a percentage of revenue. The most significant operating margin costs and expenses for our Cable Communications segment are the programming expenses we incur to provide content to our video customers. We expect that our programming expenses will continue to increase, which may negatively impact our operating margin. We will attempt to mitigate increases in operating costs and expenses by growing revenue, particularly in our high-speed Internet, video and business services businesses and through cost management.

Our operating margin in 2016, 2015 and 2014 was 40.2%, 40.6% and 41.0%, respectively.

### NBCUniversal Segments Overview

#### 2016 NBCUniversal Segments Operating Results<sup>(a)</sup>



(a) Excludes the results of NBCUniversal Headquarters, Other and eliminations.

Year ended December 31 (in millions)	2016 Actual	2015		% Change 2015 to 2016		
		Actual	Pro Forma Adjustments <sup>(a)</sup>	Pro Forma Combined	Actual	Pro Forma Combined
<b>Revenue</b>						
Cable Networks	\$ 10,464	\$ 9,628	\$ —	\$ 9,628	8.7%	
Broadcast Television	10,147	8,530	—	8,530	19.0	
Filmed Entertainment	6,360	7,287	—	7,287	(12.7)	
Theme Parks	4,946	3,339	1,052	4,391	48.2	12.7%
Headquarters, other and eliminations	(324)	(322)	—	(322)	NM	
<b>Total revenue</b>	<b>\$ 31,593</b>	<b>\$ 28,462</b>	<b>\$ 1,052</b>	<b>\$ 29,514</b>	<b>11.0%</b>	<b>7.0%</b>
<b>Operating Income Before Depreciation and Amortization</b>						
Cable Networks	\$ 3,709	\$ 3,499	\$ —	\$ 3,499	6.0%	
Broadcast Television	1,320	780	—	780	69.1	
Filmed Entertainment	697	1,234	—	1,234	(43.5)	
Theme Parks	2,190	1,464	488	1,952	49.6	12.2%
Headquarters, other and eliminations	(689)	(625)	—	(625)	(10.1)	
<b>Total operating income before depreciation and amortization</b>	<b>\$ 7,227</b>	<b>\$ 6,352</b>	<b>\$ 488</b>	<b>\$ 6,840</b>	<b>13.8%</b>	<b>5.7%</b>

**Table of Contents**

Year ended December 31 (in millions)	2015			2014			% Change 2014 to 2015	
	Actual	Pro Forma Adjustments <sup>(a)</sup>	Pro Forma Combined	Actual	Pro Forma Adjustments <sup>(a)</sup>	Pro Forma Combined	Actual	Pro Forma Combined
<b>Revenue</b>								
Cable Networks	\$ 9,628	\$ —	\$ 9,628	\$ 9,563	\$ —	\$ 9,563	0.7%	
Broadcast Television	8,530	—	8,530	8,542	—	8,542	(0.1)	
Filmed Entertainment	7,287	—	7,287	5,008	—	5,008	45.5	
Theme Parks	3,339	1,052	4,391	2,623	1,085	3,708	27.3	18.4%
Headquarters, other and eliminations	(322)	—	(322)	(308)	—	(308)	NM	
<b>Total revenue</b>	<b>\$ 28,462</b>	<b>\$ 1,052</b>	<b>\$ 29,514</b>	<b>\$ 25,428</b>	<b>\$ 1,085</b>	<b>\$ 26,513</b>	<b>11.9%</b>	<b>11.3%</b>
<b>Operating Income Before Depreciation and Amortization</b>								
Cable Networks	\$ 3,499	\$ —	\$ 3,499	\$ 3,589	\$ —	\$ 3,589	(2.5)%	
Broadcast Television	780	—	780	734	—	734	6.3	
Filmed Entertainment	1,234	—	1,234	711	—	711	73.5	
Theme Parks	1,464	488	1,952	1,096	451	1,547	33.5	26.2%
Headquarters, other and eliminations	(625)	—	(625)	(614)	—	(614)	(1.8)	
<b>Total operating income before depreciation and amortization</b>	<b>\$ 6,352</b>	<b>\$ 488</b>	<b>\$ 6,840</b>	<b>\$ 5,516</b>	<b>\$ 451</b>	<b>\$ 5,967</b>	<b>15.1%</b>	<b>14.6%</b>

Percentage changes that are considered not meaningful are denoted with NM.

(a) Pro forma adjustments are presented as if the acquisition of the 51% interest of Universal Studios Japan occurred on January 1, 2014. Pro forma information does not include adjustments for transaction-related costs, costs related to integration activities, or cost savings or synergies that have been or may be achieved by the combined businesses. The pro forma amounts are primarily based on historical results of operations, adjusted for the allocation of purchase price, and are not necessarily indicative of what our results would have been had we operated Universal Studios Japan since January 1, 2014, nor of our future results.

**Cable Networks Segment Results of Operations**

Year ended December 31 (in millions)	2016	2015	2014	% Change 2015 to 2016	% Change 2014 to 2015
<b>Revenue</b>					
Distribution	\$ 6,078	\$ 5,461	\$ 5,307	11.3%	2.9%
Advertising	3,566	3,435	3,494	3.8	(1.7)
Content licensing and other	820	732	762	11.9	(4.0)
<b>Total revenue</b>	<b>10,464</b>	<b>9,628</b>	<b>9,563</b>	<b>8.7</b>	<b>0.7</b>
<b>Operating costs and expenses</b>					
Programming and production	4,932	4,319	4,241	14.2	1.8
Other operating and administrative	1,310	1,270	1,232	3.2	3.1
Advertising, marketing and promotion	513	540	501	(5.1)	7.7
<b>Total operating costs and expenses</b>	<b>6,755</b>	<b>6,129</b>	<b>5,974</b>	<b>10.2</b>	<b>2.6</b>
<b>Operating income before depreciation and amortization</b>	<b>\$ 3,709</b>	<b>\$ 3,499</b>	<b>\$ 3,589</b>	<b>6.0%</b>	<b>(2.5)%</b>

## Table of Contents

### **Cable Networks Segment – Revenue**

#### Distribution

Distribution revenue is generated from the distribution of our cable network programming to multichannel video providers and is affected by the number of subscribers receiving our cable networks and the fees we charge per subscriber.

Distribution revenue increased in 2016 primarily due to increases in the contractual rates charged under distribution agreements and contract renewals, as well as \$298 million of revenue associated with our broadcast of the 2016 Rio Olympics, which were partially offset by a decline in the number of subscribers at some of our cable networks. Distribution revenue increased in 2015 primarily due to increases in the contractual rates charged under distribution agreements that were partially attributable to the premiere of NASCAR programming on the NBC Sports Network in 2015. The increases in 2015 were partially offset by a decrease in revenue from a decline in the number of subscribers at some of our cable networks and \$177 million of revenue in 2014 associated with our broadcast of the 2014 Sochi Olympics. Excluding revenue associated with our broadcasts of the 2016 Rio Olympics and the 2014 Sochi Olympics, distribution revenue increased 5.8% and 6.5% in 2016 and 2015, respectively.

#### Advertising

Advertising revenue is generated from the sale of advertising units sold on our cable networks and related digital media properties. Advertising revenue is primarily based on the price we charge for each advertising unit, which is generally based on audience ratings, the value of our viewer demographics to advertisers and the number of advertising units we can place in our cable networks' programming schedules. Advertising revenue is affected by the audience ratings of our programming, the strength of the national advertising market and general economic conditions. Audience ratings at our cable networks have declined, which has negatively affected advertising revenue in recent years, and may continue to decline as the number of programming choices, such as subscription video on demand services, continues to increase and as more viewers use DVRs and video on demand services to view our content outside of traditional audience ratings measurement periods.

Advertising revenue increased in 2016 primarily due to \$134 million of revenue associated with our broadcast of the 2016 Rio Olympics. Also, higher prices for advertising units were offset by the impact of declining audience ratings. Advertising revenue decreased in 2015 primarily due to \$80 million of revenue in 2014 associated with our broadcast of the 2014 Sochi Olympics. In addition, the impact of declining audience ratings in 2015 was partially offset by higher prices for, and an increase in the volume of, advertising units sold, as well as increased advertising revenue associated with the broadcast of NASCAR programming. Excluding revenue associated with our broadcasts of the 2016 Rio Olympics and the 2014 Sochi Olympics, advertising revenue decreased slightly in 2016 and increased slightly in 2015 due to the broadcast of NASCAR programming.

#### Content Licensing and Other

Content licensing and other revenue is generated primarily from the licensing of our owned programming in the United States and internationally to cable and broadcast networks and subscription video on demand services, as well as from the sale of our owned programming on DVDs and through digital distribution services such as iTunes. In addition, our cable television studio production operations generate revenue from programming it produces for third-party networks and subscription video on demand services.

Content licensing and other revenue increased in 2016 and decreased in 2015 primarily due to the timing of content provided under our licensing agreements.

## Table of Contents

In 2016, 2015 and 2014, 14%, 13% and 12%, respectively, of our Cable Networks segment revenue was generated from our Cable Communications segment. These amounts are eliminated in Comcast's consolidated financial statements but are included in the amounts presented above.

### **Cable Networks Segment – Operating Costs and Expenses**

#### Programming and Production Costs

Programming and production costs include the amortization of owned and acquired programming, sports rights, direct production costs, residual and participation payments, production overhead, costs associated with the distribution of our programming to third-party networks and other distribution platforms, and on-air talent costs.

Programming and production costs increased in 2016 primarily due to our broadcast of the 2016 Rio Olympics, as well as an increase in other sports programming rights costs. Programming and production costs increased in 2015 primarily due to our continued investment in programming, including the premiere of NASCAR programming and other sports programming rights costs. These increases in 2015 were partially offset by costs in 2014 associated with our broadcast of the 2014 Sochi Olympics.

#### Other Operating and Administrative Costs and Expenses

Other operating and administrative costs and expenses include salaries, employee benefits, rent and other overhead expenses, and these costs increased in 2016 and 2015 primarily due to increases in employee-related costs.

#### Advertising, Marketing and Promotion Expenses

Advertising, marketing and promotion expenses consist primarily of the costs associated with promoting programming on our cable networks and related digital media properties. These expenses decreased in 2016 and increased in 2015 primarily due to increased spending on marketing in 2015 related to the launch of new programming on our cable networks.

### **Broadcast Television Segment Results of Operations**

Year ended December 31 (in millions)	2016	2015	2014	% Change 2015 to 2016	% Change 2014 to 2015
<b>Revenue</b>					
Advertising	\$ 6,834	\$ 5,747	\$ 5,888	18.9%	(2.4)%
Content licensing	1,899	1,784	1,569	6.4	13.7
Distribution and other	1,414	999	1,085	41.5	(7.8)
<b>Total revenue</b>	<b>10,147</b>	<b>8,530</b>	<b>8,542</b>	<b>19.0</b>	<b>(0.1)</b>
<b>Operating costs and expenses</b>					
Programming and production	6,984	5,950	6,127	17.4	(2.9)
Other operating and administrative	1,381	1,276	1,199	8.3	6.4
Advertising, marketing and promotion	462	524	482	(11.9)	8.9
<b>Total operating costs and expenses</b>	<b>8,827</b>	<b>7,750</b>	<b>7,808</b>	<b>13.9</b>	<b>(0.7)</b>
<b>Operating income before depreciation and amortization</b>	<b>\$ 1,320</b>	<b>\$ 780</b>	<b>\$ 734</b>	<b>69.1%</b>	<b>6.3%</b>

## Table of Contents

### **Broadcast Television Segment – Revenue**

#### Advertising

Advertising revenue is generated from the sale of advertising units sold on our broadcast networks, owned local television stations and related digital media properties. Advertising revenue is primarily based on the price we charge for each advertising unit, which is generally based on audience ratings and the value of our viewer demographics to advertisers, and the number of advertising units we can place in our broadcast networks' and owned local television stations' programming schedules. Advertising revenue is affected by the strength of the national and local advertising markets, general economic conditions, cyclicity related to political campaigns and issue-oriented advertising, and the success and ratings of our programming.

Advertising revenue increased in 2016 primarily due to \$1.0 billion of revenue associated with our broadcast of the 2016 Rio Olympics. Advertising revenue also increased due to higher prices for advertising units sold, the premiere of *Thursday Night Football* and higher political advertising, which was partially offset by revenue in 2015 associated with our broadcast of the 2015 Super Bowl and a decline in audience ratings. Advertising revenue decreased in 2015 primarily due to \$730 million of revenue in 2014 associated with our broadcast of the 2014 Sochi Olympics, which was partially offset by \$376 million of revenue in 2015 associated with our broadcast of the 2015 Super Bowl. Excluding revenue associated with our broadcasts of the 2016 Rio Olympics and the 2015 Super Bowl, revenue increased 7.7% in 2016. Excluding revenue associated with our broadcasts of the 2015 Super Bowl and the 2014 Sochi Olympics, revenue increased 4.1% in 2015 primarily due to higher prices for, and an increase in the volume of, advertising units sold.

#### Content Licensing

Content licensing revenue is generated from the licensing of our owned programming in the United States and internationally to various distribution platforms, including to cable and broadcast networks, as well as to subscription video on demand services. In addition, our broadcast television studio production operations develop and produce original content that they license to broadcast networks, cable networks and local broadcast television stations owned by us and third parties, as well as to subscription video on demand services. The production and distribution costs related to our owned programming generally exceed the revenue generated from the initial network license, which means the subsequent licensing of our owned programming series following the initial network license is critical to their financial success.

Content licensing revenue increased in 2016 and 2015 primarily due to the timing of content provided under our licensing agreements.

#### Distribution and Other

We generate distribution and other revenue primarily from fees for retransmission consent of our owned local broadcast television stations and associated fees received from NBC-affiliated local broadcast television stations, as well as from the sale of our owned programming on DVDs and through digital distribution services. The sale of our owned programming is driven primarily by the popularity of our broadcast networks and programming series and therefore fluctuates based on consumer spending and acceptance. Distribution and other revenue also includes distribution revenue associated with our periodic broadcasts of the Olympic Games.

Distribution and other revenue increased in 2016 primarily due to increases in fees recognized under our retransmission consent agreements, as well as \$140 million of distribution revenue associated with our broadcast of the 2016 Rio Olympics. Distribution and other revenue decreased in 2015 primarily due to \$116 million of distribution revenue in 2014 that was associated with our broadcast of the 2014 Sochi Olympics. The decrease was partially offset by an increase in fees recognized under our retransmission consent agreements, as well as new syndication agreements entered into in 2015.

## Table of Contents

### **Broadcast Television Segment – Operating Costs and Expenses**

#### Programming and Production Costs

Programming and production costs relate to content originating on our broadcast networks and owned local broadcast television stations, as well as owned content that is licensed to third parties. These costs include the amortization of owned and acquired programming costs, sports rights, direct production costs, residual and participation payments, production overhead, costs associated with the distribution of our programming to third-party networks and other distribution platforms, and on-air talent costs.

Programming and production costs increased in 2016 primarily due to our broadcast of the 2016 Rio Olympics, as well as our broadcast of *Thursday Night Football*, which were partially offset by costs in 2015 associated with our broadcast of the 2015 Super Bowl. Programming and production costs decreased in 2015 primarily due to costs in 2014 associated with our broadcast of the 2014 Sochi Olympics, which was partially offset by costs associated with our broadcast of the 2015 Super Bowl, the timing of content provided under our licensing agreements and higher studio production costs.

#### Other Operating and Administrative Costs and Expenses

Other operating and administrative costs and expenses include salaries, employee benefits, rent and other overhead expenses, and these costs increased in 2016 and 2015 primarily due to increases in employee-related costs.

#### Advertising, Marketing and Promotion Expenses

Advertising, marketing and promotion expenses consist primarily of the costs associated with promoting our owned and acquired television programming, as well as the marketing of DVDs and costs associated with our related digital media properties. These expenses decreased in 2016 and increased in 2015 primarily due to increased spending on marketing in 2015 associated with our NBC primetime lineup.

### **Filmed Entertainment Segment Results of Operations**

Year ended December 31 (in millions)	2016	2015	2014	% Change 2015 to 2016	% Change 2014 to 2015
<b>Revenue</b>					
Theatrical	\$ 1,560	\$ 2,829	\$ 1,101	(44.9)%	156.9%
Content licensing	2,563	1,923	1,792	33.3	7.3
Home entertainment	1,254	1,801	1,457	(30.4)	23.6
Other	983	734	658	34.1	11.5
<b>Total revenue</b>	<b>6,360</b>	<b>7,287</b>	<b>5,008</b>	<b>(12.7)</b>	<b>45.5</b>
<b>Operating costs and expenses</b>					
Programming and production	2,962	3,488	2,331	(15.1)	49.6
Other operating and administrative	1,101	872	849	26.3	2.8
Advertising, marketing and promotion	1,600	1,693	1,117	(5.5)	51.7
<b>Total operating costs and expenses</b>	<b>5,663</b>	<b>6,053</b>	<b>4,297</b>	<b>(6.4)</b>	<b>40.9</b>
<b>Operating income before depreciation and amortization</b>	<b>\$ 697</b>	<b>\$ 1,234</b>	<b>\$ 711</b>	<b>(43.5)%</b>	<b>73.5%</b>

### **Filmed Entertainment Segment – Revenue**

#### Theatrical

Theatrical revenue is generated from the worldwide theatrical release of our owned and acquired films for exhibition in movie theaters and is significantly affected by the timing of each release and the number of films

## Table of Contents

we distribute, as well as their acceptance by audiences. Theatrical revenue is also affected by the number of exhibition screens, ticket prices, the percentage of ticket sale retention by the exhibitors and the popularity of competing films at the time our films are released. The success of a film in movie theaters is a significant factor in determining the revenue a film is likely to generate in succeeding distribution platforms.

Theatrical revenue decreased in 2016 and increased in 2015 primarily due to the strong performance of our larger 2015 film slate, including *Furious 7*, *Jurassic World* and *Minions*. The decrease in 2016 was partially offset by the strong performance of *The Secret Life of Pets* and *Sing* in 2016.

### Content Licensing

Content licensing revenue is generated primarily from the licensing of our owned and acquired films to cable, broadcast and premium networks, as well as to subscription video on demand services.

Content licensing revenue increased in 2016 and 2015 primarily due to the timing of when content was made available under licensing agreements. The increase in 2016 was partially due to the timing of when content related to our 2015 film slate was made available under licensing agreements.

### Home Entertainment

Home entertainment revenue is generated from the sale of our owned and acquired films on DVDs to retail stores, rental kiosks and subscription by mail services, and in digital formats. Home entertainment revenue is significantly affected by the timing and number of our releases and their acceptance by consumers. Release dates are determined by several factors, including the timing of the exhibition of a film in movie theaters, holiday periods and the timing of competitive releases. The overall DVD market continues to experience declines due to the maturation of the standard-definition DVD format, increasing shifts in consumer behavior toward digital distribution services, and subscription rental services, all of which generate less revenue per transaction than DVD sales, as well as due to piracy.

Home entertainment revenue decreased in 2016 and increased in 2015 primarily due to the strong performance of our 2015 releases, including *Minions* and *Jurassic World*. The decrease in 2016 was partially offset by the home entertainment sales of *Jason Bourne* and *The Secret Life of Pets*.

### Other

We also generate revenue from producing and licensing live stage plays, from distributing filmed entertainment produced by third parties, from Fandango, our movie ticketing and entertainment business, and from the sale of consumer products.

Other revenue increased in 2016 and 2015 primarily due to increases in revenue generated from Fandango.

## **Filmed Entertainment Segment – Operating Costs and Expenses**

### Programming and Production Costs

Programming and production costs include the amortization of capitalized film production and acquisition costs, residual and participation payments, and distribution expenses. Residual payments represent amounts payable to certain of our employees who are represented by labor unions or guilds, including freelance and temporary employees, and are based on post-theatrical revenue. Participation payments are primarily based on film performance and represent contingent consideration payable to creative talent, third parties that have entered into cofinancing agreements with us and other parties involved in the production of a film. The costs associated with producing films have generally increased in recent years and may continue to increase in the future.

## Table of Contents

Programming and production costs decreased in 2016 and increased in 2015 primarily due to higher amortization of film production costs in 2015 associated with our larger 2015 film slate, which included *Furious 7*, *Jurassic World* and *Minions*.

### Other Operating and Administrative Costs and Expenses

Other operating and administrative costs and expenses include salaries, employee benefits, rent and other overhead expenses.

Other operating and administrative expenses increased in 2016 primarily due to costs attributable to DreamWorks Animation, including \$61 million of severance costs. Other operating and administrative expenses increased slightly in 2015 due to increased expenses associated with our larger film slate.

### Advertising, Marketing and Promotion Expenses

Advertising, marketing and promotion expenses consist primarily of expenses associated with advertising for our theatrical releases and the marketing of our films on DVDs and in digital formats. We incur significant marketing expenses before and throughout the release of a film in movie theaters. As a result, we typically incur losses on a film prior to and during the film's exhibition in movie theaters and may not realize profits, if any, until the film generates home entertainment and content licensing revenue. The costs associated with marketing films have generally increased in recent years and may continue to increase in the future.

Advertising, marketing and promotion expenses decreased in 2016 and increased in 2015 primarily due to higher promotional costs associated with our larger 2015 film slate. The decrease in 2016 was partially offset due to advertising in 2016 for our domestic and international film slate. Advertising, marketing and promotion expenses also increased in 2015 due to increased advertising expenses associated with Fandango.

## Theme Parks Segment Actual and Pro Forma Results of Operations

Year ended December 31 (in millions)	2016	2015			% Change 2015 to 2016	
		Actual	Actual	Pro Forma Adjustments	Pro Forma Combined	Actual
<b>Revenue</b>	<b>\$ 4,946</b>	<b>\$ 3,339</b>	<b>\$ 1,052</b>	<b>\$ 4,391</b>	<b>48.2%</b>	<b>12.7%</b>
<b>Operating costs and expenses</b>	<b>2,756</b>	<b>1,875</b>	<b>564</b>	<b>2,439</b>	<b>47.0</b>	<b>13.0</b>
<b>Operating income before depreciation and amortization</b>	<b>\$ 2,190</b>	<b>\$ 1,464</b>	<b>\$ 488</b>	<b>\$ 1,952</b>	<b>49.6%</b>	<b>12.2%</b>

Year ended December 31 (in millions)	2015			2014			% Change 2014 to 2015	
	Actual	Pro Forma Adjustments	Pro Forma Combined	Actual	Pro Forma Adjustments	Pro Forma Combined	Actual	Pro Forma Combined
<b>Revenue</b>	<b>\$ 3,339</b>	<b>\$ 1,052</b>	<b>\$ 4,391</b>	<b>\$ 2,623</b>	<b>\$ 1,085</b>	<b>\$ 3,708</b>	<b>27.3%</b>	<b>18.4%</b>
<b>Operating costs and expenses</b>	<b>1,875</b>	<b>564</b>	<b>2,439</b>	<b>1,527</b>	<b>634</b>	<b>2,161</b>	<b>22.8</b>	<b>12.8</b>
<b>Operating income before depreciation and amortization</b>	<b>\$ 1,464</b>	<b>\$ 488</b>	<b>\$ 1,952</b>	<b>\$ 1,096</b>	<b>\$ 451</b>	<b>\$ 1,547</b>	<b>33.5%</b>	<b>26.2%</b>

### Theme Parks Segment – Revenue

Our Theme Parks segment revenue is generated primarily from ticket sales and guest spending at our Universal theme parks. Guest spending includes in-park spending on food, beverages and merchandise. Guest attendance at our theme parks and guest spending depend heavily on the general environment for travel and tourism, including consumer spending on travel and other recreational activities.

## Table of Contents

Theme Parks segment revenue increased in 2016 compared to the pro forma combined revenue in 2015 primarily due to increases in guest spending and higher guest attendance driven by the successful opening of *The Wizarding World of Harry Potter™* attraction in Hollywood in April 2016, as well as the positive impact of foreign currency translation due to the strengthening of the Japanese yen. The strengthening of the Japanese yen accounted for approximately one-third of the increase in revenue for 2016.

Theme Parks segment pro forma combined revenue increased in 2015 compared to the pro forma combined revenue in 2014 primarily due to higher guest attendance and increases in guest spending at our Universal theme parks. The increase in 2015 was primarily due to the success of our attractions, including *The Wizarding World of Harry Potter™ — Diagon Alley™* in Orlando, which opened in 2014, and the *Fast & Furious™ — Supercharged™* studio tour and *The Simpson's Springfield* attraction in Hollywood, both of which opened in 2015.

### **Theme Parks Segment – Operating Costs and Expenses**

Our Theme Parks segment operating costs and expenses consist primarily of theme park operations, including repairs and maintenance and related administrative expenses; food, beverage and merchandise costs; labor costs; and sales and marketing costs.

Theme Parks segment operating costs and expenses increased in 2016 compared to the pro forma combined operating costs and expenses in 2015 primarily due to additional costs associated with newer attractions, such as *The Wizarding World of Harry Potter™* attraction in Hollywood and *Skull Island: Reign of Kong™* attraction in Orlando, as well as the impact of foreign currency translation due to the strengthening on the Japanese yen.

Theme Parks segment pro forma combined operating costs and expenses in 2015 increased compared to the pro forma combined operating costs and expenses in 2014 primarily due to additional costs associated with newer attractions, such as the *Fast & Furious™ — Supercharged™* studio tour in Hollywood, and increases in food, beverage and merchandise costs associated with higher guest attendance.

The strengthening of the Japanese yen accounted for approximately one-third of the increase in operating income before depreciation and amortization in 2016.

### **NBCUniversal Headquarters, Other and Eliminations**

Headquarters and Other operating costs and expenses incurred by our NBCUniversal businesses include overhead, personnel costs and costs associated with corporate initiatives. Operating costs and expenses increased in 2016 and 2015 primarily due to higher employee-related costs.

### **Corporate and Other Results of Operations**

Year ended December 31 (in millions)	2016	2015	2014	% Change 2015 to 2016	% Change 2014 to 2015
<b>Revenue</b>	\$ 750	\$ 713	\$ 683	5.1%	4.4%
Operating costs and expenses	1,624	1,528	1,446	6.2	5.7
<b>Operating loss before depreciation and amortization</b>	\$ (874)	\$ (815)	\$ (763)	(7.1)%	(6.9)%

### **Corporate and Other – Revenue**

Other revenue primarily relates to Comcast Spectacor, which owns the Philadelphia Flyers and the Wells Fargo Center arena in Philadelphia, Pennsylvania and operates arena management-related businesses.

## Table of Contents

Other revenue increased in 2016 primarily due to increases in revenue from several of our Comcast Spectacor businesses. Other revenue increased in 2015 primarily due to an increase in revenue from food and other services associated with new contracts entered into by one of our Comcast Spectacor businesses.

### **Corporate and Other – Operating Costs and Expenses**

Corporate and Other operating costs and expenses primarily include overhead, personnel costs, the costs of corporate initiatives and branding, and operating costs and expenses associated with Comcast Spectacor.

Corporate and Other operating costs and expenses increased in 2016 due to an increase in expenses related to corporate activities and initiatives, including expenses associated with our anticipated wireless phone service offering. Corporate and Other operating costs and expenses increased in 2015 due to an increase in expenses related to corporate initiatives and an increase in operating costs and expenses at Comcast Spectacor that was primarily associated with new contracts entered into by one of its businesses. In addition, Corporate and Other operating costs and expenses in 2015 and 2014 included \$178 million and \$237 million, respectively, of transaction-related costs associated with the Time Warner Cable merger and related divestiture transactions.

### **Consolidated Other Income (Expense) Items, Net**

Year ended December 31 (in millions)	2016	2015	2014
Interest expense	\$ (2,942)	\$ (2,702)	\$ (2,617)
Investment income (loss), net	213	81	296
Equity in net income (losses) of investees, net	(104)	(325)	97
Other income (expense), net	327	320	(215)
<b>Total</b>	<b>\$ (2,506)</b>	<b>\$ (2,626)</b>	<b>\$ (2,439)</b>

### **Interest Expense**

Interest expense increased in 2016 primarily due to higher levels of debt outstanding, including the Universal Studios Japan term loans. Interest expense increased in 2015 primarily due to higher levels of debt outstanding and \$47 million of additional interest expense associated with the early redemption in June 2015 of our \$750 million aggregate principal amount of 5.85% senior notes due November 2015 and our \$1.0 billion aggregate principal amount of 5.90% senior notes due March 2016.

### **Investment Income (Loss), Net**

The change in investment income (loss), net in 2016 was primarily due to an increase in income of certain investments and gains recorded on the sale of certain investments. The change in investment income (loss), net in 2015 was primarily due to a \$154 million gain related to the sale of our shares of ARRIS Group, Inc. common stock in 2014. The components of investment income (loss), net are presented in a table in Note 7 to Comcast's consolidated financial statements.

### **Equity in Net Income (Losses) of Investees, Net**

The changes in equity in net income (losses) of investees, net in 2016 and 2015 were primarily due to an impairment charge related to goodwill recorded by The Weather Channel in 2015. We recorded expenses of \$333 million that represented NBCUniversal's proportionate share of the impairment charge. In addition, the changes in 2016 and 2015 were also due to increases in our proportionate share of losses at Hulu, LLC, which were driven by Hulu's higher programming and marketing costs. In 2016, 2015 and 2014, we recognized our proportionate share of losses at Hulu of \$168 million, \$106 million and \$20 million respectively. The change in 2016 was also due to our proportionate share of losses at Atairos Group, Inc., which commenced operations in 2016.

## Table of Contents

### **Other Income (Expense), Net**

Other income (expense), net for 2016 included \$225 million recognized in connection with the settlement of amounts owed to us under an agency agreement that had provided for, among other things, Verizon Wireless' sale of our cable services and \$108 million related to the sale of our investment in The Weather Channel's product and technology business to IBM.

Other income (expense), net for 2015 included gains of \$335 million on the sales of a business and an investment, \$240 million recorded on the settlement of a contingent consideration liability with General Electric Company related to the acquisition of NBCUniversal, and \$43 million related to an equity method investment. These gains were partially offset by \$236 million of expenses related to fair value adjustments to a contractual obligation.

Other income (expense), net for 2014 included a \$27 million favorable settlement of a contingency related to the AT&T Broadband transaction in 2002, which was more than offset by \$208 million of expenses related to fair value adjustments to a contractual obligation and \$35 million of expenses related to an indemnification receivable associated with an adjustment to our accruals for uncertain tax positions.

### **Consolidated Income Tax Expense**

Income tax expense reflects federal and state income taxes and adjustments associated with uncertain tax positions. Our effective income tax rate in 2016, 2015 and 2014 was 37.0%, 37.1% and 31.1%, respectively.

In 2014, we reduced our accruals for uncertain tax positions and the related accrued interest on these tax positions and, as a result, our income tax expense decreased by \$759 million. See Note 14 to Comcast's consolidated financial statements for additional information on the changes in our accruals for uncertain tax positions and related interest on these tax positions.

We expect our 2017 annual effective tax rate to be in the range of 35% to 37%, absent changes in tax laws or significant changes in uncertain tax positions. The expected annual effective tax rate includes the impact of the adoption of the new accounting guidance related to share-based compensation (see Note 3 to Comcast's consolidated financial statements). If significant tax legislation is enacted in 2017 that includes a change to the federal statutory rate, this could significantly impact our deferred income taxes. For example, using information as of December 31, 2016, for each 1% change in the federal statutory rate, our deferred income tax liability would change by \$850 million, which would primarily result in a corresponding change to income tax expense.

### **Consolidated Net (Income) Loss Attributable to Noncontrolling Interests and Redeemable Subsidiary Preferred Stock**

The increases in net income attributable to noncontrolling interests and redeemable subsidiary preferred stock in 2016 and 2015 were primarily due to NBCUniversal's acquisition of the 51% interest in Universal Studios Japan.

### **Liquidity and Capital Resources**

Our businesses generate significant cash flows from operating activities. We believe that we will be able to continue to meet our current and long-term liquidity and capital requirements, including fixed charges, through our cash flows from operating activities; existing cash, cash equivalents and investments; available borrowings under our existing credit facilities; and our ability to obtain future external financing. We anticipate that we will continue to use a substantial portion of our cash flows in repaying our debt obligations, funding our capital expenditures, investing in business opportunities and returning capital to shareholders.

## Table of Contents

We also maintain significant availability under our lines of credit and our commercial paper programs to meet our short-term liquidity requirements. Our commercial paper programs provide a lower-cost source of borrowing to fund our short-term working capital requirements. See Note 10 and Note 19 to Comcast's consolidated financial statements for additional information on the Comcast and NBCUniversal Enterprise revolving credit facilities and the related guarantees.

As of December 31, 2016, amounts available under our consolidated credit facilities, net of amounts outstanding under our commercial paper programs and outstanding letters of credit, totaled \$5.5 billion, which included \$460 million available under the NBCUniversal Enterprise revolving credit facility.

We, NBCUniversal and Comcast Cable Communications, LLC are subject to the covenants and restrictions set forth in the indentures governing our public debt securities and in the credit agreements governing the Comcast revolving credit facility. The only financial covenant is in the credit facility and pertains to leverage, which is the ratio of debt to operating income before depreciation and amortization, as defined in the credit facility. We test for compliance with this financial covenant on an ongoing basis. As of December 31, 2016, we met this financial covenant by a significant margin. We do not expect to have to reduce debt or improve operating results in order to continue to comply with this financial covenant. In addition, the Universal Studios Japan term loans contain certain financial covenants. As of December 31, 2016, Universal Studios Japan was in compliance with all of these covenants.

## **Operating Activities**

### Components of Net Cash Provided by Operating Activities

Year ended December 31 (in millions)	2016	2015	2014
Operating income	\$ 16,859	\$ 15,998	\$ 14,904
Depreciation and amortization	9,558	8,680	8,019
Operating income before depreciation and amortization	26,417	24,678	22,923
Noncash share-based compensation	640	567	513
Changes in operating assets and liabilities	(1,782)	(267)	(357)
Cash basis operating income	25,275	24,978	23,079
Payments of interest	(2,565)	(2,443)	(2,389)
Payments of income taxes	(3,693)	(3,726)	(3,668)
Proceeds from investments and other	456	251	190
Excess tax benefits under share-based compensation	(233)	(282)	(267)
Net cash provided by operating activities	\$ 19,240	\$ 18,778	\$ 16,945

The variance in changes in operating assets and liabilities in 2016 compared to 2015 was primarily due to the timing of film and television production spending and related costs, net of amortization, including certain sports programming obligations; the recognition of deferred revenue associated with the broadcast of the 2016 Rio Olympics; an increase in certain benefit payments; and the payment of a tax receivable agreement that DreamWorks Animation entered into with one of its former stockholders prior to our acquisition. The variance in changes in operating assets and liabilities in 2015 compared to 2014 was primarily related to the timing of film and television production spending and related costs, net of amortization; the timing of payments related to our accounts payable and accrued expenses related to trade creditors; and increases in deferred revenue associated with our Olympics broadcasts, which were partially offset by the timing of collections on our receivables.

The increases in interest payments in 2016 and 2015 were primarily due to higher levels of debt outstanding.

## Table of Contents

The decrease in income tax payments in 2016 was primarily due to taxable losses in 2016 related to the sale of certain investments as well as taxable gains in 2015 related to the sale of a business and investments partially offset by higher taxable income from operations. The increase in income tax payments in 2015 was primarily due to higher taxable income from operations offset by the timing of certain tax deductions. We expect income tax payments to increase in 2017 primarily due to higher taxable income from operations.

### **Investing Activities**

Net cash used in investing activities in 2016 consisted primarily of cash paid for capital expenditures, acquisitions, deposits, purchases of investments and intangible assets. Net cash used in investing activities in 2015 consisted primarily of cash paid for capital expenditures, acquisitions, intangible assets and purchases of investments, which was partially offset by proceeds from the sales of businesses and investments. Net cash used in investing activities in 2014 consisted primarily of cash paid for capital expenditures and intangible assets.

#### Capital Expenditures

Our most significant recurring investing activity has been capital expenditures in our Cable Communications segment, and we expect that this will continue in the future. The table below summarizes the capital expenditures we incurred in our Cable Communications segment in 2016, 2015 and 2014.

Year ended December 31 (in millions)	2016	2015	2014
Customer premise equipment	\$ 3,665	\$ 3,698	\$ 3,397
Scalable infrastructure	1,827	1,539	1,375
Line extensions	1,208	886	673
Support capital	896	917	711
<b>Total</b>	<b>\$ 7,596</b>	<b>\$ 7,040</b>	<b>\$ 6,156</b>

Cable Communications capital expenditures increased in 2016 and 2015 primarily due to increased investment in line extensions and increased spending in scalable infrastructure to increase network capacity, as well as continued spending on customer premise equipment related to the deployment of our X1 platform and wireless gateways.

Capital expenditures in our NBCUniversal segments increased 4.8% to \$1.5 billion in 2016 and 13.5% to \$1.4 billion in 2015 primarily due to continued investment in our Universal theme parks, including Universal Studios Japan and a purchase of land in 2015.

Our capital expenditures for 2017 are focused on continued investment in scalable infrastructure to increase network capacity; increased investment in line extensions primarily for the expansion of business services; and the continued deployment of wireless gateways, our X1 platform, and cloud DVR technology. In addition, we expect to continue to invest in existing and new attractions at our Universal theme parks. Capital expenditures for subsequent years will depend on numerous factors, including acquisitions, competition, changes in technology, regulatory changes, the timing and rate of deployment of new services, the capacity required for existing services, and the timing of new attractions at our theme parks. We are developing a Universal theme park in Beijing, China, and we expect to continue to develop this park throughout 2017.

#### Cash Paid for Intangible Assets

In 2016, 2015 and 2014, cash paid for intangible assets consisted primarily of expenditures for software in our Cable Communications segment.

#### Acquisitions and Construction of Real Estate Properties

Acquisitions and construction of real estate properties in 2016 and 2015 primarily included our investment in the construction of the Comcast Technology Center in Philadelphia, Pennsylvania.

## Table of Contents

### Acquisitions, Net of Cash Acquired

In August 2016, we acquired all of the outstanding stock of DreamWorks Animation. In November 2015, NBCUniversal acquired a 51% interest in Universal Studios Japan.

### Proceeds from Sales of Businesses and Investments

Proceeds from sales of businesses and investments in 2016 were primarily related to the sale of our investment in The Weather Channel's product and technology business to IBM. Proceeds from sales of businesses and investments in 2015 were primarily related to the sale of our investment in TV One, LLC and the sale of a business, CTI Towers Assets I, LLC. Proceeds from sales of businesses and investments in 2014 were primarily related to the sale of our investment in Arris Group and the sale of equity securities following the settlement of certain of our prepaid forward sale agreements.

### Purchases of Investments

Purchases of investments in 2016 were primarily related to capital contributions to Atairos and NBCUniversal's additional investment in BuzzFeed, Inc. Purchases of investments in 2015 were primarily related to NBCUniversal's investments in Vox Media, Inc. and BuzzFeed. Purchases of investments in 2014 were not significant.

### Financing Activities

Net cash provided by financing activities in 2016 consisted primarily of proceeds from new borrowings, which were partially offset by repurchases of our common stock, repayments of debt, dividend payments and our purchase of the remaining noncontrolling interest in Comcast Spectacor. Net cash used in financing activities in 2015 and 2014 consisted primarily of repurchases of our common stock, repayments of debt and dividend payments, which were partially offset by proceeds from new borrowings. Proceeds from borrowings fluctuate from year to year based on the amounts paid to fund acquisitions and debt repayments.

We have made, and may from time to time in the future make, optional repayments on our debt obligations, which may include repurchases of our outstanding public notes and debentures, depending on various factors, such as market conditions. See Note 10 to Comcast's consolidated financial statements for additional information on our financing activities, including details of our debt repayments and borrowings.

### Share Repurchases and Dividends

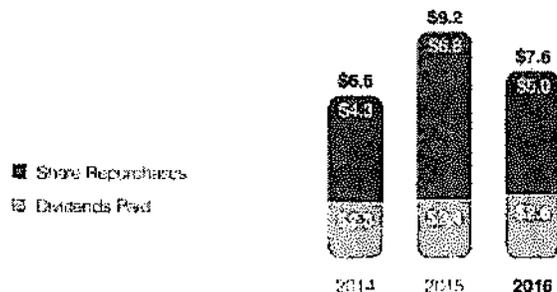
In 2016, we repurchased a total of 81 million shares of our Class A common stock for \$5.0 billion. Effective January 1, 2017, our Board of Directors increased our share repurchase program authorization to a total of \$12 billion, which does not have an expiration date. Under the authorization, we may repurchase shares in the open market or in private transactions. We expect to repurchase \$5.0 billion of our Class A common stock during 2017, subject to market conditions.

Our Board of Directors declared quarterly dividends totaling \$2.7 billion in 2016. We paid dividends of \$2.6 billion in 2016. In January 2017, our Board of Directors approved a 15% increase in our dividend to \$1.26 per share on an annualized, pre-split basis, or \$0.63 per share on an annualized, post-split basis. In addition, the Board of Directors approved our first quarter dividend of \$0.1575 a share on a post-split basis to be paid in April 2017. We expect to continue to pay quarterly dividends, although each dividend is subject to approval by our Board of Directors.

## Table of Contents

The table below sets forth information on our share repurchases and dividends paid in 2016, 2015 and 2014.

### Share Repurchases and Dividends Paid (in millions)



## Contractual Obligations

As of December 31, 2016 (in millions)	Payment Due by Period				
	Total	Year 1	Years 2-3	Years 4-5	More than 5
Debt obligations <sup>(a)</sup>	\$ 61,133	\$ 5,454	\$ 6,604	\$ 8,189	\$ 40,886
Capital lease obligations	238	29	65	71	73
Operating lease obligations	4,007	517	918	699	1,873
Purchase obligations <sup>(b)</sup>	51,649	9,978	11,404	8,538	21,729
Other long-term liabilities reflected on the balance sheet <sup>(c)</sup>	5,928	336	1,262	2,316	2,014
<b>Total<sup>(d)(e)</sup></b>	<b>\$ 122,955</b>	<b>\$ 16,314</b>	<b>\$ 20,253</b>	<b>\$ 19,813</b>	<b>\$ 66,575</b>

Refer to Note 10 and Note 16 to Comcast's consolidated financial statements.

(a) Excludes interest payments.

(b) Purchase obligations consist of agreements to purchase goods and services that are legally binding on us and specify all significant terms, including fixed or minimum quantities to be purchased and price provisions. Our purchase obligations related to our Cable Communications segment and other activities include programming contracts with cable networks and local broadcast television stations; contracts with customer premise equipment manufacturers; communications vendors and multichannel video providers for which we provide advertising sales representation; contracts to acquire handsets and other equipment; and other contracts entered into in the normal course of business. Cable Communications programming contracts in the table above include amounts payable under fixed or minimum guaranteed commitments and do not represent the total fees that are expected to be paid under programming contracts, which we expect to be significantly higher because these contracts are generally based on the number of subscribers receiving the programming. Our purchase obligations related to our NBCUniversal segments consist primarily of commitments to acquire film and television programming, including U.S. broadcast rights to future Olympic Games through 2032, *Sunday Night Football* through the 2022-23 season, including the Super Bowl in 2018 and 2021, *Thursday Night Football* through the 2017-18 season, NHL games through the 2020-21 season, Spanish-language U.S. broadcast rights to FIFA World Cup games through 2022, U.S. broadcast rights to English Premier League soccer games through the 2021-22 season, certain PGA TOUR and other golf events through 2030, and certain NASCAR events through 2024, as well as obligations under various creative talent agreements, including obligations to actors, producers and television personalities, and various other television commitments. Purchase obligations do not include contracts with immaterial future commitments.

(c) Other long-term liabilities reflected on the balance sheet consist primarily of subsidiary preferred shares; deferred compensation obligations; and postretirement, pension and postemployment benefit obligations. A contractual obligation with a carrying value of \$1.1 billion is not included in the table above because it is uncertain if the arrangement will be settled. The contractual obligation involves an interest held by a third party in the revenue of certain theme parks. The arrangement provides the counterparty with the right to periodic payments associated with current period revenue and, beginning in June 2017, the option to require NBCUniversal to purchase the interest for cash in an amount based on a contractual formula. The contractual formula is based on an average of specified historical theme park revenue at the time of exercise, which amount could be significantly higher than the carrying value. If the option had been exercisable as of December 31, 2016, the estimated value of the contractual obligation would have been approximately \$1.4 billion, based on inputs to the contractual formula as of that date. See Note 16 to Comcast's consolidated financial statements for additional information related to this arrangement. Reserves for uncertain tax positions of \$1.1 billion are not included in the table above because it is uncertain if or when these reserves will become payable. Payments of \$2.4 billion of participations and residuals are also not included in the table above because we cannot make a reliable estimate of the period in which these obligations will be settled.

(d) Our contractual obligations do not include our commitment to invest up to \$4 billion at any one time as an investor in Atairus due to our inability to estimate the timing of this funding. As of December 31, 2016, our remaining commitment is \$2.4 billion based on the capital

## Table of Contents

calls received as of that date (see Note 7 to Comcast's consolidated financial statements). In addition, our contractual obligations do not include any future expenditures related to the construction and development of the proposed Universal Studios theme park in Beijing, China or the Comcast Technology Center, as we do not currently have any obligation to fund either initiative.

(e) Total contractual obligations are made up of the following components.

(in millions)	
Liabilities recorded on the balance sheet	\$ 68,694
Commitments not recorded on the balance sheet	54,261
<b>Total</b>	<b>\$ 122,955</b>

## Off-Balance Sheet Arrangements

As of December 31, 2016, we did not have any material off-balance sheet arrangements that are reasonably likely to have a current or future effect on our financial condition, results of operations, liquidity, capital expenditures or capital resources.

## Recent Accounting Pronouncements

See Note 3 to each of Comcast's and NBCUniversal's consolidated financial statements for additional information related to recent accounting pronouncements.

## Critical Accounting Judgments and Estimates

The preparation of our consolidated financial statements requires us to make estimates that affect the reported amounts of assets, liabilities, revenue and expenses, and the related disclosure of contingent assets and contingent liabilities. We base our judgments on our historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making estimates about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe our judgments and related estimates associated with the valuation and impairment testing of our cable franchise rights and the accounting for film and television costs are critical in the preparation of our consolidated financial statements. Management has discussed the development and selection of these critical accounting judgments and estimates with the Audit Committee of our Board of Directors, and the Audit Committee has reviewed our disclosures relating to them, which are presented below. See Notes 9 and 6 to Comcast's consolidated financial statements for a discussion of our accounting policies with respect to these items.

### **Valuation and Impairment Testing of Cable Franchise Rights**

Our largest asset, our cable franchise rights, results from agreements we have with state and local governments that allow us to construct and operate a cable business within a specified geographic area. The value of a franchise is derived from the economic benefits we receive from the right to solicit new customers and to market additional services, such as advanced video services and high-speed Internet and voice services, in a particular service area. The amounts we record for cable franchise rights are primarily a result of cable system acquisitions. Typically when we acquire a cable system, the most significant asset we record is the value of the cable franchise rights. Often these cable system acquisitions include multiple franchise areas. We currently serve approximately 6,400 franchise areas in the United States.

We have concluded that our cable franchise rights have an indefinite useful life since there are no legal, regulatory, contractual, competitive, economic or other factors which limit the period over which these rights will contribute to our cash flows. Accordingly, we do not amortize our cable franchise rights but assess the carrying value of our cable franchise rights annually, or more frequently whenever events or changes in circumstances indicate that the carrying amount may exceed the fair value ("impairment testing").

## Table of Contents

For the purpose of our impairment testing, we have grouped the recorded values of our various cable franchise rights into our three Cable Communications divisions or units of account. We evaluate the unit of account periodically to ensure our impairment testing is performed at an appropriate level.

The annual impairment test for indefinite-lived intangibles allows for the option to first assess qualitative factors to determine whether it is more likely than not that the fair value of an indefinite-lived intangible is less than its carrying amount. An entity may choose to perform the qualitative assessment or an entity may bypass the qualitative assessment and proceed directly to the quantitative impairment test. If it is determined, on the basis of qualitative factors, that the fair value of the indefinite-lived intangible asset is, more likely than not, less than its carrying value, the quantitative impairment test is required. When performing a quantitative assessment, we estimate the fair value of our cable franchise rights primarily based on a discounted cash flow analysis that involves significant judgment. When analyzing the fair values indicated under the discounted cash flow models, we also consider multiples of operating income before depreciation and amortization generated by the underlying assets, current market transactions and profitability information.

In 2016, we performed a qualitative assessment of our cable franchise rights. At the time of our previous quantitative assessment in 2014, the estimated fair values of our franchise rights exceeded the carrying value in our three Cable Communications divisions by 26%, 42% and 50%, respectively. We also considered various factors that would affect the estimated fair values of our cable franchise rights in our qualitative assessment in 2016, including changes in our projected future cash flows associated with our Cable Communications segment; market transactions and macroeconomic conditions; weighted-average cost of capital; and an increase in our market capitalization. Based on this assessment, we concluded that it was more likely than not that the estimated fair values of our cable franchise rights were higher than the carrying values and that the performance of a quantitative impairment test was not required.

Since the adoption of the accounting guidance related to goodwill and intangible assets in 2002, we have not recorded any significant impairment charges to cable franchise rights as a result of our impairment testing.

We could record impairment charges in the future if there are changes in long-term market conditions, in expected future operating results, or in federal or state regulations that prevent us from recovering the carrying value of these cable franchise rights. Assumptions made about increased competition and economic conditions could also impact the results of any qualitative assessment and the valuations used in future annual quantitative impairment testing and result in a reduction in the fair values of our cable franchise rights. In addition, a future change in the unit of account could result in the recognition of an impairment charge.

### **Film and Television Costs**

We capitalize film and television production costs, including direct costs, production overhead, print costs, development costs and interest. We amortize capitalized film and television production costs, including acquired libraries, and accrue costs associated with participation and residual payments to programming and production expenses. We generally record the amortization and the accrued costs using the individual film forecast computation method, which amortizes the costs using the ratio of the current period's revenue to estimated total remaining revenue from all sources ("ultimate revenue"). Estimates of ultimate revenue have a significant impact on how quickly capitalized costs are amortized and, therefore, are updated regularly.

Our estimates of ultimate revenue for films generally include revenue from all sources that are expected to be earned within 10 years from the date of a film's initial release. These estimates are based on the historical performance of similar content, as well as factors unique to the content itself. The most sensitive factor affecting our estimate of ultimate revenue for a film intended for theatrical release is the film's theatrical performance, as subsequent revenue from the licensing and sale of a film has historically exhibited a high correlation to its theatrical performance. Upon a film's release, our estimates of revenue from succeeding

## Table of Contents

markets, including from content licensing across multiple platforms and home entertainment sales, are revised based on historical relationships and an analysis of current market trends.

With respect to television series or other owned television programming, the most sensitive factor affecting our estimate of ultimate revenue is whether the series can be successfully licensed beyond its initial license. Initial estimates of ultimate revenue are limited to the amount of revenue contracted for each episode under the initial license. Once it is determined that a television series or other owned television programming can be licensed for subsequent platforms, revenue estimates for these platforms, such as U.S. and international syndication, home entertainment, and other distribution platforms, are included in ultimate revenue. Revenue estimates for produced episodes include revenue expected to be earned within 10 years of delivery of the initial episode or, if still in production, 5 years from the delivery of the most recent episode, if later.

We capitalize the costs of programming content that we license but do not own, including rights to multiyear, live-event sports programming, at the earlier of when payments are made for the programming or when the license period begins and the content is made available for use. We amortize capitalized programming costs as the associated programs are broadcast. We generally amortize multiyear, live-event sports programming rights using the ratio of the current period revenue to the estimated ultimate revenue or under the terms of the contract.

Capitalized film and television costs, as well as stage play production costs, are subject to impairment testing when certain triggering events are identified. If the fair value of a production were to fall below its unamortized cost, we would record an adjustment for the amount by which the unamortized capitalized costs exceed the production's fair value. The fair value assessment is generally based on estimated future discounted cash flows, which are supported by our internal forecasts. Adjustments to capitalized film and stage play production costs of \$14 million, \$42 million and \$26 million were recorded in 2016, 2015 and 2014, respectively.

## Item 7A: Quantitative and Qualitative Disclosures About Market Risk

### Interest Rate Risk Management

---

We maintain a mix of fixed-rate and variable-rate debt and we are exposed to the market risk of adverse changes in interest rates. In order to manage the cost and volatility relating to the interest cost of our outstanding debt, we enter into various interest rate risk management derivative transactions in accordance with our policies.

We monitor our exposure to the risk of adverse changes in interest rates through the use of techniques that include market value and sensitivity analyses. We do not engage in any speculative or leveraged derivative transactions.

Our interest rate derivative financial instruments, which may include swaps, rate locks, caps and collars, represent an integral part of our interest rate risk management program. Comcast's interest rate derivative financial instruments reduced the portion of Comcast's total consolidated debt at fixed rates as of December 31, 2016 to 85.3% from 88.9%. As of December 31, 2016, NBCUniversal had no outstanding interest rate derivative financial instruments.

In 2016, 2015 and 2014, the effect of our interest rate derivative financial instruments was to decrease Comcast's consolidated interest expense by \$36 million, \$62 million and \$66 million, respectively. The effect

## Table of Contents

of NBCUniversal's interest rate derivative financial instruments was not material to NBCUniversal's consolidated financial statements for all periods presented. Interest rate derivative financial instruments may have a significant effect on Comcast's interest expense in the future.

The table below summarizes as of December 31, 2016 by contractual year of maturity the principal cash flows, notional amounts, fair values and contract terms of financial instruments subject to interest rate risk maintained by us.

(in millions)	2017	2018	2019	2020	2021	Thereafter	Total	Estimated Fair Value as of December 31, 2016
<b>Debt</b>								
Fixed rate	\$ 2,589	\$ 3,346	\$ 2,234	\$ 3,429	\$ 2,043	\$ 40,959	\$ 54,600	\$ 59,561
Average interest rate	6.9%	4.5%	3.2%	5.1%	4.4%	4.8%	4.8%	
Variable rate	\$ 2,894	\$ 857	\$ 232	\$ 2,788	\$ —	\$ —	\$ 6,771	\$ 6,777
Average interest rate	1.8%	2.5%	2.4%	3.0%	—%	—%	2.4%	
<b>Interest Rate Instruments</b>								
Fixed to variable swaps	\$ 400	\$ 1,600	\$ 200	\$ —	\$ —	\$ —	\$ 2,200	\$ 34
Average pay rate	6.0%	4.5%	5.1%	—%	—%	—%	4.5%	
Average receive rate	6.3%	5.8%	5.7%	—%	—%	—%	5.9%	

We use the notional amount of each interest rate derivative financial instrument to calculate the interest to be paid or received. The notional amounts do not represent our exposure to credit loss. The estimated fair value approximates the amount of payments to be made or proceeds to be received to settle the outstanding contracts, including accrued interest. We estimate interest rates on variable rate debt and swaps using the relevant average implied forward rates through the year of maturity based on the yield curve in effect on December 31, 2016, plus the applicable borrowing margin on December 31, 2016.

See Note 2 to each of Comcast's and NBCUniversal's consolidated financial statements for additional information on our accounting policies for derivative financial instruments.

## Foreign Exchange Risk Management

NBCUniversal has significant operations in a number of countries outside the United States, and certain of NBCUniversal's operations are conducted in foreign currencies. The value of these currencies fluctuates relative to the U.S. dollar. These changes could adversely affect the U.S. dollar equivalent value of our non-U.S. dollar revenue and operating costs and expenses and reduce international demand for our content, all of which could negatively affect our business, financial condition and results of operations in a given period or in specific territories.

As part of our overall strategy to manage the level of exposure to the risk of foreign exchange rate fluctuations, NBCUniversal enters into derivative financial instruments related to a significant portion of its foreign currency exposure, which is a result of transactions denominated in other than the functional currency. NBCUniversal enters into foreign currency forward contracts that change in value as currency exchange rates fluctuate to protect the U.S. dollar equivalent value of its non-U.S. dollar assets, liabilities, commitments, and forecasted foreign currency revenue and expenses. In accordance with our policy, NBCUniversal hedges forecasted foreign currency transactions for periods generally not to exceed 18 months. In certain circumstances, NBCUniversal enters into foreign exchange contracts with initial maturities in excess of 18 months. As of December 31, 2016 and 2015, NBCUniversal had foreign exchange contracts with a total notional value of \$1.5 billion and \$998 million, respectively. As of December 31, 2016 and 2015, the aggregate estimated fair value of these foreign exchange contracts was not material.

## Table of Contents

We have analyzed our foreign currency exposure related to NBCUniversal's operations as of December 31, 2016, including our hedging contracts, to identify assets and liabilities denominated in a currency other than their functional currency. For those assets and liabilities, we then evaluated the effect of a 10% shift in currency exchange rates between the functional currency and the U.S. dollar. Our analysis of such a shift in exchange rates indicated that there would be an immaterial effect on our 2016 income. In addition, the impact of fluctuations in currencies relative to the U.S. dollar for our non-U.S. dollar functional currency operations did not have a material impact on our financial condition or results of operations in 2016.

Comcast is also exposed to the market risks associated with fluctuations in currency exchange rates as they relate to its foreign currency denominated debt obligations. We use cross-currency swaps for foreign currency denominated debt obligations when those obligations are denominated in a currency other than the functional currency. Cross-currency swaps effectively convert fixed-rate foreign currency denominated debt to fixed-rate U.S. dollar denominated debt in order to hedge the risk that the cash flows related to annual interest payments and the payment of principal at maturity may be adversely affected by fluctuations in currency exchange rates. The gains and losses on the cross-currency swaps offset changes in the U.S. dollar equivalent value of the related exposures. As of December 31, 2016 and 2015, the fair value of our cross-currency swaps on our £625 million principal amount of 5.50% senior notes due 2029 was a liability of \$189 million and \$71 million, respectively.

### Counterparty Credit Risk Management

Comcast and NBCUniversal manage the credit risks associated with our derivative financial instruments through diversification and the evaluation and monitoring of the creditworthiness of counterparties. Although we may be exposed to losses in the event of nonperformance by counterparties, we do not expect such losses, if any, to be significant. Comcast has agreements with certain counterparties that include collateral provisions. These provisions require a party with an aggregate unrealized loss position in excess of certain thresholds to post cash collateral for the amount in excess of the threshold. The threshold levels in our collateral agreements are based on our and the counterparty's credit ratings. As of December 31, 2016 and 2015, Comcast was not required to post collateral under the terms of these agreements. As of December 31, 2016 and 2015, we did not hold any collateral under the terms of these agreements.

Table of Contents

## Item 8: Comcast Corporation Financial Statements and Supplementary Data

<u>Index</u>	<u>Page</u>
<u>Report of Management</u>	73
<u>Report of Independent Registered Public Accounting Firm</u>	74
<u>Consolidated Balance Sheet</u>	75
<u>Consolidated Statement of Income</u>	76
<u>Consolidated Statement of Comprehensive Income</u>	77
<u>Consolidated Statement of Cash Flows</u>	78
<u>Consolidated Statement of Changes in Equity</u>	79
<u>Notes to Consolidated Financial Statements</u>	80

**NBCUniversal Media, LLC**

See Index to NBCUniversal Media, LLC Financial Statements and Supplemental Data on page 137.

## Table of Contents

### Report of Management

#### **Management's Report on Comcast's Financial Statements**

Our management is responsible for the preparation, integrity and fair presentation of information in Comcast's consolidated financial statements, including estimates and judgments. The consolidated financial statements presented in this report have been prepared in accordance with accounting principles generally accepted in the United States. Our management believes the Comcast consolidated financial statements and other financial information included in this report fairly present, in all material respects, Comcast's financial condition, results of operations and cash flows as of and for the periods presented in this report. The Comcast consolidated financial statements have been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report, which is included herein.

#### **Management's Report on Comcast's Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining an adequate system of internal control over financial reporting. Our system of internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States.

Our internal control over financial reporting includes those policies and procedures that:

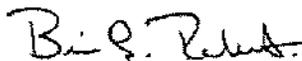
- Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect our transactions and dispositions of our assets.
- Provide reasonable assurance that our transactions are recorded as necessary to permit preparation of our financial statements in accordance with accounting principles generally accepted in the United States, and that our receipts and expenditures are being made only in accordance with authorizations of our management and our directors.
- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Because of its inherent limitations, a system of internal control over financial reporting can provide only reasonable assurance and may not prevent or detect misstatements. Further, because of changes in conditions, effectiveness of internal control over financial reporting may vary over time. Our system contains self-monitoring mechanisms, and actions are taken to correct deficiencies as they are identified.

Our management conducted an evaluation of the effectiveness of the system of internal control over financial reporting based on the framework in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, our management concluded that Comcast's system of internal control over financial reporting was effective as of December 31, 2016. Our assessment of the effectiveness of internal control over financial reporting as of December 31, 2016 did not include the internal controls of DreamWorks Animation, which we acquired on August 22, 2016, as permitted by Securities and Exchange Commission guidelines that allow companies to exclude certain acquisitions from their assessment of internal control over financial reporting during the first year of an acquisition. The total assets and total revenues of DreamWorks Animation represented approximately 2% of our total assets as of December 31, 2016, and less than 1% of our total revenues for the year ended December 31, 2016. The effectiveness of Comcast's internal controls over financial reporting of Comcast has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report, which is included herein.

#### **Audit Committee Oversight**

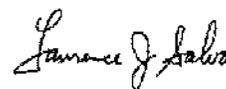
The Audit Committee of the Board of Directors, which is comprised solely of independent directors, has oversight responsibility for our financial reporting process and the audits of Comcast's consolidated financial statements and internal control over financial reporting. The Audit Committee meets regularly with management and with our internal auditors and independent registered public accounting firm (collectively, the "auditors") to review matters related to the quality and integrity of our financial reporting, internal control over financial reporting (including compliance matters related to our Code of Conduct), and the nature, extent, and results of internal and external audits. Our auditors have full and free access and report directly to the Audit Committee. The Audit Committee recommended, and the Board of Directors approved, that the Comcast audited consolidated financial statements be included in this Form 10-K.



**Brian L. Roberts**  
Chairman and  
Chief Executive Officer



**Michael J. Cavanagh**  
Senior Executive Vice President and  
Chief Financial Officer



**Lawrence J. Salva**  
Executive Vice President  
and Chief Accounting Officer

Table of Contents**Report of Independent Registered Public Accounting Firm****To the Board of Directors and Stockholders of  
Comcast Corporation  
Philadelphia, Pennsylvania**

We have audited the accompanying consolidated balance sheets of Comcast Corporation and subsidiaries (the "Company") as of December 31, 2016 and 2015, and the related consolidated statements of income, comprehensive income, cash flows and changes in equity for each of the three years in the period ended December 31, 2016. We also have audited the Company's internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. As described in the Report of Management on Internal Control over Financial Reporting, management excluded from its assessment the internal control over financial reporting at DreamWorks Animation, acquired on August 22, 2016 and whose financial statements constitute approximately 2% of total assets as of December 31, 2016 and less than 1% of total revenue for the year ended December 31, 2016. Accordingly, our audit did not include the internal control over financial reporting at DreamWorks Animation. The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying *Management's Report on Comcast's Internal Control Over Financial Reporting*. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Comcast Corporation and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on the criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

**/s/ Deloitte & Touche LLP**  
Philadelphia, Pennsylvania  
February 3, 2017

Table of Contents**Comcast Corporation**  
Consolidated Balance Sheet

December 31 (in millions, except share data)	2016	2015
<b>Assets</b>		
Current Assets:		
Cash and cash equivalents	\$ 3,301	\$ 2,295
Receivables, net	7,955	6,896
Programming rights	1,250	1,213
Deposits	1,772	21
Other current assets	2,083	1,878
<b>Total current assets</b>	<b>16,361</b>	<b>12,303</b>
Film and television costs	7,252	5,855
Investments	5,247	3,224
Property and equipment, net	36,253	33,665
Franchise rights	59,364	59,364
Goodwill	35,980	32,945
Other intangible assets, net	17,274	16,946
Other noncurrent assets, net	2,769	2,272
<b>Total assets</b>	<b>\$ 180,500</b>	<b>\$ 166,574</b>
<b>Liabilities and Equity</b>		
Current Liabilities:		
Accounts payable and accrued expenses related to trade creditors	\$ 6,915	\$ 6,215
Accrued participations and residuals	1,726	1,572
Deferred revenue	1,132	1,302
Accrued expenses and other current liabilities	6,282	5,462
Current portion of long-term debt	5,480	3,627
<b>Total current liabilities</b>	<b>21,535</b>	<b>18,178</b>
Long-term debt, less current portion	55,566	48,994
Deferred income taxes	34,854	33,566
Other noncurrent liabilities	10,925	10,637
Commitments and contingencies (Note 16)		
Redeemable noncontrolling interests and redeemable subsidiary preferred stock	1,446	1,221
Equity:		
Preferred stock—authorized, 20,000,000 shares; issued, zero	—	—
Class A common stock, \$0.01 par value—authorized, 7,500,000,000 shares; issued, 2,802,752,832 and 2,869,349,502; outstanding, 2,366,357,318 and 2,432,953,988	28	29
Class B common stock, \$0.01 par value—authorized, 75,000,000 shares; issued and outstanding, 9,444,375	—	—
Additional paid-in capital	38,258	38,518
Retained earnings	23,076	21,413
Treasury stock, 436,395,514 Class A common shares	(7,517)	(7,517)
Accumulated other comprehensive income (loss)	98	(174)
<b>Total Comcast Corporation shareholders' equity</b>	<b>53,943</b>	<b>52,269</b>
Noncontrolling interests	2,231	1,709
<b>Total equity</b>	<b>56,174</b>	<b>53,978</b>
<b>Total liabilities and equity</b>	<b>\$ 180,500</b>	<b>\$ 166,574</b>

See accompanying notes to consolidated financial statements.

Table of Contents**Comcast Corporation**  
Consolidated Statement of Income

Year ended December 31 (in millions, except per share data)	2016	2015	2014
<b>Revenue</b>	<b>\$ 80,403</b>	<b>\$ 74,510</b>	<b>\$ 68,775</b>
Costs and Expenses:			
Programming and production	24,463	22,550	20,912
Other operating and administrative	23,409	21,319	19,839
Advertising, marketing and promotion	6,114	5,963	5,101
Depreciation	7,464	6,781	6,337
Amortization	2,094	1,899	1,682
	<b>63,544</b>	<b>58,512</b>	<b>53,871</b>
<b>Operating income</b>	<b>16,859</b>	<b>15,998</b>	<b>14,904</b>
Other Income (Expense):			
Interest expense	(2,942)	(2,702)	(2,617)
Investment income (loss), net	213	81	296
Equity in net income (losses) of investees, net	(104)	(325)	97
Other income (expense), net	327	320	(215)
	<b>(2,506)</b>	<b>(2,626)</b>	<b>(2,439)</b>
Income before income taxes	14,353	13,372	12,465
Income tax expense	(5,308)	(4,959)	(3,873)
Net income	9,045	8,413	8,592
Net (income) loss attributable to noncontrolling interests and redeemable subsidiary preferred stock	(350)	(250)	(212)
<b>Net income attributable to Comcast Corporation</b>	<b>\$ 8,695</b>	<b>\$ 8,163</b>	<b>\$ 8,380</b>
<b>Basic earnings per common share attributable to Comcast Corporation shareholders</b>	<b>\$ 3.61</b>	<b>\$ 3.28</b>	<b>\$ 3.24</b>
<b>Diluted earnings per common share attributable to Comcast Corporation shareholders</b>	<b>\$ 3.57</b>	<b>\$ 3.24</b>	<b>\$ 3.20</b>
<b>Dividends declared per common share</b>	<b>\$ 1.10</b>	<b>\$ 1.00</b>	<b>\$ 0.90</b>
<b>Unaudited pro forma diluted earnings per common share attributable to Comcast Corporation shareholders, adjusted for the two-for-one stock split. See Note 1.</b>	<b>\$ 1.78</b>	<b>\$ 1.62</b>	<b>\$ 1.60</b>

See accompanying notes to consolidated financial statements.

Table of Contents**Comcast Corporation**  
Consolidated Statement of Comprehensive Income

Year ended December 31 (in millions)	2016	2015	2014
Net income	\$ 9,045	\$ 8,413	\$ 8,592
Unrealized gains (losses) on marketable securities, net of deferred taxes of \$(1), \$(1) and \$(19)	—	1	33
Deferred gains (losses) on cash flow hedges, net of deferred taxes of \$35, \$62 and \$3	(60)	(106)	(5)
Amounts reclassified to net income:			
Realized (gains) losses on marketable securities, net of deferred taxes of \$1, \$1 and \$59	(1)	(1)	(99)
Realized (gains) losses on cash flow hedges, net of deferred taxes of \$(54), \$(38) and \$(27)	92	64	46
Employee benefit obligations, net of deferred taxes of \$(125), \$(43) and \$82	213	74	(139)
Currency translation adjustments, net of deferred taxes of \$(14), \$34 and \$23	102	(89)	(38)
Comprehensive income	9,391	8,356	8,390
Net (income) loss attributable to noncontrolling interests and redeemable subsidiary preferred stock	(350)	(250)	(212)
Other comprehensive (income) loss attributable to noncontrolling interests	(74)	29	—
<b>Comprehensive income attributable to Comcast Corporation</b>	<b>\$ 8,967</b>	<b>\$ 8,135</b>	<b>\$ 8,178</b>

See accompanying notes to consolidated financial statements.

Table of Contents**Comcast Corporation**  
Consolidated Statement of Cash Flows

Year ended December 31 (in millions)	2016	2015	2014
<b>Operating Activities</b>			
Net income	\$ 9,045	\$ 8,413	\$ 8,592
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	9,558	8,680	8,019
Share-based compensation	640	567	513
Noncash interest expense (income), net	230	205	180
Equity in net (income) losses of investees, net	104	325	(97)
Cash received from investees	85	168	104
Net (gain) loss on investment activity and other	(169)	(318)	4
Deferred income taxes	1,444	958	1,165
Changes in operating assets and liabilities, net of effects of acquisitions and divestitures:			
Current and noncurrent receivables, net	(782)	(708)	(33)
Film and television costs, net	(495)	(299)	(562)
Accounts payable and accrued expenses related to trade creditors	374	384	153
Other operating assets and liabilities	(794)	403	(1,093)
<b>Net cash provided by operating activities</b>	<b>19,240</b>	<b>18,778</b>	<b>16,945</b>
<b>Investing Activities</b>			
Capital expenditures	(9,135)	(8,499)	(7,420)
Cash paid for intangible assets	(1,686)	(1,370)	(1,122)
Acquisitions and construction of real estate properties	(428)	(178)	(43)
Acquisitions, net of cash acquired	(3,929)	(1,786)	(477)
Proceeds from sales of businesses and investments	218	433	666
Purchases of investments	(1,697)	(784)	(191)
Deposits	(1,749)	(18)	—
Other	21	238	(146)
<b>Net cash provided by (used in) investing activities</b>	<b>(18,385)</b>	<b>(11,964)</b>	<b>(8,733)</b>
<b>Financing Activities</b>			
Proceeds from (repayments of) short-term borrowings, net	1,790	135	(504)
Proceeds from borrowings	9,231	5,486	4,182
Repurchases and repayments of debt	(3,052)	(4,378)	(3,175)
Repurchases and retirements of common stock	(5,000)	(6,750)	(4,251)
Dividends paid	(2,601)	(2,437)	(2,254)
Issuances of common stock	23	36	35
Distributions to noncontrolling interests and dividends for redeemable subsidiary preferred stock	(253)	(232)	(220)
Other	13	(289)	167
<b>Net cash provided by (used in) financing activities</b>	<b>151</b>	<b>(8,429)</b>	<b>(6,020)</b>
Increase (decrease) in cash and cash equivalents	1,006	(1,615)	2,192
Cash and cash equivalents, beginning of year	2,295	3,910	1,718
<b>Cash and cash equivalents, end of year</b>	<b>\$ 3,301</b>	<b>\$ 2,295</b>	<b>\$ 3,910</b>

See accompanying notes to consolidated financial statements.

## Table of Contents

### Comcast Corporation Consolidated Statement of Changes in Equity

(in millions)	Redeemable Noncontrolling Interests and Redeemable Subsidiary Preferred Stock	Common Stock			Additional Paid-In Capital	Retained Earnings	Treasury Stock at Cost	Accumulated Other Comprehensive Income (Loss)	Non- controlling Interests	Total Equity
		A	A Special	B						
Balance, December 31, 2013	\$ 957	\$ 25	\$ 5	\$ —	\$ 38,890	\$ 19,235	\$ (7,517)	\$ 56	\$ 364	\$ 51,058
Stock compensation plans					732	(433)				299
Repurchases and retirements of common stock					(928)	(3,323)				(4,251)
Employee stock purchase plans					118					118
Dividends declared						(2,320)				(2,320)
Other comprehensive income (loss)							(202)			(202)
Issuance of subsidiary shares to noncontrolling interests	85								11	11
Contributions from (distributions to) noncontrolling interests, net	(19)								(132)	(132)
Other	(33)				(7)				(22)	(29)
Net income (loss)	76					8,380			136	8,516
Balance, December 31, 2014	1,066	25	5	—	38,805	21,539	(7,517)	(146)	357	53,068
Stock compensation plans					739	(402)				337
Repurchases and retirements of common stock			(1)		(1,345)	(5,404)				(6,750)
Employee stock purchase plans					136					136
Dividends declared						(2,483)				(2,483)
Other comprehensive income (loss)							(28)	(29)		(57)
Contributions from (distributions to) noncontrolling interests, net	11								(146)	(146)
Reclassification of Class A Special common stock		4	(4)							—
Universal Studios Japan									1,440	1,440
Other	58				183				(77)	106
Net income (loss)	86					8,163			164	8,327
Balance, December 31, 2015	1,221	29	—	—	38,518	21,413	(7,517)	(174)	1,709	53,978
Stock compensation plans					720	(326)				394
Repurchases and retirements of common stock		(1)			(949)	(4,050)				(5,000)
Employee stock purchase plans					156					156
Dividends declared						(2,656)				(2,656)
Other comprehensive income (loss)								272	74	346
Contributions from (distributions to) noncontrolling interests, net	(16)								(134)	(134)
Other	148				(187)				325	138
Net income (loss)	93					8,695			257	8,952
Balance, December 31, 2016	\$ 1,446	\$ 28	\$ —	\$ —	\$ 38,258	\$ 23,076	\$ (7,517)	\$ 98	\$ 2,231	\$ 56,174

See accompanying notes to consolidated financial statements.

## Table of Contents

### **Comcast Corporation**

#### Notes to Consolidated Financial Statements

##### **Note 1: Business and Basis of Presentation**

---

We are a global media and technology company with two primary businesses, Comcast Cable and NBCUniversal. We were incorporated under the laws of Pennsylvania in December 2001. Through our predecessors, we have developed, managed and operated cable systems since 1963.

We present our operations for Comcast Cable in one reportable business segment, referred to as Cable Communications, and our operations for NBCUniversal in four reportable business segments: Cable Networks, Broadcast Television, Filmed Entertainment and Theme Parks (collectively, the "NBCUniversal segments"). See Note 17 for additional information on our reportable business segments.

Our Cable Communications segment primarily manages and operates cable systems that serve residential and business customers in the United States. As of December 31, 2016, our cable systems had 28.6 million total customer relationships and served 22.5 million video customers, 24.7 million high-speed Internet customers and 11.7 million voice customers.

Our Cable Networks segment consists primarily of a diversified portfolio of cable television networks. Our cable networks are comprised of our national cable networks that provide a variety of entertainment, news and information, and sports content, our regional sports and news networks, our international cable networks, and our cable television studio production operations.

Our Broadcast Television segment consists primarily of the NBC and Telemundo broadcast networks, our owned NBC and Telemundo local broadcast television stations, the NBC Universo national cable network, and our broadcast television studio production operations.

Our Filmed Entertainment segment primarily produces, acquires, markets and distributes filmed entertainment worldwide. Our films are produced primarily under the Universal Pictures, Illumination and Focus Features names and in August 2016, we acquired DreamWorks Animation. See Note 5 for additional information on the acquisition.

Our Theme Parks segment consists primarily of our Universal theme parks in Orlando, Florida and Hollywood, California and our 51% interest in the Universal Studios theme park in Osaka, Japan ("Universal Studios Japan"), which we acquired in November 2015. See Note 5 for additional information on the acquisition.

Our other business interests, which are included in Corporate and Other, consist primarily of Comcast Spectacor, which owns the Philadelphia Flyers and the Wells Fargo Center arena in Philadelphia, Pennsylvania and operates arena management-related businesses.

##### **Basis of Presentation**

The accompanying consolidated financial statements include all entities in which we have a controlling voting interest and variable interest entities ("VIEs") required to be consolidated in accordance with generally accepted accounting principles in the United States ("GAAP").

We translate assets and liabilities of our foreign operations where the functional currency is the local currency, primarily the Japanese yen, euro and British pound, into U.S. dollars at the exchange rate as of the balance sheet date and translate revenue and expenses using average monthly exchange rates. The related translation adjustments are recorded as a component of accumulated other comprehensive income (loss) in our consolidated balance sheet. Any foreign currency transaction gains or losses are included in our consolidated statement of income.

## Table of Contents

### **Comcast Corporation**

#### **Reclassifications**

Reclassifications have been made to our consolidated financial statements for the prior years to conform to classifications used in 2016.

#### **Stock Split**

On January 24, 2017, our Board of Directors approved a two-for-one stock split in the form of a 100% stock dividend (the "Stock Split") payable on February 17, 2017 to shareholders of record as of February 8, 2017. The Stock Split will be in the form of one additional share for every share held and will be payable in shares of Class A common stock on the outstanding Class A common stock and Class B common stock. The pro forma diluted earnings per common share attributable to Comcast Corporation shareholders in our consolidated statement of income has been adjusted to reflect the Stock Split for all periods presented. All other share-based data, including the number of shares outstanding and related prices, per share amounts, and share authorizations and conversions have not been adjusted to reflect the Stock Split for any of the periods presented.

#### **Note 2: Accounting Policies**

---

Our consolidated financial statements are prepared in accordance with GAAP, which require us to select accounting policies, including in certain cases industry-specific policies, and make estimates that affect the reported amount of assets, liabilities, revenue and expenses, and the related disclosure of contingent assets and contingent liabilities. Actual results could differ from these estimates. We believe that the judgments and related estimates for the following items are critical in the preparation of our consolidated financial statements:

- valuation and impairment testing of cable franchise rights (see Note 9)
- film and television costs (see Note 6)

In addition, the following accounting policies are specific to the industries in which we operate:

- capitalization and amortization of film and television costs (see Note 6)
- installation revenue and costs for connecting customers to our cable systems (see revenue recognition below and Note 8)

Information on our other accounting policies and methods that are used in the preparation of our consolidated financial statements are included, where applicable, in their respective footnotes that follow. Below is a discussion of accounting policies and methods used in our consolidated financial statements that are not presented within other footnotes.

#### **Revenue Recognition**

##### **Cable Communications Segment**

Our Cable Communications segment generates revenue primarily from subscriptions to our video, high-speed Internet and voice services ("cable services") and from the sale of advertising. We recognize revenue from cable services as each service is provided. Customers are typically billed in advance on a monthly basis based on the services and features they receive and the type of equipment they use. Since installation revenue obtained from the connection of customers to our cable systems is less than the related direct selling costs, we recognize revenue as connections are completed. We manage credit risk by screening applicants through the use of internal customer information, identification verification tools and credit bureau data. If a customer's account is delinquent, various measures are used to collect outstanding amounts, including termination of the customer's cable services.

## Table of Contents

### **Comcast Corporation**

As part of our distribution agreements with cable networks, we generally receive an allocation of scheduled advertising time on cable networks that we sell through our advertising business, Spotlight, to local, regional and national advertisers. We recognize advertising revenue when the advertising is aired or viewed. In most cases, the available advertising units are sold by our sales force. In some cases, we work with representation firms as an extension of our sales force to sell a portion of the advertising units allocated to us. We also represent the advertising sales efforts of other multichannel video providers in some markets. Since we are acting as the principal in these arrangements, we record the advertising that is sold in revenue and the fees paid to representation firms and multichannel video providers in other operating and administrative expenses.

Revenue earned from other sources, such as our home security and automation services, is recognized when services are provided or events occur. Under the terms of our cable franchise agreements, we are generally required to pay to the cable franchising authority an amount based on our gross video revenue. We pass these fees through to our cable services customers and classify the fees as a component of revenue with the corresponding costs included in other operating and administrative expenses.

#### **Cable Networks and Broadcast Television Segments**

Our Cable Networks segment generates revenue primarily from the distribution of our cable network programming to multichannel video providers, from the sale of advertising on our cable networks and related digital media properties, from the licensing of our owned programming to cable and broadcast networks and subscription video on demand services, from the sale of our owned programming on standard-definition digital video discs and Blu-ray discs (together, "DVDs") and through digital distribution services such as iTunes, and from the sale of programming by our cable television studio production operations to third-party networks and subscription video on demand services. Our Broadcast Television segment generates revenue primarily from the sale of advertising on our broadcast networks, owned local broadcast television stations and related digital media properties, from the licensing of our owned programming by our broadcast television studio production operations to various distribution platforms, including to cable and broadcast networks as well as to subscription video on demand services, from the fees received under retransmission consent agreements and associated fees received from NBC-affiliated local broadcast television stations, and from the sale of our owned programming on DVDs and through digital distribution services. We recognize revenue from distributors as programming is provided, generally under multiyear distribution agreements. From time to time, the distribution agreements expire while programming continues to be provided to the distributor based on interim arrangements while the parties negotiate new contract terms. Revenue recognition is generally limited to current payments being made by the distributor, typically under the prior contract terms, until a new contract is negotiated, sometimes with effective dates that affect prior periods. Differences between actual amounts determined upon resolution of negotiations and amounts recorded during these interim arrangements are recorded in the period of resolution.

Advertising revenue for our Cable Networks and Broadcast Television segments is recognized in the period in which commercials are aired or viewed. In some instances, we guarantee audience ratings for the commercials. To the extent there is a shortfall in the ratings that were guaranteed, a portion of the revenue is deferred until the shortfall is settled, primarily by providing additional advertising units. We recognize revenue from the licensing of our owned programming and programming produced by our studios for third parties when the content is made available for use by the licensee, and when certain other conditions are met. When license fees include advertising time, we recognize the component of revenue associated with the advertisements when they are aired or viewed.

#### **Filmed Entertainment Segment**

Our Filmed Entertainment segment generates revenue primarily from the worldwide distribution of our produced and acquired films for exhibition in movie theaters, from the licensing of our owned and acquired films through various distribution platforms, and from the sale of our owned and acquired films on DVDs and

## Table of Contents

### **Comcast Corporation**

through digital distribution services. Our Filmed Entertainment segment also generates revenue from producing and licensing live stage plays, from the distribution of filmed entertainment produced by third parties, and from Fandango, our movie ticketing and entertainment business. We recognize revenue from the distribution of films to movie theaters when the films are exhibited. We recognize revenue from the licensing of a film when the film is available for use by the licensee, and when certain other conditions are met. We recognize revenue from the sale of DVDs, net of estimated returns and customer incentives, on the date that the DVDs are delivered to and made available for sale by retailers.

#### Theme Parks Segment

Our Theme Parks segment generates revenue primarily from ticket sales and guest spending at our Universal theme parks. We recognize revenue from advance theme park ticket sales when the tickets are used. For annual passes, we recognize revenue on a straight-line basis over the period following the activation date.

### **Cable Communications Programming Expenses**

Cable Communications programming expenses are the fees we pay to license the programming we distribute to our video customers. Programming is generally acquired under multiyear distribution agreements, with rates typically based on the number of customers that receive the programming, channel positioning and the extent of distribution. From time to time, these contracts expire and programming continues to be provided under interim arrangements while the parties negotiate new contract terms, sometimes with effective dates that affect prior periods. While payments are typically made under the prior contract's terms, the amount of programming expenses recorded during the interim arrangement is based on our estimate of the ultimate contract terms expected to be negotiated. Differences between actual amounts determined upon resolution of negotiations and amounts recorded during these interim arrangements are recorded in the period of resolution.

When our Cable Communications segment receives incentives from a cable network for the licensing of its programming, we defer a portion of these incentives, which are included in other current and noncurrent liabilities, and recognize them over the term of the contract as a reduction to programming expenses.

### **Advertising Expenses**

Advertising costs are expensed as incurred.

### **Cash Equivalents**

The carrying amounts of our cash equivalents approximate their fair values. Our cash equivalents consist primarily of money market funds and U.S. government obligations, as well as commercial paper and certificates of deposit with maturities of three months or less when purchased.

### **Derivative Financial Instruments**

We use derivative financial instruments to manage our exposure to the risks associated with fluctuations in interest rates, foreign exchange rates and equity prices. Our objective is to manage the financial and operational exposure arising from these risks by offsetting gains and losses on the underlying exposures with gains and losses on the derivatives used to economically hedge them.

Our derivative financial instruments are recorded in our consolidated balance sheet at fair value. The impact of our derivative financial instruments on our consolidated financial statements was not material in any of the periods presented.

### **Fair Value Measurements**

The accounting guidance related to financial assets and financial liabilities ("financial instruments") establishes a hierarchy that prioritizes fair value measurements based on the types of inputs used for the various

## Table of Contents

### **Comcast Corporation**

valuation techniques (market approach, income approach and cost approach). The levels of the hierarchy are described below.

- Level 1: Values are determined using quoted market prices for identical financial instruments in an active market
- Level 2: Values are determined using quoted prices for similar financial instruments and valuation models whose inputs are observable
- Level 3: Values are determined using pricing models that use significant inputs that are primarily unobservable, discounted cash flow methodologies or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation

We use these levels of hierarchy for the measurement of fair value related to acquisitions, investments, long-term debt, redeemable subsidiary preferred stock and impairment testing, among others. Our assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the valuation and classification within the fair value hierarchy. Our financial instruments that are accounted for at fair value on a recurring basis were not material as of December 31, 2016 and 2015.

### **Asset Retirement Obligations**

Certain of our cable franchise agreements and lease agreements contain provisions requiring us to restore facilities or remove property in the event that the franchise or lease agreement is not renewed. We expect to continually renew our cable franchise agreements and therefore cannot reasonably estimate any liabilities associated with such agreements. A remote possibility exists that franchise agreements could be terminated unexpectedly, which could result in us incurring significant expense in complying with restoration or removal provisions. We do not have any significant liabilities related to asset retirements recorded in our consolidated financial statements.

### **Note 3: Recent Accounting Pronouncements**

#### **Revenue Recognition**

In May 2014, the Financial Accounting Standards Board ("FASB") updated the accounting guidance related to revenue recognition. The updated accounting guidance provides a single, contract-based revenue recognition model to help improve financial reporting by providing clearer guidance on when an entity should recognize revenue and by reducing the number of standards to which an entity has to refer. The updated accounting guidance is effective for us as of January 1, 2018.

We have reviewed a majority of our revenue arrangements and expect our review to be completed in the second quarter of 2017. As a result of our review, we do not expect any material impact on our consolidated financial statements. However, we do expect that the new standard will impact the timing of recognition for (1) our Cable Communications segment's installation revenue and commission expenses, which upon adoption will be recognized as revenue and costs over a period of time instead of immediately, and (2) our Cable Networks, Broadcast Television and Filmed Entertainment segments' content licensing revenue associated with renewals or extensions of existing program licensing agreements, which upon adoption will be recognized as revenue when the licensed content becomes available under the renewal or extension instead of when the agreement is renewed or extended.

The guidance provides companies with alternative methods of adoption and we are in the process of determining our method of adoption, which depends in part upon our completion of the evaluation of our remaining revenue arrangements.

## Table of Contents

### **Comcast Corporation**

#### **Consolidations**

In February 2015, the FASB updated the accounting guidance related to consolidation under the variable interest entity and voting interest entity models. The updated accounting guidance modifies the consolidation guidance for VIEs, limited partnerships and similar legal entities. We have adopted this guidance as of January 1, 2016 and it did not have a material impact on our consolidated financial statements.

#### **Financial Assets and Financial Liabilities**

In January 2016, the FASB updated the accounting guidance related to the recognition and measurement of financial assets and financial liabilities. The updated accounting guidance, among other things, requires that all nonconsolidated equity investments, except those accounted for under the equity method, be measured at fair value and that the changes in fair value be recognized in net income. The updated guidance is effective for us as of January 1, 2018. The updated accounting guidance requires, with certain exceptions, a cumulative effect adjustment to beginning retained earnings when the guidance is adopted. We are currently in the process of determining the impact that the updated accounting guidance will have on our consolidated financial statements.

#### **Leases**

In February 2016, the FASB updated the accounting guidance related to leases. The updated accounting guidance requires lessees to recognize a right-of-use asset and a lease liability on the balance sheet for all leases with the exception of short-term leases. The asset and liability are initially measured based on the present value of committed lease payments. For a lessee, the recognition, measurement and presentation of expenses and cash flows arising from a lease do not significantly change from previous guidance. For a lessor, the accounting applied is also largely unchanged from previous guidance. The updated guidance is effective for us as of January 1, 2019 and early adoption is permitted. The updated accounting guidance must be adopted using a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. We are currently in the process of determining the impact that the updated accounting guidance will have on our consolidated financial statements. See Note 16 for a summary of our undiscounted minimum rental commitments under operating leases as of December 31, 2016.

#### **Share-Based Compensation**

In March 2016, the FASB updated the accounting guidance that affects several aspects of the accounting for share-based compensation. The most significant change for us relates to the presentation of the income and withholding tax consequences of share-based compensation in our consolidated financial statements. Among the changes, the updated guidance requires that the excess income tax benefits or deficiencies that arise when the tax consequences of share-based compensation differ from amounts previously recognized in the statement of income be recognized as income tax benefit or expense in the statement of income rather than as additional paid-in capital in the balance sheet. The guidance also states that excess income tax benefits should not be presented separately from other income taxes in the statement of cash flows and, thus, should be classified as an operating activity rather than a financing activity as they are under the current guidance. In addition, the updated guidance requires when an employer withholds shares upon exercise of options or the vesting of restricted stock for the purpose of meeting withholding tax requirements, that the cash paid for withholding taxes be classified as a financing activity. We currently record these amounts within operating activities.

We will adopt the updated guidance in the first quarter of 2017. As required under the updated guidance, we will prospectively adopt the provisions of this guidance that relate to the recognition of the excess income tax benefits or deficiencies in the statement of income. If we had adopted the updated guidance in 2016, our income tax expense and effective tax rate would have decreased by \$233 million and 1.6%, respectively, and

Table of Contents**Comcast Corporation**

our diluted earnings per common share attributable to Comcast Corporation shareholders in 2016 would have increased by \$0.08.

In addition, upon adoption we will retrospectively adopt the provisions of this guidance related to changes to the statement of cash flows in any of the periods presented. The table below presents the effect on our consolidated statement of cash flows for each of the years ended December 31, 2016, 2015 and 2014. These amounts are not necessarily indicative of amounts that we will recognize in future years related to the excess income tax benefits or deficiencies nor the cash paid for withholding taxes.

Year ended December 31 (in millions)	As Reported	Effect of Adoption	Upon Adoption
<b>2016</b>			
Net cash provided by operating activities	\$ 19,240	\$ 585	\$ 19,825
Net cash provided by (used in) financing activities	\$ 151	\$ (585)	\$ (434)
<b>2015</b>			
Net cash provided by operating activities	\$ 18,778	\$ 708	\$ 19,486
Net cash provided by (used in) financing activities	\$ (8,429)	\$ (708)	\$ (9,137)
<b>2014</b>			
Net cash provided by operating activities	\$ 16,945	\$ 652	\$ 17,597
Net cash provided by (used in) financing activities	\$ (6,020)	\$ (652)	\$ (6,672)

**Note 4: Earnings Per Share**

## Computation of Diluted EPS

Year ended December 31 (in millions, except per share data)	2016			2015			2014		
	Net Income Attributable to Comcast Corporation	Shares	Per Share Amount	Net Income Attributable to Comcast Corporation	Shares	Per Share Amount	Net Income Attributable to Comcast Corporation	Shares	Per Share Amount
<b>Basic EPS attributable to Comcast Corporation shareholders</b>	<b>\$ 8,695</b>	<b>2,410</b>	<b>\$ 3.61</b>	<b>\$ 8,163</b>	<b>2,486</b>	<b>\$ 3.28</b>	<b>\$ 8,380</b>	<b>2,583</b>	<b>\$ 3.24</b>
<b>Effect of dilutive securities:</b>									
Assumed exercise or issuance of shares relating to stock plans		28			32			37	
<b>Diluted EPS attributable to Comcast Corporation shareholders</b>	<b>\$ 8,695</b>	<b>2,438</b>	<b>\$ 3.57</b>	<b>\$ 8,163</b>	<b>2,518</b>	<b>\$ 3.24</b>	<b>\$ 8,380</b>	<b>2,620</b>	<b>\$ 3.20</b>

Diluted earnings per common share attributable to Comcast Corporation shareholders ("diluted EPS") considers the impact of potentially dilutive securities using the treasury stock method. Our potentially dilutive securities include potential common shares related to our stock options and our restricted share units ("RSUs"). Diluted EPS excludes the impact of potential common shares related to our stock options in periods in which the combination of the option exercise price and the associated unrecognized compensation expense is greater than the average market price of our common stock.

The amount of potential common shares related to our share-based compensation plans that were excluded from diluted EPS because their effect would have been antidilutive was not material in any of the periods presented.

Table of Contents**Comcast Corporation****Note 5: Significant Transactions****2016***DreamWorks Animation*

On August 22, 2016, we acquired all of the outstanding stock of DreamWorks Animation for \$3.8 billion. DreamWorks Animation's stockholders received \$41 in cash for each share of DreamWorks Animation common stock. DreamWorks Animation creates animated feature films, television series and specials, live entertainment and related consumer products. The results of operations for DreamWorks Animation are reported in our Filmed Entertainment segment following the acquisition date.

*Preliminary Allocation of Purchase Price*

The transaction was accounted for under the acquisition method of accounting and, accordingly, the assets and liabilities are to be recorded at their fair market values as of the acquisition date. We recorded the acquired assets and liabilities of DreamWorks Animation at their estimated fair values based on preliminary valuation analyses. In valuing acquired assets and liabilities, fair value estimates are primarily based on Level 3 inputs including future expected cash flows, market rate assumptions and discount rates. The fair value of the assumed debt was primarily based on quoted market values. The fair value of the liability related to a tax receivable agreement that DreamWorks Animation had previously entered into with one of its former stockholders (the "tax receivable agreement") was based on the contractual settlement provisions in the agreement. Further, we recorded the deferred income taxes based on our estimates of the tax basis of the acquired net assets and the valuation allowances based on the expected use of net operating loss carryforwards. The goodwill is not deductible for tax purposes. We will adjust the assets and liabilities as valuations are completed and we obtain information necessary to complete the analyses, but no later than one year from the acquisition date.

The table below presents the preliminary allocation of the purchase price to the assets and liabilities of DreamWorks Animation.

*Preliminary Allocation of Purchase Price**(in millions)*

Film and television costs (see Note 6)	\$ 854
Intangible assets (see Note 9)	164
Working capital	248
Debt (see Note 10)	(381)
Tax receivable agreement	(146)
Deferred income taxes (see Note 14)	366
Other noncurrent assets and liabilities	137
Identifiable net assets (liabilities) acquired	1,242
Noncontrolling interest	(89)
Goodwill (see Note 9)	2,620
Cash consideration transferred	\$ 3,773

The tax receivable agreement was settled immediately following the acquisition and the payment was recorded as an operating activity in our consolidated statement of cash flows. In addition, we repaid all of the assumed debt of DreamWorks Animation.

Revenue and net income attributable to the acquisition of DreamWorks Animation were not material for 2016.

Table of Contents**Comcast Corporation****2015**

## Universal Studios Japan

On November 13, 2015, NBCUniversal acquired a 51% economic interest in Universal Studios Japan for \$1.5 billion.

Universal Studios Japan is a VIE based on the governance structure and we consolidate Universal Studios Japan since we have the power to direct activities that most significantly impact its economic performance. There are no liquidity arrangements, guarantees or other financial commitments between us and Universal Studios Japan, and therefore our maximum risk of financial loss is NBCUniversal's 51% interest. Universal Studios Japan's results of operations are reported in our Theme Parks segment following the acquisition date.

*Allocation of Purchase Price*

The transaction was accounted for under the acquisition method of accounting and, accordingly, the acquired assets and liabilities and the 49% noncontrolling interest were recorded at their estimated fair values. In 2016, we updated the allocation of the purchase price for Universal Studios Japan based on final valuation analyses, which primarily resulted in increases to property and equipment and intangible assets and a decrease in goodwill. The changes did not have a material impact on our consolidated financial statements. The goodwill is not deductible for tax purposes.

The table below presents the allocation of the purchase price to the assets and liabilities of Universal Studios Japan.

## Allocation of Purchase Price

<i>(in millions)</i>	
Property and equipment (see Note 8)	\$ 780
Intangible assets (see Note 9)	323
Working capital	(33)
Debt (see Note 10)	(3,271)
Other noncurrent assets and liabilities	17
Identifiable net assets (liabilities) acquired	(2,184)
Noncontrolling interest	(1,440)
Goodwill (see Note 9)	5,123
Cash consideration transferred	\$ 1,499

*Actual and Unaudited Pro Forma Results*

Our consolidated revenue in 2016 and 2015 included \$1.4 billion and \$169 million, respectively, from the acquisition of Universal Studios Japan. Our net income attributable to Comcast Corporation in 2016 and 2015 included \$124 million and \$18 million, respectively, from the acquisition of Universal Studios Japan.

Table of Contents**Comcast Corporation**

The following unaudited pro forma information has been presented as if the acquisition of Universal Studios Japan occurred on January 1, 2014. This information is primarily based on historical results of operations, adjusted for the allocation of purchase price, and is not necessarily indicative of what our results would have been had we operated Universal Studios Japan since January 1, 2014. No pro forma adjustments have been made for our transaction-related expenses.

Year ended December 31 (in millions, except per share amounts)	2015	2014
Revenue	\$ 75,563	\$ 69,860
Net income	\$ 8,591	\$ 8,704
Net income attributable to Comcast Corporation	\$ 8,253	\$ 8,435
Basic earnings per common share attributable to Comcast Corporation shareholders	\$ 3.32	\$ 3.27
Diluted earnings per common share attributable to Comcast Corporation shareholders	\$ 3.28	\$ 3.22

**Time Warner Cable Merger and Related Divestiture Transactions**

On April 24, 2015, we and Time Warner Cable Inc. terminated our planned merger, and we terminated our related agreement with Charter Communications, Inc. to spin off, exchange and sell certain cable systems. In connection with these proposed transactions, we incurred incremental transaction-related expenses of \$198 million and \$237 million in 2015 and 2014, respectively. The transaction-related expenses are included primarily in other operating and administrative expenses, with \$20 million recorded in depreciation and amortization expenses associated with the write-off of certain capitalized costs in 2015.

**Note 6: Film and Television Costs**

December 31 (in millions)	2016	2015
<b>Film Costs:</b>		
Released, less amortization	\$ 1,750	\$ 1,275
Completed, not released	50	226
In production and in development	1,310	907
	<b>3,110</b>	<b>2,408</b>
<b>Television Costs:</b>		
Released, less amortization	1,953	1,573
In production and in development	853	737
	<b>2,806</b>	<b>2,310</b>
<b>Programming rights, less amortization</b>	<b>2,586</b>	<b>2,350</b>
	<b>8,502</b>	<b>7,068</b>
Less: Current portion of programming rights	1,250	1,213
<b>Film and television costs</b>	<b>\$ 7,252</b>	<b>\$ 5,855</b>

Based on our current estimates of the total remaining revenue from all sources ("ultimate revenue"), in 2017 we expect to amortize approximately \$1.9 billion of film and television costs associated with our original film and television productions that have been released, or are completed and have not been released. Through 2019, we expect to amortize approximately 88% of unamortized film and television costs for our released productions, excluding amounts allocated to acquired libraries.

As of December 31, 2016, acquired film and television libraries, which are included within the "released, less amortization" captions in the table above, had remaining unamortized costs of \$596 million. These costs are generally amortized over a period not to exceed 20 years, and approximately 45% of these costs are expected to be amortized through 2019.

## Table of Contents

### Comcast Corporation

#### **Capitalization of Film and Television Costs**

We capitalize film and television production costs, including direct costs, production overhead, print costs, development costs and interest. We amortize capitalized film and television production costs, including acquired libraries, and accrue costs associated with participation and residual payments to programming and production expenses. We generally record the amortization and the accrued costs using the individual film forecast computation method, which amortizes the costs in the same ratio as the associated ultimate revenue. Estimates of ultimate revenue and total costs are based on anticipated release patterns, public acceptance and historical results for similar productions. Unamortized film and television costs, including acquired film and television libraries, are stated at the lower of unamortized cost or fair value. We do not capitalize costs related to the distribution of a film in movie theaters or the licensing or sale of a film or television production, which are primarily costs associated with the marketing and distribution of them.

In determining the method of amortization and estimated life of an acquired film or television library, we generally use the method and the life that most closely follow the undiscounted cash flows over the estimated life of the asset.

When an event or a change in circumstance occurs that was known or knowable as of the balance sheet date and that indicates the fair value of a film is less than its unamortized costs, we determine the fair value of the film and record an impairment charge for the amount by which the unamortized capitalized costs exceed the film's fair value. The estimated fair value of a production is based on Level 3 inputs that primarily use an analysis of future expected cash flows. Adjustments to capitalized film and stage play production costs of \$14 million, \$42 million and \$26 million were recorded in 2016, 2015 and 2014, respectively.

We enter into cofinancing arrangements with third parties to jointly finance or distribute certain of our film productions. Cofinancing arrangements can take various forms, but in most cases involve the grant of an economic interest in a film to an investor. The number of investors and the terms of these arrangements can vary, although investors generally assume the full risks and rewards for the portion of the film acquired in these arrangements. We account for the proceeds received from a third-party investor under these arrangements as a reduction to our capitalized film costs. Under these arrangements, the investor owns an undivided copyright interest in the film, and therefore in each period we record either a charge or a benefit to programming and production expenses to reflect the estimate of the third-party investor's interest in the profit or loss of the film. The estimate of the third-party investor's interest in the profit or loss of a film is determined using the ratio of actual revenue earned to date to the ultimate revenue expected to be recognized over the film's useful life.

We capitalize the costs of programming content that we license but do not own, including rights to multiyear, live-event sports programming, at the earlier of when payments are made for the programming or when the license period begins and the content is made available for use. We amortize capitalized programming costs as the associated programs are broadcast. We generally amortize multiyear, live-event sports programming rights using the ratio of the current period revenue to the estimated ultimate revenue or under the terms of the contract.

Acquired programming costs are recorded at the lower of unamortized cost or net realizable value on a program by program, package, channel or daypart basis. A daypart is an aggregation of programs broadcast during a particular time of day or programs of a similar type. Programming acquired by our Cable Networks segment is primarily tested on a channel basis for impairment, whereas programming acquired by our Broadcast Television segment is tested on a daypart basis. If we determine that the estimates of future cash flows are insufficient or if there is no plan to broadcast certain programming, we recognize an impairment charge to programming and production expenses.

Table of Contents**Comcast Corporation****Note 7: Investments**

December 31 (in millions)	2016	2015	
Fair Value Method	\$ 198	\$ 167	
Equity Method:			
Atairios	1,601	—	
Hulu	225	184	
Other	550	494	
	2,376	678	
Cost Method:			
AirTouch	1,599	1,583	
BuzzFeed	400	200	
Other	771	702	
	2,770	2,485	
Total investments	5,344	3,330	
Less: Current investments	97	106	
Noncurrent investments	\$ 5,247	\$ 3,224	
Investment Income (Loss), Net			
Year ended December 31 (in millions)	2016	2015	2014
Gains on sales and exchanges of investments, net	\$ 46	\$ 12	\$ 192
Investment impairment losses	(34)	(59)	(50)
Unrealized gains on securities underlying prepaid forward sale agreements	—	42	66
Mark to market adjustments on derivative component of prepaid forward sale agreements and indexed debt instruments	(4)	(42)	(56)
Interest and dividend income	123	115	116
Other, net	82	13	28
Investment income (loss), net	\$ 213	\$ 81	\$ 296

**Fair Value Method**

We classify publicly traded investments that are not accounted for under the equity method as available-for-sale ("AFS") or trading securities and record them at fair value. For AFS securities, we record unrealized gains or losses resulting from changes in fair value between measurement dates as a component of other comprehensive income (loss), except when we consider declines in value to be other than temporary. For trading securities, we record unrealized gains or losses resulting from changes in fair value between measurement dates as a component of investment income (loss), net. We recognize realized gains and losses associated with our fair value method investments using the specific identification method. We classify the cash flows related to purchases of and proceeds from the sale of trading securities based on the nature of the securities and the purpose for which they were acquired.

**Equity Method**

We use the equity method to account for investments in which we have the ability to exercise significant influence over the investee's operating and financial policies or in which we hold a significant partnership or LLC interest. Equity method investments are recorded at cost and are adjusted to recognize (1) our proportionate share of the investee's net income or loss after the date of investment, (2) amortization of the recorded investment that exceeds our share of the book value of the investee's net assets, (3) additional contributions made and dividends received, and (4) impairments resulting from other-than-temporary declines in fair value.

## Table of Contents

### **Comcast Corporation**

For some investments, we record our share of the investee's net income or loss one quarter in arrears due to the timing of our receipt of such information. Gains or losses on the sale of equity method investments are recorded to other income (expense), net. If an equity method investee were to issue additional securities that would change our proportionate share of the entity, we would recognize the change, if any, as a gain or loss in our consolidated statement of income.

#### **Atairos**

In 2015, we entered into an agreement to establish Atairos Group, Inc., a strategic company focused on investing in and operating companies in a range of industries and business sectors, both domestically and internationally. The agreement became effective as of January 1, 2016. Atairos has a term of up to 12 years and is controlled by management companies led by our former CFO through interests that carry all of the voting rights. We are the only investor other than our former CFO and the other management company employees. We have committed to fund Atairos up to \$4 billion in the aggregate at any one time, subject to certain offsets, and \$40 million annually for a management fee, subject to certain adjustments, while the management company investors have committed to fund up to \$100 million, with at least \$40 million to be funded by our former CFO, subject to his continued role with Atairos. Our economic interests do not carry voting rights and obligate us to absorb approximately 99% of any losses and they provide us the right to receive approximately 86.5% of any residual returns in Atairos, in either case on a cumulative basis.

We have concluded that Atairos is a VIE, that we do not have the power to direct the activities that most significantly impact the economic performance of Atairos as we have no voting rights and only certain consent rights, and that we are not a related party with our former CFO or the management companies. We therefore do not consolidate Atairos and account for our investment as an equity method investment. There are no other liquidity arrangements, guarantees or other financial commitments between Comcast and Atairos, and therefore our maximum risk of financial loss is our investment balance and remaining unfunded capital commitment.

In 2016, we made cash capital contributions totaling \$1.2 billion to Atairos. In addition, we recorded capital contributions of \$447 million that were accrued in 2016 and paid in January 2017.

#### **Hulu**

In August 2016, Time Warner Inc. acquired a 10% interest in Hulu, LLC, which diluted our interest in Hulu from 33% to 30%. For a period not to exceed 3 years, Time Warner may put its shares to Hulu or Hulu may call Time Warner's shares under certain limited circumstances arising from regulatory review. Given the contingent nature of the put and call options, we recorded a deferred gain of \$159 million and a corresponding increase to our investment in Hulu as a result of the dilution. The deferred gain will be recognized in other income (expense), net if and when the options expire unexercised.

In 2016, 2015 and 2014, we recognized our proportionate share of losses of \$168 million, \$106 million and \$20 million, respectively, related to our investment in Hulu.

#### **The Weather Channel**

In January 2016, following a legal restructuring at The Weather Channel, we and the other investors sold the entity holding The Weather Channel's product and technology businesses to IBM. Following the close of the transaction, we continue to hold an investment in The Weather Channel cable network through a new holding company. As a result of the sale of our investment, we recognized a pretax gain of \$108 million in other income (expense), net.

In June and December 2015, The Weather Channel recorded impairment charges related to goodwill. In 2015, we recorded expenses of \$333 million that represented NBCUniversal's proportionate share of these impairment charges in equity in net income (losses) of investees, net in our consolidated statement of income.

## Table of Contents

### **Comcast Corporation**

#### **Cost Method**

We use the cost method to account for investments not accounted for under the fair value method or the equity method.

#### **AirTouch**

We hold two series of preferred stock of Verizon Americas, Inc., formerly known as AirTouch Communications, Inc., a subsidiary of Verizon Communications Inc., which are redeemable in April 2020. As of both December 31, 2016 and 2015, the estimated fair value of the AirTouch preferred stock was \$1.7 billion.

The dividend and redemption activity of the AirTouch preferred stock determines the dividend and redemption payments associated with substantially all of the preferred shares issued by one of our consolidated subsidiaries, which is a VIE. The subsidiary has three series of preferred stock outstanding with an aggregate redemption value of \$1.75 billion. Substantially all of the AirTouch preferred stock is redeemable in April 2020 at a redemption value of \$1.65 billion. As of both December 31, 2016 and 2015, the two series of redeemable subsidiary preferred shares were recorded at \$1.6 billion, and those amounts are included in other noncurrent liabilities. As of both December 31, 2016 and 2015, the liability related to the redeemable subsidiary preferred shares had an aggregate estimated fair value of \$1.7 billion. The estimated fair values of the AirTouch preferred stock and redeemable subsidiary preferred shares are based on Level 2 inputs that use pricing models whose inputs are derived primarily from or corroborated by observable market data through correlation or other means for substantially the full term of the financial instrument. The one series of nonredeemable subsidiary preferred shares was recorded at \$100 million as of both December 31, 2016 and 2015, and those amounts are included in noncontrolling interests in our consolidated balance sheet. The carrying amount of the nonredeemable subsidiary preferred stock approximates its fair value.

#### **BuzzFeed and Vox Media**

In September 2015, NBCUniversal acquired an interest in BuzzFeed, Inc. and made an additional investment in Vox Media, Inc. for \$200 million each in cash. In November 2016, NBCUniversal made an additional investment of \$200 million in BuzzFeed. BuzzFeed is a global media company that produces and distributes original news, entertainment and videos. Vox Media is a digital media company comprised of eight distinct brands.

#### **Impairment Testing of Investments**

We review our investment portfolio each reporting period to determine whether there are identified events or circumstances that would indicate there is a decline in the fair value that would be considered other than temporary. For our nonpublic investments, if there are no identified events or circumstances that would have a significant adverse effect on the fair value of the investment, then the fair value is not estimated. If an investment is deemed to have experienced an other-than-temporary decline below its cost basis, we reduce the carrying amount of the investment to its quoted or estimated fair value, as applicable, and establish a new cost basis for the investment. For our AFS securities and our cost method investments, we record the impairment to investment income (loss), net. For our equity method investments, we record the impairment to other income (expense), net.

Table of Contents**Comcast Corporation****Note 8: Property and Equipment**

December 31 (in millions)	Weighted-Average Original Useful Life As of December 31, 2016	2016	2015
Cable distribution system	11 years	\$ 34,028	\$ 32,586
Customer premise equipment	6 years	28,621	28,559
Other equipment	8 years	9,475	8,539
Buildings and leasehold improvements	29 years	12,550	10,829
Land	N/A	1,273	1,252
Property and equipment, at cost		85,947	81,765
Less: Accumulated depreciation		49,694	48,100
Property and equipment, net		\$ 36,253	\$ 33,665

Property and equipment are stated at cost. We capitalize improvements that extend asset lives and expense repairs and maintenance costs as incurred. We record depreciation using the straight-line method over the asset's estimated useful life. For assets that are sold or retired, we remove the applicable cost and accumulated depreciation and, unless the gain or loss on disposition is presented separately, we recognize it as a component of depreciation expense.

In accordance with the accounting guidance related to cable television companies, we capitalize the costs associated with the construction of and improvements to our cable transmission and distribution facilities, including scalable infrastructure and line extensions; costs associated with acquiring and deploying new customer premise equipment; and costs associated with installation of our services. Costs capitalized include all direct costs for labor and materials, as well as various indirect costs. Costs incurred in connection with subsequent disconnects and reconnects are expensed as they are incurred.

We evaluate the recoverability of our property and equipment whenever events or substantive changes in circumstances indicate that the carrying amount may not be recoverable. The evaluation is based on the cash flows generated by the underlying asset groups, including estimated future operating results, trends or other determinants of fair value. If the total of the expected future undiscounted cash flows were less than the carrying amount of the asset group, we would recognize an impairment charge to the extent the carrying amount of the asset group exceeded its estimated fair value. Unless presented separately, the impairment charge is included as a component of depreciation expense.

Table of Contents**Comcast Corporation****Note 9: Goodwill and Intangible Assets****Goodwill**

(in millions)	NBCUniversal						Corporate and Other	Total
	Cable Communications	Cable Networks	Broadcast Television	Filmed Entertainment	Theme Parks			
Balance, December 31, 2014	\$ 12,217	\$ 12,948	\$ 767	\$ 211	\$ 982	\$ 191	\$ 27,316	
Acquisitions <sup>(a)</sup>	173	17	39	58	5,373	1	5,661	
Adjustments	(1)	—	—	—	—	—	(1)	
Foreign currency translation	—	(18)	—	(2)	(11)	—	(31)	
Balance, December 31, 2015	12,389	12,947	806	267	6,344	192	32,945	
Acquisitions <sup>(b)</sup>	82	232	—	2,717	—	1	3,032	
Adjustments <sup>(c)</sup>	174	—	—	—	(250)	(181)	(257)	
Foreign currency translation	—	4	—	9	247	—	260	
<b>Balance, December 31, 2016</b>	<b>\$ 12,645</b>	<b>\$ 13,183</b>	<b>\$ 806</b>	<b>\$ 2,993</b>	<b>\$ 6,341</b>	<b>\$ 12</b>	<b>\$ 35,980</b>	

(a) Acquisitions in 2015 in our Theme Parks segment included the Universal Studios Japan transaction (see Note 5 for additional information).

(b) Acquisitions in 2016 in our Filmed Entertainment segment primarily included the DreamWorks Animation acquisition (see Note 5 for additional information).

(c) Adjustments in 2016 primarily included the updated allocation of the purchase price for Universal Studios Japan in our Theme Parks segment (see Note 5 for additional information) and the reclassification of certain operations and businesses from Corporate and Other to our Cable Communications segment.

Goodwill is calculated as the excess of the consideration transferred over the identifiable net assets acquired in a business combination and represents the future economic benefits expected to arise from anticipated synergies and intangible assets acquired that do not qualify for separate recognition, including assembled workforce, noncontractual relationships and other agreements. We assess the recoverability of our goodwill annually, or more frequently whenever events or substantive changes in circumstances indicate that the carrying amount of a reporting unit may exceed its fair value. We test goodwill for impairment at the reporting unit level. To determine our reporting units, we evaluate the components one level below the segment level and we aggregate the components if they have similar economic characteristics. As a result of this assessment, our reporting units are the same as our five reportable segments. We evaluate the determination of our reporting units used to test for impairment periodically or whenever events or substantive changes in circumstances occur. The assessment of recoverability may first consider qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. A quantitative assessment is performed if the qualitative assessment results in a more-likely-than-not determination or if a qualitative assessment is not performed. The quantitative assessment considers whether the carrying amount of a reporting unit exceeds its fair value, in which case an impairment charge is recorded to the extent the carrying amount of the reporting unit's goodwill exceeds its implied fair value. Unless presented separately, the impairment charge is included as a component of amortization expense. We did not recognize any impairment charges in any of the periods presented.

Table of Contents**Comcast Corporation****Intangible Assets**

December 31 (in millions)	Weighted-Average Original Useful Life as of December 31, 2016	2016		2015	
		Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
<b>Indefinite-Lived Intangible Assets:</b>					
Franchise rights	N/A	\$ 59,364		\$ 59,364	
Trade names	N/A	2,981		2,857	
FCC licenses	N/A	651		651	
<b>Finite-Lived Intangible Assets:</b>					
Customer relationships	19 years	13,478	\$ (5,110)	13,396	\$ (4,442)
Software	4 years	7,017	(3,997)	6,008	(3,429)
Cable franchise renewal costs and contractual operating rights	9 years	1,460	(800)	1,499	(849)
Patents and other technology rights	7 years	257	(208)	409	(350)
Other agreements and rights	15 years	2,443	(898)	1,994	(798)
<b>Total</b>		<b>\$ 87,651</b>	<b>\$ (11,013)</b>	<b>\$ 86,178</b>	<b>\$ (9,868)</b>

**Indefinite-Lived Intangible Assets**

Indefinite-lived intangible assets consist primarily of our cable franchise rights. Our cable franchise rights represent the values we attributed to agreements with state and local authorities that allow access to homes and businesses in cable service areas acquired in business combinations. We do not amortize our cable franchise rights because we have determined that they meet the definition of indefinite-lived intangible assets since there are no legal, regulatory, contractual, competitive, economic or other factors which limit the period over which these rights will contribute to our cash flows. We reassess this determination periodically or whenever events or substantive changes in circumstances occur. Costs we incur in negotiating and renewing cable franchise agreements are included in other intangible assets and are generally amortized on a straight-line basis over the term of the franchise agreement.

We assess the recoverability of our cable franchise rights and other indefinite-lived intangible assets annually, or more frequently whenever events or substantive changes in circumstances indicate that the assets might be impaired. Our three Cable Communications divisions represent the unit of account we use to test for impairment of our cable franchise rights. We evaluate the unit of account used to test for impairment of our cable franchise rights and other indefinite-lived intangible assets periodically or whenever events or substantive changes in circumstances occur to ensure impairment testing is performed at an appropriate level. The assessment of recoverability may first consider qualitative factors to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount. A quantitative assessment is performed if the qualitative assessment results in a more-likely-than-not determination or if a qualitative assessment is not performed. When performing a quantitative assessment, we estimate the fair value of our cable franchise rights and other indefinite-lived intangible assets primarily based on a discounted cash flow analysis that involves significant judgment. When analyzing the fair values indicated under the discounted cash flow models, we also consider multiples of operating income before depreciation and amortization generated by the underlying assets, current market transactions, and profitability information. If the fair value of our cable franchise rights or other indefinite-lived intangible assets was less than the carrying amount, we would recognize an impairment charge for the difference between the estimated fair value and the carrying value of the assets. Unless presented separately, the impairment charge is included as a component of amortization expense. We did not recognize any material impairment charges in any of the periods presented.

Table of Contents**Comcast Corporation**

## Finite-Lived Intangible Assets

## Estimated Amortization Expense of Finite-Lived Intangible Assets

(in millions)	
2017	\$ 2,077
2018	\$ 1,828
2019	\$ 1,475
2020	\$ 1,168
2021	\$ 939

Finite-lived intangible assets are subject to amortization and consist primarily of customer relationships acquired in business combinations, software, cable franchise renewal costs, contractual operating rights and intellectual property rights. Our finite-lived intangible assets are amortized primarily on a straight-line basis over their estimated useful life or the term of the associated agreement.

We capitalize direct development costs associated with internal-use software, including external direct costs of material and services and payroll costs for employees devoting time to these software projects. We also capitalize costs associated with the purchase of software licenses. We include these costs in other intangible assets and generally amortize them on a straight-line basis over a period not to exceed five years. We expense maintenance and training costs, as well as costs incurred during the preliminary stage of a project, as they are incurred. We capitalize initial operating system software costs and amortize them over the life of the associated hardware.

We evaluate the recoverability of our finite-lived intangible assets whenever events or substantive changes in circumstances indicate that the carrying amount may not be recoverable. The evaluation is based on the cash flows generated by the underlying asset groups, including estimated future operating results, trends or other determinants of fair value. If the total of the expected future undiscounted cash flows were less than the carrying amount of the asset group, we would recognize an impairment charge to the extent the carrying amount of the asset group exceeded its estimated fair value. Unless presented separately, the impairment charge is included as a component of amortization expense.

**Note 10: Long-Term Debt**

## Long-Term Debt Outstanding

December 31 (in millions)	Weighted-Average Interest Rate as of December 31, 2016	2016	2015
Commercial paper	1.01%	\$ 2,781	\$ 975
Revolving bank credit facilities	—%	—	—
Term loans <sup>(a)</sup>	2.93%	3,262	3,259
Senior notes with maturities of 5 years or less, at face value	4.68%	13,850	14,300
Senior notes with maturities between 5 and 10 years, at face value	3.86%	12,049	9,630
Senior notes with maturities greater than 10 years, at face value <sup>(b)</sup>	5.19%	28,587	23,925
Other, including capital lease obligations	—	842	794
Debt issuance costs, premiums, discounts and fair value adjustments for hedged positions, net	—	(325)	(262)
<b>Total debt</b>	4.50% <sup>(c)</sup>	<b>61,046</b>	<b>52,621</b>
Less: Current portion		5,480	3,627
<b>Long-term debt</b>		<b>\$ 55,566</b>	<b>\$ 48,994</b>

## Table of Contents

### Comcast Corporation

- (a) The December 31, 2016 and 2015 amounts consist of ¥382 billion and ¥400 billion, respectively, of Universal Studios Japan term loans translated using the exchange rates as of these dates.
- (b) The December 31, 2016 and 2015 amounts include £625 million of 5.50% notes due 2029, which translated to \$771 million and \$921 million, respectively, using the exchange rates as of these dates.
- (c) Includes the effects of our derivative financial instruments.

As of December 31, 2016 and 2015, our debt had an estimated fair value of \$66.3 billion and \$58.0 billion, respectively. The estimated fair value of our publicly traded debt is primarily based on Level 1 inputs that use quoted market values for the debt. The estimated fair value of debt for which there are no quoted market prices is based on Level 2 inputs that use interest rates available to us for debt with similar terms and remaining maturities. See Note 19 for additional information on our cross-guarantee structure.

#### Principal Maturities of Debt

(in millions)	Weighted-Average Interest Rate as of December 31, 2016	
2017	4.22%	\$ 5,483
2018	4.05%	\$ 4,203
2019	3.11%	\$ 2,466
2020	4.18%	\$ 6,217
2021	4.36%	\$ 2,043
Thereafter	4.82%	\$ 40,959

#### 2016 Debt Borrowings

Year ended December 31, 2016 (in millions)	
Comcast 3.15% senior notes due 2026	\$ 2,200
Comcast 4.05% senior notes due 2046	1,430
Comcast 2.35% senior notes due 2027	1,400
Comcast 3.40% senior notes due 2046	1,400
Comcast 2.75% senior notes due 2023	1,100
Comcast 3.20% senior notes due 2036	1,000
Comcast 1.625% senior notes due 2022	700
Other	1
<b>Total</b>	<b>\$ 9,231</b>

#### 2016 Debt Redemptions and Repayments

Year ended December 31, 2016 (in millions)	
NBCUniversal 2.875% senior notes due 2016	\$ 1,000
Comcast 4.95% senior notes due 2016	750
NBCUniversal Enterprise senior notes due 2016	700
DreamWorks Animation assumed debt (see Note 5)	381
Other	221
<b>Total</b>	<b>\$ 3,052</b>

#### Debt Instruments

##### Revolving Bank Credit Facilities

In May 2016, we entered into a new \$7 billion revolving credit facility due 2021 with a syndicate of banks ("Comcast revolving credit facility") that may be used for general corporate purposes. We may increase the commitment under the Comcast revolving credit facility up to a total of \$10 billion, as well as extend the

## Table of Contents

### Comcast Corporation

expiration date to a date no later than 2023, subject to approval of the lenders. In addition, NBCUniversal Enterprise entered into a new \$1.5 billion revolving credit facility due 2021 with a syndicate of banks ("NBCUniversal Enterprise revolving credit facility") that may be used for general corporate purposes. We may increase the commitment under the NBCUniversal Enterprise revolving credit facility up to a total of \$2 billion, as well as extend the expiration date to a date no later than 2023, subject to approval of the lenders. The new revolving credit facilities replaced Comcast's \$6.25 billion and NBCUniversal Enterprise's \$1.35 billion revolving credit facilities, which were terminated in connection with the execution of the new revolving credit facilities. The interest rates on the new revolving credit facilities consist of a base rate plus a borrowing margin that is determined based on Comcast's credit rating. As of December 31, 2016, the borrowing margin for borrowings based on the London Interbank Offered Rate was 1.00%. Similar to the Comcast and NBCUniversal Enterprise prior revolving credit facilities, each of the new revolving credit facilities require that we maintain certain financial ratios based on their respective debt and operating income before depreciation and amortization, as defined in the credit facility. We were in compliance with all financial covenants for all periods presented.

As of December 31, 2016, amounts available under our consolidated credit facilities, net of amounts outstanding under our commercial paper programs and outstanding letters of credit, totaled \$5.5 billion, which included \$460 million available under the NBCUniversal Enterprise revolving credit facility.

#### Commercial Paper Programs

Our commercial paper programs provide a lower-cost source of borrowing to fund our short-term working capital requirements. The maximum borrowing capacity under the Comcast commercial paper program is \$6.25 billion. We support this commercial paper program with unused capacity under the Comcast revolving credit facility. The maximum borrowing capacity under the NBCUniversal Enterprise commercial paper program is \$1.35 billion. We support this commercial paper program with unused capacity under the NBCUniversal Enterprise revolving credit facility.

#### Term Loans

Our term loans consist of the Universal Studios Japan term loans, which have a final maturity of November 2020. These term loans contain financial and operating covenants and are secured by the assets of Universal Studios Japan and the equity interests of the other investors. We do not guarantee these term loans and they are otherwise nonrecourse to us.

#### Letters of Credit

As of December 31, 2016, we and certain of our subsidiaries had unused irrevocable standby letters of credit totaling \$443 million to cover potential fundings under various agreements.

### Note 11: Postretirement, Pension and Other Employee Benefit Plans

#### Postretirement Benefit Plans

Year ended December 31 (in millions)	2016	2015	2014
Benefit obligation	\$ 538	\$ 820	\$ 837
Plan funded status and recorded benefit obligation	\$ (538)	\$ (820)	\$ (837)
Portion of benefit obligation not yet recognized in benefits expense	\$ (372)	\$ (33)	\$ 46
Benefits expense	\$ 70	\$ 75	\$ 59
Discount rate	4.07-4.56%	4.70-4.73%	4.25%

We sponsor various benefit plans that provide postretirement benefits to eligible employees based on years of service. The Comcast Postretirement Healthcare Stipend Program (the "stipend plan") provides an annual stipend for

## Table of Contents

### **Comcast Corporation**

reimbursement of healthcare costs to each eligible employee based on years of service. Under the stipend plan, we are not exposed to the increasing costs of healthcare because the benefits are fixed at a predetermined amount. In December 2016, the stipend plan was amended primarily to reduce the benefits of active employees who retire after December 31, 2017. The plan amendments reduced our benefit obligation in 2016 by \$361 million.

NBCUniversal's postretirement medical and life insurance plans provide continuous coverage to employees eligible to receive such benefits. A small number of eligible employees also participate in legacy plans of acquired companies.

All of our postretirement benefit plans are unfunded and substantially all of our postretirement benefit obligations are recorded to noncurrent liabilities. The expense we recognize for our postretirement benefit plans is determined using certain assumptions, including the discount rate.

### **Pension Plans**

NBCUniversal sponsors various qualified and nonqualified defined benefit pension plans for domestic employees. Since the future benefits have been frozen since the beginning of 2013, we did not recognize service costs related to the pension plans for all periods presented. The benefits expense we recognized for our defined benefit plans was not material for all periods presented. In addition to the defined benefit plans it sponsors, NBCUniversal is also obligated to reimburse General Electric ("GE") for future benefit payments to those participants who were vested in the supplemental pension plan sponsored by GE at the time of the NBCUniversal transaction in 2011. These pension plans are currently unfunded and we recorded a benefit obligation of \$314 million and \$309 million as of December 31, 2016 and 2015, respectively, which consists primarily of our obligations to reimburse GE.

### **Other Employee Benefits**

#### **Deferred Compensation Plans**

We maintain unfunded, nonqualified deferred compensation plans for certain members of management and nonemployee directors (each, a "participant"). The amount of compensation deferred by each participant is based on participant elections. Participant accounts, except for those in the NBCUniversal plan, are credited with income primarily based on a fixed annual rate. Participants in the NBCUniversal plan designate one or more valuation funds, independently established funds or indices that are used to determine the amount of investment gain or loss in the participant's account. Participants are eligible to receive distributions from their account based on elected deferral periods that are consistent with the plans and applicable tax law.

The table below presents the benefit obligation and interest expense for our deferred compensation plans.

Year ended December 31 (in millions)	2016	2015	2014
Benefit obligation	\$ 2,164	\$ 2,038	\$ 1,774
Interest expense	\$ 178	\$ 171	\$ 149

We have purchased life insurance policies to recover a portion of the future payments related to our deferred compensation plans. As of December 31, 2016 and 2015, the cash surrender value of these policies, which is recorded to other noncurrent assets, was \$709 million and \$658 million, respectively.

#### **Retirement Investment Plans**

We sponsor several 401(k) defined contribution retirement plans that allow eligible employees to contribute a portion of their compensation through payroll deductions in accordance with specified plan guidelines. We make contributions to the plans that include matching a percentage of the employees' contributions up to certain limits. In 2016, 2015 and 2014, expenses related to these plans totaled \$446 million, \$416 million and \$379 million, respectively.

## Table of Contents

### **Comcast Corporation**

#### **Multiemployer Benefit Plans**

We participate in various multiemployer benefit plans, including pension and postretirement benefit plans, that cover some of our employees and temporary employees who are represented by labor unions. We also participate in other multiemployer benefit plans that provide health and welfare and retirement savings benefits to active and retired participants. We make periodic contributions to these plans in accordance with the terms of applicable collective bargaining agreements and laws but do not sponsor or administer these plans. We do not participate in any multiemployer benefit plans for which we consider our contributions to be individually significant, and the largest plans in which we participate are funded at a level of 80% or greater.

In 2016, 2015 and 2014, the total contributions we made to multiemployer pension plans were \$84 million, \$77 million and \$58 million, respectively. In 2016, 2015 and 2014, the total contributions we made to multiemployer postretirement and other benefit plans were \$136 million, \$119 million and \$125 million, respectively.

If we cease to be obligated to make contributions or were to otherwise withdraw from participation in any of these plans, applicable law would require us to fund our allocable share of the unfunded vested benefits, which is known as a withdrawal liability. In addition, actions taken by other participating employers may lead to adverse changes in the financial condition of one of these plans, which could result in an increase in our withdrawal liability.

#### **Severance Benefits**

We provide severance benefits to certain former employees. A liability is recorded when payment is probable, the amount is reasonably estimable, and the obligation relates to rights that have vested or accumulated. In 2016, 2015 and 2014, we recorded severance costs of \$315 million, \$181 million and \$152 million, respectively. Severance costs in 2016 included \$61 million of severance costs associated with the acquisition of DreamWorks Animation.

### **Note 12: Equity**

---

#### **Common Stock**

In the aggregate, holders of our Class A common stock have 66 <sup>2</sup>/<sub>3</sub>% of the voting power of our common stock and holders of our Class B common stock have 33 <sup>1</sup>/<sub>3</sub>% of the voting power of our common stock. Each share of our Class B common stock is entitled to 15 votes. The number of votes held by each share of our Class A common stock depends on the number of shares of Class A and Class B common stock outstanding at any given time. The 33 <sup>1</sup>/<sub>3</sub>% aggregate voting power of our Class B common stock cannot be diluted by additional issuances of any other class of common stock. Our Class B common stock is convertible, share for share, into Class A common stock, subject to certain restrictions.

#### **Class A Special Common Stock Reclassification**

In December 2015, our shareholders approved a proposal to amend and restate our Amended and Restated Certificate of Incorporation in order to reclassify each issued share of our Class A Special common stock into one share of our Class A common stock. This reclassification became effective as of the close of business on December 11, 2015, at which time our Class A Special common stock was no longer outstanding and ceased trading on the NASDAQ under the symbol CMCSK and instead became listed on the NASDAQ under the symbol CMCSA. There was no impact on basic and diluted EPS or the carrying value of total common stock as presented in our consolidated balance sheet because it was a one-for-one stock exchange.

Table of Contents**Comcast Corporation**

## Shares of Common Stock Outstanding

(in millions)	A	A Special	B
Balance, December 31, 2013	2,138	459	9
Stock compensation plans	13	—	—
Repurchases and retirements of common stock	(22)	(59)	—
Employee stock purchase plans	2	—	—
Balance, December 31, 2014	2,131	400	9
Stock compensation plans	12	—	—
Repurchases and retirements of common stock	(62)	(54)	—
Employee stock purchase plans	2	—	—
Reclassification of Class A Special common stock	346	(346)	—
Other	4	—	—
Balance, December 31, 2015	2,433	—	9
<b>Stock compensation plans</b>	<b>11</b>	<b>—</b>	<b>—</b>
<b>Repurchases and retirements of common stock</b>	<b>(81)</b>	<b>—</b>	<b>—</b>
<b>Employee stock purchase plans</b>	<b>3</b>	<b>—</b>	<b>—</b>
<b>Balance, December 31, 2016</b>	<b>2,366</b>	<b>—</b>	<b>9</b>

## Share Repurchases

Effective January 1, 2017, our Board of Directors increased our share repurchase program authorization to a total of \$12 billion, which does not have an expiration date. Under the authorization, we may repurchase shares in the open market or in private transactions.

## Share Repurchases

Year ended December 31 (in millions)	2016	2015	2014
Cash consideration	\$ 5,000	\$ 6,750	\$ 4,251
Shares repurchased	81	116	81

## Accumulated Other Comprehensive Income (Loss)

December 31 (in millions)	2016	2015
Unrealized gains (losses) on marketable securities	\$ —	\$ 1
Deferred gains (losses) on cash flow hedges	(14)	(46)
Unrecognized gains (losses) on employee benefit obligations	219	6
Cumulative translation adjustments	(107)	(135)
Accumulated other comprehensive income (loss), net of deferred taxes	\$ 98	\$ (174)

**Note 13: Share-Based Compensation**

The tables below provide condensed information on our share-based compensation.

## Recognized Share-Based Compensation Expense

Year ended December 31 (in millions)	2016	2015	2014
Restricted share units	\$ 306	\$ 273	\$ 231
Stock options	173	157	160
Employee stock purchase plans	28	25	23
Total	\$ 507	\$ 455	\$ 414

## Table of Contents

### Comcast Corporation

As of December 31, 2016, we had unrecognized pretax compensation expense of \$712 million related to nonvested RSUs and unrecognized pretax compensation expense of \$375 million related to nonvested stock options that will be recognized over a weighted-average period of approximately 1.7 years and 1.8 years, respectively. In 2016, 2015 and 2014, we recorded increases to additional paid-in capital of \$233 million, \$311 million and \$299 million, respectively, which were the result of tax benefits associated with our share-based compensation plans.

#### Stock Options and Restricted Share Units

As of December 31, 2016, unless otherwise stated (in millions, except per share data)	Stock Options	RSUs
Awards granted during 2016	21	8
Weighted-average exercise price of awards granted during 2016	\$ 60.01	
Stock options outstanding and nonvested RSUs	95	22
Weighted-average exercise price of stock options outstanding	\$ 42.60	
Weighted-average fair value at grant date of nonvested RSUs		\$ 52.11

As of December 31, 2016, substantially all of our stock options outstanding were net settled stock options. Net settled stock options, as opposed to stock options exercised with a cash payment, result in fewer shares being issued and no cash proceeds being received by us when the options are exercised. Our share-based compensation primarily consists of awards of RSUs and stock options to certain employees and directors as part of our approach to long-term incentive compensation. Awards generally vest over a period of 5 years and in the case of stock options, have a 10 year term. Additionally, through our employee stock purchase plans, employees are able to purchase shares of Comcast common stock at a discount through payroll deductions.

The cost associated with our share-based compensation is based on an award's estimated fair value at the date of grant and is recognized over the period in which any related services are provided. RSUs are valued based on the closing price of our common stock on the date of grant and are discounted for the lack of dividends, if any, during the vesting period. We use the Black-Scholes option pricing model to estimate the fair value of stock option awards. The table below presents the weighted-average fair value on the date of grant of RSUs and stock options awarded under our various plans and the related weighted-average valuation assumptions.

Year ended December 31	2016	2015	2014
RSUs fair value	\$ 60.03	\$ 58.81	\$ 47.91
Stock options fair value	\$ 11.55	\$ 11.78	\$ 11.11
Stock Option Valuation Assumptions:			
Dividend yield	1.8%	1.7%	1.8%
Expected volatility	23.0%	23.0%	24.0%
Risk-free interest rate	1.5%	1.6%	2.2%
Expected option life (in years)	6.1	6.0	6.5

Table of Contents**Comcast Corporation****Note 14: Income Taxes**

## Components of Income Tax Expense

Year ended December 31 (in millions)	2016	2015	2014
<b>Current Expense (Benefit):</b>			
Federal	\$ 3,190	\$ 3,210	\$ 2,392
State	480	570	174
Foreign	194	221	142
	<b>3,864</b>	<b>4,001</b>	<b>2,708</b>
<b>Deferred Expense (Benefit):</b>			
Federal	1,192	890	1,000
State	154	66	173
Foreign	98	2	(8)
	<b>1,444</b>	<b>958</b>	<b>1,165</b>
<b>Income tax expense</b>	<b>\$ 5,308</b>	<b>\$ 4,959</b>	<b>\$ 3,873</b>

Our income tax expense differs from the federal statutory amount because of the effect of the items detailed in the table below.

Year ended December 31 (in millions)	2016	2015	2014
Federal tax at statutory rate	\$ 5,024	\$ 4,680	\$ 4,363
State income taxes, net of federal benefit	373	326	329
Foreign income taxes, net of federal credit	65	13	—
Nontaxable income attributable to noncontrolling interests	(128)	(69)	(62)
Adjustments to uncertain and effectively settled tax positions, net	24	15	(408)
Accrued interest on uncertain and effectively settled tax positions, net	17	73	(235)
Other	(67)	(79)	(114)
<b>Income tax expense</b>	<b>\$ 5,308</b>	<b>\$ 4,959</b>	<b>\$ 3,873</b>

We base our provision for income taxes on our current period income, changes in our deferred income tax assets and liabilities, income tax rates, changes in estimates of our uncertain tax positions, and tax planning opportunities available in the jurisdictions in which we operate. We recognize deferred tax assets and liabilities when there are temporary differences between the financial reporting basis and tax basis of our assets and liabilities and for the expected benefits of using net operating loss carryforwards. When a change in the tax rate or tax law has an impact on deferred taxes, we apply the change based on the years in which the temporary differences are expected to reverse. We record the change in our consolidated financial statements in the period of enactment.

The determination of the income tax consequences of a business combination includes identifying the tax basis of assets and liabilities acquired and any contingencies associated with uncertain tax positions assumed or resulting from the business combination. Deferred tax assets and liabilities related to temporary differences of an acquired entity are recorded as of the date of the business combination and are based on our estimate of the ultimate tax basis that will be accepted by the various tax authorities. We record liabilities for contingencies associated with prior tax returns filed by the acquired entity based on criteria set forth in the appropriate accounting guidance. We adjust the deferred tax accounts and the liabilities periodically to reflect any revised estimated tax basis and any estimated settlements with the various tax authorities. The effects of these adjustments are recorded to income tax expense.

## Table of Contents

### Comcast Corporation

From time to time, we engage in transactions in which the tax consequences may be subject to uncertainty. In these cases, we evaluate our tax position using the recognition threshold and the measurement attribute in accordance with the accounting guidance related to uncertain tax positions. Examples of these transactions include business acquisitions and dispositions, including consideration paid or received in connection with these transactions, certain financing transactions, and the allocation of income among state and local tax jurisdictions. Significant judgment is required in assessing and estimating the tax consequences of these transactions. We determine whether it is more likely than not that a tax position will be sustained on examination, including the resolution of any related appeals or litigation processes, based on the technical merits of the position. A tax position that meets the more-likely-than-not recognition threshold is measured to determine the amount of benefit to be recognized in our consolidated financial statements. We classify interest and penalties, if any, associated with our uncertain tax positions as a component of income tax expense.

### NBCUniversal

For U.S. federal income tax purposes, NBCUniversal Holdings is treated as a partnership and NBCUniversal is disregarded as an entity separate from NBCUniversal Holdings. Accordingly, for U.S. federal and state income tax purposes, the income of NBCUniversal Holdings and NBCUniversal is included in tax returns filed by us and our subsidiaries. Therefore, neither NBCUniversal Holdings nor NBCUniversal and its subsidiaries incur any material current or deferred domestic income taxes.

We are indemnified by GE for any income tax liability attributable to the NBCUniversal contributed businesses for periods prior to the close of the NBCUniversal transaction in January 2011 and also for any income tax liability attributable to NBCUniversal Enterprise for periods prior to the date of the NBCUniversal redemption transaction in March 2013. We have indemnified GE for any income tax liability attributable to the businesses we contributed to NBCUniversal for periods prior to the close of the NBCUniversal transaction.

Current and deferred foreign income taxes are incurred by NBCUniversal's foreign subsidiaries. In 2016, 2015 and 2014, NBCUniversal had foreign income before taxes of \$871 million, \$704 million and \$385 million, respectively, on which foreign income tax expense was recorded. We recorded U.S. income tax expense on our allocable share of our subsidiaries' income before domestic and foreign taxes, which was reduced by a U.S. tax credit equal to our allocable share of our subsidiaries' foreign income tax expense.

### Components of Net Deferred Tax Liability

December 31 (in millions)	2016	2015
<b>Deferred Tax Assets:</b>		
Net operating loss carryforwards	\$ 544	\$ 551
Differences between book and tax basis of investments	—	101
Nondeductible accruals and other	3,789	3,704
Less: Valuation allowance	266	342
	<b>4,067</b>	<b>4,014</b>
<b>Deferred Tax Liabilities:</b>		
Differences between book and tax basis of property and equipment and intangible assets	37,401	36,392
Differences between book and tax basis of investments	144	—
Differences between book and tax basis of indexed debt securities	375	457
Differences between book and tax basis of foreign subsidiaries and undistributed foreign earnings	960	731
	<b>38,880</b>	<b>37,580</b>
<b>Net deferred tax liability</b>	<b>\$ 34,813</b>	<b>\$ 33,566</b>

## Table of Contents

### Comcast Corporation

Changes in our net deferred tax liability in 2016 that were not recorded as deferred income tax expense are primarily related to an increase of \$158 million associated with items included in other comprehensive income (loss), a decrease of \$226 million related to acquisitions and a decrease of \$129 million associated with our purchase of a noncontrolling interest. Our net deferred tax liability includes \$23 billion related to cable franchise rights that will remain unchanged unless we recognize an impairment or dispose of a cable franchise or there is a change in the tax law.

As of December 31, 2016, we had federal net operating loss carryforwards of \$598 million, including losses of DreamWorks Animation, and various state net operating loss carryforwards that expire in periods through 2036. As of December 31, 2016, we also had foreign net operating loss carryforwards of \$431 million that are related to the foreign operations of NBCUniversal, the majority of which expire in periods through 2026. The determination of the realization of the state and foreign net operating loss carryforwards is dependent on our subsidiaries' taxable income or loss, apportionment percentages, redetermination from taxing authorities, and state and foreign laws that can change from year to year and impact the amount of such carryforwards. We recognize a valuation allowance if we determine it is more likely than not that some portion, or all, of a deferred tax asset will not be realized. As of December 31, 2016 and 2015, our valuation allowance was primarily related to state and foreign net operating loss carryforwards.

### Uncertain Tax Positions

Our uncertain tax positions as of December 31, 2016 totaled \$1.1 billion, which exclude the federal benefits on state tax positions that were recorded as deferred income taxes. Included in our uncertain tax positions was \$181 million related to tax positions of NBCUniversal and NBCUniversal Enterprise for which we have been indemnified by GE. If we were to recognize the tax benefit for our uncertain tax positions in the future, \$600 million would impact our effective tax rate and the remaining amount would increase our deferred income tax liability. The amount and timing of the recognition of any such tax benefit is dependent on the completion of examinations of our tax filings by the various tax authorities and the expiration of statutes of limitations. In 2014, we reduced our accruals for uncertain tax positions and the related accrued interest on these tax positions and, as a result, our income tax expense decreased by \$759 million. It is reasonably possible that certain tax contests could be resolved within the next 12 months that may result in a decrease in our effective tax rate.

### Reconciliation of Unrecognized Tax Benefits

(in millions)	2016	2015	2014
Balance, January 1	\$ 1,136	\$ 1,171	\$ 1,701
Additions based on tax positions related to the current year	74	67	63
Additions based on tax positions related to prior years	67	98	111
Additions from acquired subsidiaries	13	—	—
Reductions for tax positions of prior years	(62)	(84)	(220)
Reductions due to expiration of statutes of limitations	(44)	(41)	(448)
Settlements with tax authorities	(81)	(75)	(36)
Balance, December 31	\$ 1,103	\$ 1,136	\$ 1,171

As of December 31, 2016 and 2015, our accrued interest associated with uncertain tax positions was \$483 million and \$510 million, respectively. As of December 31, 2016 and 2015, \$39 million and \$49 million, respectively, of these amounts were related to tax positions of NBCUniversal and NBCUniversal Enterprise for which we have been indemnified by GE.

During 2016, the IRS completed its examination of our income tax returns for the year 2014. Various states are examining our tax returns, with most of the periods relating to tax years 2000 and forward. The tax years of our state tax returns currently under examination vary by state.

Table of Contents**Comcast Corporation****Note 15: Supplemental Financial Information**

## Receivables

December 31 (in millions)	2016	2015
Receivables, gross	\$ 8,622	\$ 7,595
Less: Allowance for returns and customer incentives	417	473
Less: Allowance for doubtful accounts	250	226
Receivables, net	\$ 7,955	\$ 6,896

In addition to the amounts in the table above, as of December 31, 2016 and 2015, noncurrent receivables of \$939 million and \$721 million, respectively, are included in other noncurrent assets, net that primarily relate to the licensing of our television and film productions to third parties.

## Cash Payments for Interest and Income Taxes

Year ended December 31 (in millions)	2016	2015	2014
Interest	\$ 2,565	\$ 2,443	\$ 2,389
Income taxes	\$ 3,693	\$ 3,726	\$ 3,668

**Noncash Investing and Financing Activities**

## During 2016:

- we acquired \$1.3 billion of property and equipment and intangible assets that were accrued but unpaid
- we recorded a liability of \$653 million for a quarterly cash dividend of \$0.275 per common share paid in January 2017
- we recorded a liability for capital contributions for an investment that were accrued in December and paid in January 2017 (see Note 7 for additional information)

## During 2015:

- we acquired \$1.1 billion of property and equipment and intangible assets that were accrued but unpaid
- we recorded a liability of \$612 million for a quarterly cash dividend of \$0.25 per common share paid in January 2016
- we assumed liabilities related to the Universal Studios Japan transaction (see Note 5 for additional information)
- we used \$517 million of equity securities to settle a portion of our obligations under prepaid forward sale agreements

## During 2014:

- we acquired \$797 million of property and equipment and intangible assets that were accrued but unpaid
- we recorded a liability of \$572 million for a quarterly cash dividend of \$0.225 per common share paid in January 2015
- we used \$3.2 billion of equity securities to settle a portion of our obligations under prepaid forward sale agreements

## Table of Contents

### Comcast Corporation

#### Note 16: Commitments and Contingencies

##### Commitments

NBCUniversal enters into long-term commitments with third parties in the ordinary course of its business, including commitments to acquire film and television programming, obligations under various creative talent agreements, and various other television-related commitments. Many of NBCUniversal's employees, including writers, directors, actors, technical and production personnel, and others, as well as some of its on-air and creative talent, are covered by collective bargaining agreements or works councils. As of December 31, 2016, the total number of NBCUniversal full-time, part-time and hourly employees on its payroll covered by collective bargaining agreements was 8,500 full-time equivalent employees. Approximately 15% of these full-time equivalent employees were covered by collective bargaining agreements that have expired or are scheduled to expire during 2017.

We, through Comcast Spectacor, have employment agreements with both players and coaches of the Philadelphia Flyers. Certain of these employment agreements, which provide for payments that are guaranteed regardless of employee injury or termination, are covered by disability insurance if certain conditions are met.

The table below summarizes our minimum annual programming and talent commitments and our minimum annual rental commitments for office space, equipment and transponder service agreements under operating leases. Programming and talent commitments include acquired film and television programming, including U.S. broadcast rights to the Olympic Games through 2032, *Sunday Night Football* through the 2022-23 season, *Thursday Night Football* through the 2017-18 season, certain NASCAR events through 2024 and other programming commitments, as well as various contracts with creative talent.

As of December 31, 2016 (in millions)	Programming and Talent Commitments	Operating Leases
2017	\$ 5,222	\$ 517
2018	\$ 4,879	\$ 485
2019	\$ 3,503	\$ 433
2020	\$ 4,587	\$ 378
2021	\$ 3,177	\$ 321
Thereafter	\$ 20,847	\$ 1,873

The table below presents our rental expense charged to operations.

Year ended December 31 (in millions)	2016	2015	2014
Rental expense	\$ 744	\$ 608	\$ 580

##### Contractual Obligation

We are party to a contractual obligation that involves an interest held by a third party in the revenue of certain theme parks. The arrangement provides the counterparty with the right to periodic payments associated with current period revenue and, beginning in June 2017, the option to require NBCUniversal to purchase the interest for cash in an amount based on a contractual formula. The contractual formula is based on an average of specified historical theme park revenue at the time of exercise, which amount could be significantly higher than our carrying value. As of December 31, 2016, our carrying value was \$1.1 billion, and if the option had been exercisable as of December 31, 2016, the estimated value of the contractual obligation would have been approximately \$1.4 billion, based on inputs to the contractual formula as of that date.

##### Contingent Consideration

In June 2015, we settled a contingent consideration liability related to the acquisition of NBCUniversal, which was based upon future net tax benefits realized by us that would affect future payments to GE, for a payment

## Table of Contents

### **Comcast Corporation**

of \$450 million, which is included as a financing activity in our consolidated statement of cash flows. The settlement resulted in a gain of \$240 million, which was recorded to other income (expense), net in our consolidated statement of income.

#### **Redeemable Subsidiary Preferred Stock**

NBCUniversal Enterprise is a holding company that we control and consolidate whose principal assets are its interests in NBCUniversal Holdings. The NBCUniversal Enterprise preferred stock pays dividends at a fixed rate of 5.25% per annum. The holders have the right to cause NBCUniversal Enterprise to redeem their shares at a price equal to the liquidation preference plus accrued but unpaid dividends for a 30 day period beginning on March 19, 2020 and thereafter on every third anniversary of such date (each such date, a "put date"). Shares of preferred stock can be called for redemption by NBCUniversal Enterprise at a price equal to the liquidation preference plus accrued but unpaid dividends one year following the put date applicable to such shares. Because certain of these redemption provisions are outside of our control, the NBCUniversal Enterprise preferred stock is presented outside of equity under the caption "redeemable noncontrolling interests and redeemable subsidiary preferred stock" in our consolidated balance sheet. Its initial value was based on the liquidation preference of the preferred stock and is adjusted for accrued but unpaid dividends. As of December 31, 2016 and 2015, the fair value of the NBCUniversal Enterprise redeemable subsidiary preferred stock was \$741 million and \$758 million, respectively. The estimated fair values are based on Level 2 inputs that use pricing models whose inputs are derived primarily from or corroborated by observable market data through correlation or other means for substantially the full term of the financial instrument.

#### **Contingencies**

We are a defendant in several unrelated lawsuits claiming infringement of various patents relating to various aspects of our businesses. In certain of these cases other industry participants are also defendants, and also in certain of these cases we expect that any potential liability would be in part or in whole the responsibility of our equipment and technology vendors under applicable contractual indemnification provisions. We are also subject to other legal proceedings and claims that arise in the ordinary course of our business. While the amount of ultimate liability with respect to such actions is not expected to materially affect our results of operations, cash flows or financial position, any litigation resulting from any such legal proceedings or claims could be time-consuming and injure our reputation.

Table of Contents**Comcast Corporation****Note 17: Financial Data by Business Segment**

We present our operations in one reportable business segment for Cable Communications and four reportable business segments for NBCUniversal. The Cable Networks, Broadcast Television, Filmed Entertainment and Theme Parks segments comprise the NBCUniversal businesses and are collectively referred to as the NBCUniversal segments. Our financial data by reportable business segment is presented in the tables below. We do not present a measure of total assets for our reportable business segments as this information is not used by management to allocate resources and capital.

(in millions)	Revenue <sup>(f)</sup>	Operating Income (Loss) Before Depreciation and Amortization <sup>(g)</sup>	Depreciation and Amortization	Operating Income (Loss)	Capital Expenditures	Cash Paid for Intangible Assets
<b>2016</b>						
Cable Communications <sup>(a)(b)</sup>	\$ 50,048	\$ 20,109	\$ 7,670	\$ 12,439	\$ 7,596	\$ 1,377
NBCUniversal						
Cable Networks <sup>(c)</sup>	10,464	3,709	745	2,964	32	20
Broadcast Television <sup>(c)</sup>	10,147	1,320	125	1,195	153	19
Filmed Entertainment	6,360	697	47	650	33	16
Theme Parks	4,946	2,190	512	1,678	922	72
Headquarters and Other <sup>(d)</sup>	20	(699)	376	(1,075)	312	156
Eliminations <sup>(e)</sup>	(344)	10	—	10	—	—
NBCUniversal	31,593	7,227	1,805	5,422	1,452	283
Corporate and Other <sup>(b)</sup>	750	(874)	83	(957)	87	26
Eliminations <sup>(e)</sup>	(1,988)	(45)	—	(45)	—	—
<b>Comcast Consolidated</b>	<b>\$ 80,403</b>	<b>\$ 26,417</b>	<b>\$ 9,558</b>	<b>\$ 16,859</b>	<b>\$ 9,135</b>	<b>\$ 1,686</b>

(in millions)	Revenue <sup>(f)</sup>	Operating Income (Loss) Before Depreciation and Amortization <sup>(g)</sup>	Depreciation and Amortization	Operating Income (Loss)	Capital Expenditures	Cash Paid for Intangible Assets
<b>2015</b>						
Cable Communications <sup>(a)(b)</sup>	\$ 46,928	\$ 19,037	\$ 7,051	\$ 11,986	\$ 7,040	\$ 1,151
NBCUniversal						
Cable Networks	9,628	3,499	784	2,715	44	22
Broadcast Television <sup>(c)</sup>	8,530	780	111	669	117	17
Filmed Entertainment	7,287	1,234	26	1,208	14	20
Theme Parks	3,339	1,464	292	1,172	833	54
Headquarters and Other <sup>(d)</sup>	14	(625)	326	(951)	378	98
Eliminations <sup>(e)</sup>	(336)	—	—	—	—	—
NBCUniversal	28,462	6,352	1,539	4,813	1,386	211
Corporate and Other <sup>(b)</sup>	713	(815)	90	(905)	73	8
Eliminations <sup>(e)</sup>	(1,593)	104	—	104	—	—
<b>Comcast Consolidated</b>	<b>\$ 74,510</b>	<b>\$ 24,678</b>	<b>\$ 8,680</b>	<b>\$ 15,998</b>	<b>\$ 8,499</b>	<b>\$ 1,370</b>

Table of Contents**Comcast Corporation**

(in millions)	Revenue <sup>(f)</sup>	Operating Income (Loss) Before Depreciation and Amortization <sup>(g)</sup>	Depreciation and Amortization	Operating Income (Loss)	Capital Expenditures	Cash Paid for Intangible Assets
<b>2014</b>						
Cable Communications <sup>(a)(b)</sup>	\$ 44,165	\$ 18,097	\$ 6,436	\$ 11,661	\$ 6,156	\$ 979
NBCUniversal						
Cable Networks <sup>(c)</sup>	9,563	3,589	748	2,841	49	21
Broadcast Television <sup>(c)</sup>	8,542	734	127	607	76	12
Filmed Entertainment	5,008	711	21	690	11	7
Theme Parks	2,623	1,096	273	823	671	15
Headquarters and Other <sup>(d)</sup>	13	(613)	326	(939)	414	75
Eliminations <sup>(e)</sup>	(321)	(1)	—	(1)	—	—
NBCUniversal	25,428	5,516	1,495	4,021	1,221	130
Corporate and Other <sup>(b)</sup>	683	(763)	88	(851)	43	13
Eliminations <sup>(e)</sup>	(1,501)	73	—	73	—	—
<b>Comcast Consolidated</b>	<b>\$ 68,775</b>	<b>\$ 22,923</b>	<b>\$ 8,019</b>	<b>\$ 14,904</b>	<b>\$ 7,420</b>	<b>\$ 1,122</b>

(a) For the years ended December 31, 2016, 2015 and 2014, Cable Communications segment revenue was derived from the following sources:

	2016	2015	2014
Residential:			
Video	44.7%	45.9%	47.1%
High-speed Internet	27.0%	26.6%	25.6%
Voice	7.1%	7.7%	8.3%
Business services	11.0%	10.1%	9.0%
Advertising	5.0%	4.9%	5.4%
Other	5.2%	4.8%	4.6%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

Subscription revenue received from customers who purchase bundled services at a discounted rate is allocated proportionally to each service based on the individual service's price on a stand-alone basis.

For each of 2016, 2015 and 2014, 2.8% of Cable Communications revenue was derived from franchise and other regulatory fees.

- (b) Beginning in 2016, certain operations and businesses, including several strategic business initiatives, that were previously presented in Corporate and Other are now presented in our Cable Communications segment to reflect a change in our management reporting presentation. For segment reporting purposes, we have adjusted all periods presented to reflect this change.
- (c) The revenue and operating costs and expenses associated with our broadcast of the 2016 Rio Olympics and 2014 Sochi Olympics were reported in our Cable Networks and Broadcast Television segments. The revenue and operating costs and expenses associated with our broadcast of the 2015 Super Bowl were reported in our Broadcast Television segment.
- (d) NBCUniversal Headquarters and Other activities include costs associated with overhead, allocations, personnel costs and headquarter initiatives.
- (e) Included in Eliminations are transactions that our segments enter into with one another. The most common types of transactions are the following:
- our Cable Networks segment generates revenue by selling programming to our Cable Communications segment, which represents a substantial majority of the revenue elimination amount
  - our Broadcast Television segment generates revenue from the fees received under retransmission consent agreements with our Cable Communications segment
  - our Cable Communications segment generates revenue by selling advertising and by selling the use of satellite feeds to our Cable Networks segment
  - our Filmed Entertainment and Broadcast Television segments generate revenue by licensing content to our Cable Networks segment
- (f) Revenue from customers located outside of the United States, primarily in Europe and Asia, in 2016, 2015 and 2014 was \$6.5 billion, \$5.8 billion and \$4.4 billion, respectively. No single customer accounted for a significant amount of revenue in any period.
- (g) We use operating income (loss) before depreciation and amortization, excluding impairment charges related to fixed and intangible assets and gains or losses from the sale of assets, if any, as the measure of profit or loss for our operating segments. This measure eliminates the significant level of noncash depreciation and amortization expense that results from the capital-intensive nature of certain of our busi-

## Table of Contents

### Comcast Corporation

nesses and from intangible assets recognized in business combinations. Additionally, it is unaffected by our capital structure or investment activities. We use this measure to evaluate our consolidated operating performance and the operating performance of our operating segments and to allocate resources and capital to our operating segments. It is also a significant performance measure in our annual incentive compensation programs. We believe that this measure is useful to investors because it is one of the bases for comparing our operating performance with that of other companies in our industries, although our measure may not be directly comparable to similar measures used by other companies. This measure should not be considered a substitute for operating income (loss), net income (loss) attributable to Comcast Corporation, net cash provided by operating activities, or other measures of performance or liquidity we have reported in accordance with GAAP.

### Note 18: Quarterly Financial Information (Unaudited)

(in millions, except per share data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total Year
<b>2016</b>					
Revenue	\$ 18,790	\$ 19,269	\$ 21,319	\$ 21,025	\$ 80,403
Operating income	\$ 4,089	\$ 4,066	\$ 4,440	\$ 4,264	\$ 16,859
Net income attributable to Comcast Corporation <sup>(a)</sup>	\$ 2,134	\$ 2,028	\$ 2,237	\$ 2,296	\$ 8,695
Basic earnings per common share attributable to Comcast Corporation shareholders	\$ 0.88	\$ 0.84	\$ 0.93	\$ 0.96	\$ 3.61
Diluted earnings per common share attributable to Comcast Corporation shareholders	\$ 0.87	\$ 0.83	\$ 0.92	\$ 0.95	\$ 3.57
Dividends declared per common share	\$ 0.275	\$ 0.275	\$ 0.275	\$ 0.275	\$ 1.10
<b>2015</b>					
Revenue	\$ 17,853	\$ 18,743	\$ 18,669	\$ 19,245	\$ 74,510
Operating income	\$ 3,890	\$ 4,105	\$ 4,001	\$ 4,002	\$ 15,998
Net income attributable to Comcast Corporation	\$ 2,059	\$ 2,137	\$ 1,996	\$ 1,971	\$ 8,163
Basic earnings per common share attributable to Comcast Corporation shareholders	\$ 0.82	\$ 0.85	\$ 0.81	\$ 0.80	\$ 3.28
Diluted earnings per common share attributable to Comcast Corporation shareholders	\$ 0.81	\$ 0.84	\$ 0.80	\$ 0.79	\$ 3.24
Dividends declared per common share	\$ 0.25	\$ 0.25	\$ 0.25	\$ 0.25	\$ 1.00

(a) In the fourth quarter of 2016, net income attributable to Comcast Corporation included \$225 million, \$143 million net of tax, recognized in connection with the settlement of amounts owed to us under an agency agreement that had provided for, among other things, Verizon Wireless' sale of our cable services.

### Note 19: Condensed Consolidating Financial Information

Comcast ("Comcast Parent"), Comcast Cable Communications, LLC ("CCCL Parent") and NBCUniversal ("NBCUniversal Media Parent") have fully and unconditionally guaranteed each other's debt securities, including the Comcast revolving credit facility. The principal amount of debt securities within the guarantee structure total \$52.9 billion, of which \$12.3 billion will mature within the next five years.

Comcast Parent and CCCL Parent also fully and unconditionally guarantee NBCUniversal Enterprise's \$3.3 billion principal amount of senior notes, revolving credit facility and commercial paper program. NBCUniversal Media Parent does not guarantee the NBCUniversal Enterprise senior notes, revolving credit facility or commercial paper program.

Comcast Parent provides an unconditional subordinated guarantee of the \$185 million principal amount currently outstanding of Comcast Holdings' ZONES due October 2029. Neither CCCL Parent nor NBCUniversal Media Parent guarantee the Comcast Holdings' ZONES due October 2029. None of Comcast Parent, CCCL Parent nor NBCUniversal Media Parent guarantee the \$62 million principal amount currently outstanding of Comcast Holdings' ZONES due November 2029 or the \$3.3 billion of Universal Studios Japan term loans.

Table of Contents**Comcast Corporation**

## Condensed Consolidating Balance Sheet

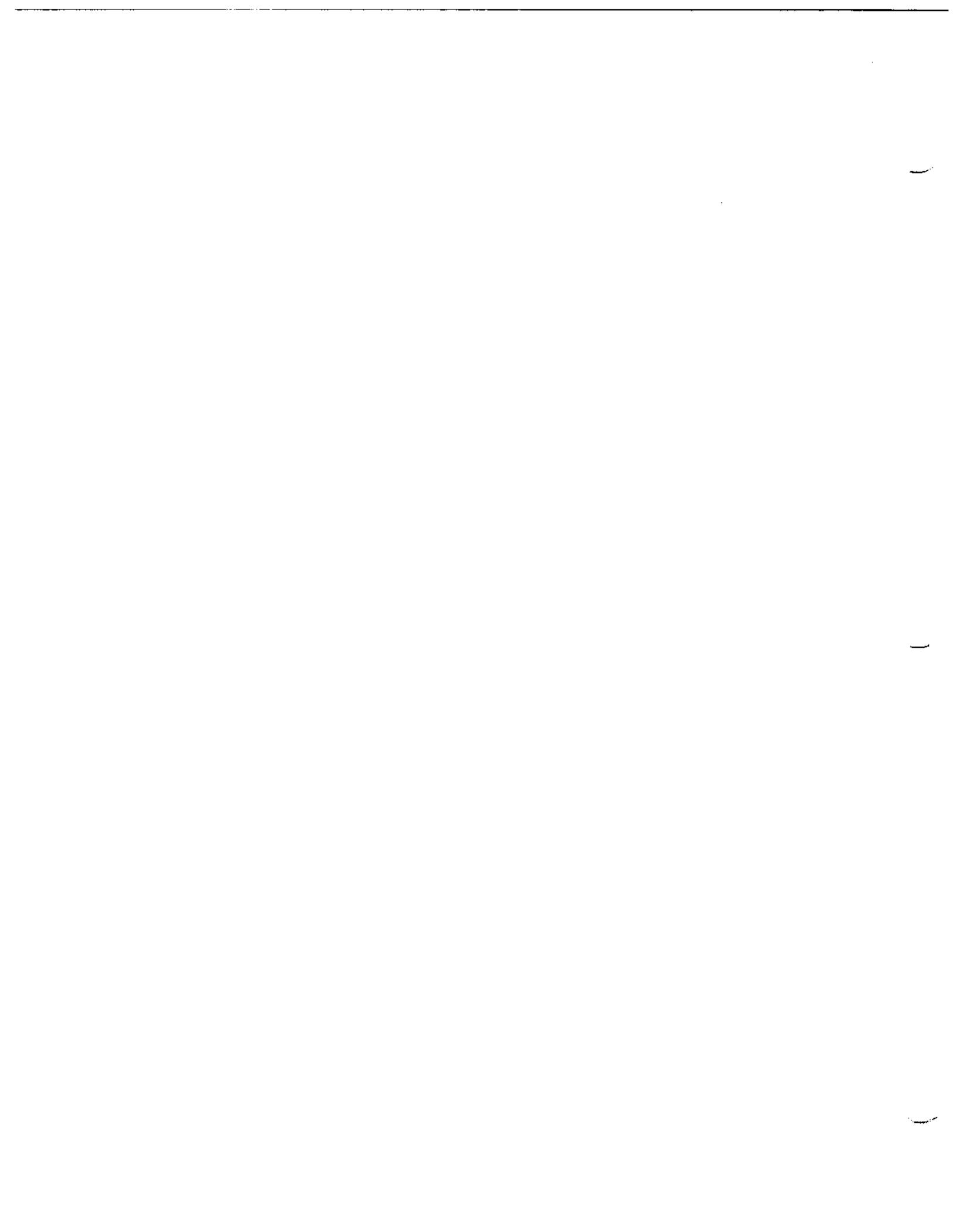
December 31, 2016 (in millions)	Comcast Parent	Comcast Holdings	CCCL Parent	NBCUniversal Media Parent	Non-Guarantor Subsidiaries	Elimination and Consolidation Adjustments	Consolidated Comcast Corporation
<b>Assets</b>							
Cash and cash equivalents	\$ —	\$ —	\$ —	\$ 482	\$ 2,819	\$ —	\$ 3,301
Receivables, net	—	—	—	—	7,955	—	7,955
Programming rights	—	—	—	—	1,250	—	1,250
Deposits	—	—	—	—	1,772	—	1,772
Other current assets	151	—	—	36	1,896	—	2,083
<b>Total current assets</b>	<b>151</b>	<b>—</b>	<b>—</b>	<b>518</b>	<b>15,692</b>	<b>—</b>	<b>16,361</b>
Film and television costs	—	—	—	—	7,252	—	7,252
Investments	75	—	—	651	4,521	—	5,247
Investments in and amounts due from subsidiaries eliminated upon consolidation	98,350	120,071	117,696	47,393	97,704	(481,214)	—
Property and equipment, net	298	—	—	—	35,955	—	36,253
Franchise rights	—	—	—	—	59,364	—	59,364
Goodwill	—	—	—	—	35,980	—	35,980
Other intangible assets, net	13	—	—	—	17,261	—	17,274
Other noncurrent assets, net	1,138	638	—	89	1,921	(1,017)	2,769
<b>Total assets</b>	<b>\$ 100,025</b>	<b>\$ 120,709</b>	<b>\$ 117,696</b>	<b>\$ 48,651</b>	<b>\$ 275,650</b>	<b>\$ (482,231)</b>	<b>\$ 180,500</b>
<b>Liabilities and Equity</b>							
Accounts payable and accrued expenses related to trade creditors	\$ 23	\$ —	\$ —	\$ —	\$ 6,892	\$ —	\$ 6,915
Accrued participations and residuals	—	—	—	—	1,726	—	1,726
Accrued expenses and other current liabilities	1,726	—	341	302	5,045	—	7,414
Current portion of long-term debt	3,739	—	550	4	1,187	—	5,480
<b>Total current liabilities</b>	<b>5,488</b>	<b>—</b>	<b>891</b>	<b>306</b>	<b>14,850</b>	<b>—</b>	<b>21,535</b>
Long-term debt, less current portion	38,123	141	2,100	8,208	6,994	—	55,566
Deferred income taxes	—	542	—	70	35,259	(1,017)	34,854
Other noncurrent liabilities	2,471	—	—	1,166	7,288	—	10,925
Redeemable noncontrolling interests and redeemable subsidiary preferred stock	—	—	—	—	1,446	—	1,446
Equity:							
Common stock	28	—	—	—	—	—	28
Other shareholders' equity	53,915	120,026	114,705	38,901	207,582	(481,214)	53,915
<b>Total Comcast Corporation shareholders' equity</b>	<b>53,943</b>	<b>120,026</b>	<b>114,705</b>	<b>38,901</b>	<b>207,582</b>	<b>(481,214)</b>	<b>53,943</b>
Noncontrolling interests	—	—	—	—	2,231	—	2,231
<b>Total equity</b>	<b>53,943</b>	<b>120,026</b>	<b>114,705</b>	<b>38,901</b>	<b>209,813</b>	<b>(481,214)</b>	<b>56,174</b>
<b>Total liabilities and equity</b>	<b>\$ 100,025</b>	<b>\$ 120,709</b>	<b>\$ 117,696</b>	<b>\$ 48,651</b>	<b>\$ 275,650</b>	<b>\$ (482,231)</b>	<b>\$ 180,500</b>

Table of Contents**Comcast Corporation****Condensed Consolidating Balance Sheet**

December 31, 2015 (in millions)	Comcast Parent	Comcast Holdings	CCCL Parent	NBCUniversal Media Parent	Non-Guarantor Subsidiaries	Elimination and Consolidation Adjustments	Consolidated Comcast Corporation
<b>Assets</b>							
Cash and cash equivalents	\$ —	\$ —	\$ —	\$ 414	\$ 1,881	\$ —	\$ 2,295
Receivables, net	—	—	—	—	6,896	—	6,896
Programming rights	—	—	—	—	1,213	—	1,213
Deposits	—	—	—	—	21	—	21
Other current assets	69	—	—	17	1,792	—	1,878
<b>Total current assets</b>	<b>69</b>	<b>—</b>	<b>—</b>	<b>431</b>	<b>11,803</b>	<b>—</b>	<b>12,303</b>
Film and television costs	—	—	—	—	5,855	—	5,855
Investments	33	—	—	430	2,761	—	3,224
Investments in and amounts due from subsidiaries eliminated upon consolidation	87,142	111,241	119,354	42,441	109,598	(469,776)	—
Property and equipment, net	210	—	—	—	33,455	—	33,665
Franchise rights	—	—	—	—	59,364	—	59,364
Goodwill	—	—	—	—	32,945	—	32,945
Other intangible assets, net	12	—	—	—	16,934	—	16,946
Other noncurrent assets, net	1,301	147	—	78	2,114	(1,368)	2,272
<b>Total assets</b>	<b>\$ 88,767</b>	<b>\$ 111,388</b>	<b>\$ 119,354</b>	<b>\$ 43,380</b>	<b>\$ 274,829</b>	<b>\$ (471,144)</b>	<b>\$ 166,574</b>
<b>Liabilities and Equity</b>							
Accounts payable and accrued expenses related to trade creditors	\$ 16	\$ —	\$ —	\$ —	\$ 6,199	\$ —	\$ 6,215
Accrued participations and residuals	—	—	—	—	1,572	—	1,572
Accrued expenses and other current liabilities	1,789	335	290	389	3,961	—	6,764
Current portion of long-term debt	1,149	—	—	1,005	1,473	—	3,627
<b>Total current liabilities</b>	<b>2,954</b>	<b>335</b>	<b>290</b>	<b>1,394</b>	<b>13,205</b>	<b>—</b>	<b>18,178</b>
Long-term debt, less current portion	31,106	130	2,650	8,211	6,897	—	48,994
Deferred income taxes	—	624	—	66	34,098	(1,222)	33,566
Other noncurrent liabilities	2,438	—	—	1,087	7,258	(146)	10,637
Redeemable noncontrolling interests and redeemable subsidiary preferred stock	—	—	—	—	1,221	—	1,221
Equity:							
Common stock	29	—	—	—	—	—	29
Other shareholders' equity	52,240	110,299	116,414	32,622	210,441	(469,776)	52,240
<b>Total Comcast Corporation shareholders' equity</b>	<b>52,269</b>	<b>110,299</b>	<b>116,414</b>	<b>32,622</b>	<b>210,441</b>	<b>(469,776)</b>	<b>52,269</b>
Noncontrolling interests	—	—	—	—	1,709	—	1,709
<b>Total equity</b>	<b>52,269</b>	<b>110,299</b>	<b>116,414</b>	<b>32,622</b>	<b>212,150</b>	<b>(469,776)</b>	<b>53,978</b>
<b>Total liabilities and equity</b>	<b>\$ 88,767</b>	<b>\$ 111,388</b>	<b>\$ 119,354</b>	<b>\$ 43,380</b>	<b>\$ 274,829</b>	<b>\$ (471,144)</b>	<b>\$ 166,574</b>

Table of Contents**Comcast Corporation****Condensed Consolidating Statement of Income**

For the Year Ended December 31, 2016 (in millions)	Comcast Parent	Comcast Holdings	CCCL Parent	NBCUniversal Media Parent	Non-Guarantor Subsidiaries	Elimination and Consolidation Adjustments	Consolidated Comcast Corporation
<b>Revenue:</b>							



**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**Form 10-K**

(Mark One)

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

For the fiscal year ended December 31, 2016

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 001-32408

**FairPoint Communications, Inc.**

(Exact name of registrant as specified in its charter)

<p style="text-align:center"><b>Delaware</b> (State or other jurisdiction of incorporation or organization)</p> <p style="text-align:center"><b>521 East Morehead Street, Suite 500</b> <b>Charlotte, North Carolina</b> (Address of principal executive offices)</p>	<p><b>13-3725229</b> (I.R.S. Employer Identification No.)</p> <p><b>28202</b> (Zip Code)</p>
---	--

Registrant's telephone number, including area code:  
(704) 344-8150

**Securities registered pursuant to Section 12(b) of the Act:**

Title of each class	Name of exchange on which registered
Common Stock, par value \$0.01 per share	The Nasdaq Stock Market LLC (Nasdaq Capital Market)

**Securities registered pursuant to Section 12(g) of the Act:**

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes  No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for

such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark 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	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company	<input type="checkbox"/>

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

The aggregate market value of the common stock of the registrant held by non-affiliates of the registrant as of June 30, 2016 (based on the closing price of \$14.68 per share) was \$384,049,851.

As of February 27, 2017, there were 27,266,570 shares of the registrant's common stock, par value \$0.01 per share, outstanding.

**FAIRPOINT COMMUNICATIONS, INC.**  
**ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2016**

**TABLE OF CONTENTS**

<u>Item Number</u>	<u>Page Number</u>
<b><u>PART I</u></b>	
1. Business	5
1A. Risk Factors	17
1B. Unresolved Staff Comments	31
2. Properties	31
3. Legal Proceedings	31
4. Mine Safety Disclosures	31
<b><u>PART II</u></b>	
5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	32
6. Selected Financial Data	34
7. Management's Discussion and Analysis of Financial Condition and Results of Operations	36
7A. Quantitative and Qualitative Disclosures About Market Risk	56
8. Financial Statements and Supplementary Data	57
9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure	95
9A. Controls and Procedures	95
9B. Other Information	95
<b><u>PART III</u></b>	
10. Directors, Executive Officers and Corporate Governance	96
11. Executive Compensation	100
12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	123
13. Certain Relationships and Related Transactions, and Director Independence	126
14. Principal Accounting Fees and Services	126
<b><u>PART IV</u></b>	
15. Exhibits, Financial Statement Schedules	128
16. Form 10-K Summary	128
Signatures	129
Exhibit Index	130

### CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

Some statements in this Annual Report on Form 10-K for the fiscal year ended December 31, 2016 (this "Annual Report") are known as "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These forward-looking statements include, but are not limited to, statements about our plans, objectives, expectations and intentions and other statements contained in this Annual Report that are not historical facts. When used in this Annual Report, the words "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates," "should," "could," "may," "will" and similar expressions are generally intended to identify forward-looking statements. Because these forward-looking statements involve known and unknown risks and uncertainties, there are important factors that could cause actual results, events or developments to differ materially from those expressed or implied by these forward-looking statements, including factors discussed under "Item 1A. Risk Factors" and other parts of this Annual Report and the factors set forth below:

- the timing and ability to complete the Merger (as defined below) with Consolidated Communications Holdings, Inc.;
- the outcome of legal and regulatory proceedings that have been, or may be, instituted following the announcement of our entering into the Merger Agreement (as defined below);
- risks that the Merger disrupts current plans and operations including potential impairments to our ability to retain and motivate key personnel;
- the possibility that the Merger is not consummated, including, but not limited to, due to the failure to satisfy the closing conditions;
- the diversion of management's attention from ongoing business operations and opportunities as a result of the Merger;
- the amounts of costs, fees, and expenses relating to the Merger;
- future performance generally and our share price as a result thereof;
- changes in strategic direction, including as a result of mergers, acquisitions or dispositions;
- restrictions imposed by the agreements governing our indebtedness;
- our ability to satisfy certain financial covenants included in the agreements governing our indebtedness;
- financing sources and availability, and future interest expense;
- our ability to repay or refinance our indebtedness;
- our ability to fund substantial capital expenditures;
- anticipated business development activities and future capital expenditures;
- the effects of regulation and enforcement, including changes in federal and state regulatory policies, procedures and their enforcement mechanisms including but not limited to the availability and levels of regulatory support payments and penalties associated with performance;
- our ability to satisfy our Connect America Fund ("CAF") Phase II obligations;
- adverse changes in economic and industry conditions, and any resulting financial or operational impact, in the markets we serve;
- labor matters, including workforce levels, our workforce reduction initiatives, labor negotiations and any resulting financial or operational impact;
- material technological developments and changes in the communications industry, including declines in access lines;
- disruption of our third party suppliers' provisioning of critical products or services;
- change in preference and use by customers of alternative technologies;
- the effects of competition on our business and market share;
- our ability to overcome changes to or pressure on pricing and their impact on our profitability;
- intellectual property infringement claims by third parties;
- failure of, or attack on, our information technology infrastructure;
- risks related to our reported financial information and operating results;
- availability of net operating loss ("NOL") carryforwards to offset anticipated tax liabilities;
- the impact of changes in assumptions on our ability to meet obligations to our company-sponsored qualified pension plans and other post-employment benefit plans;
- the impact of lump sum payments under certain of our company-sponsored qualified pension plans on future pension

contributions;

- the effects of severe weather events, such as hurricanes, storms, tornadoes and floods, terrorist attacks, cyber-attacks or other natural or man-made disasters; and
- changes in accounting assumptions that regulatory agencies, including the Securities and Exchange Commission (the "SEC"), may require or that result from changes in the accounting rules or their application, which could result in an impact on earnings.

You should not place undue reliance on such forward-looking statements, which are based on the information currently available to us and speak only as of the date on which this Annual Report is filed with the SEC. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, changes in our expectations or otherwise, except as required by law. However, your attention is directed to any further disclosures made on related subjects in our subsequent reports filed with the SEC on Forms 10-K, 10-Q and 8-K.

## PART I

### ITEM 1. BUSINESS

*Except as otherwise required by the context, references in this Annual Report to:*

- *"FairPoint Communications" refers to FairPoint Communications, Inc., excluding its subsidiaries.*
- *"FairPoint", the "Company", "we", "us" or "our" refer to the combined business of FairPoint Communications, Inc. and all of its subsidiaries after giving effect to the merger on March 31, 2008 with Northern New England Spinco Inc., a subsidiary of Verizon Communications Inc. ("Verizon"), which transaction is referred to herein as the "Spinco Merger".*
- *"Northern New England operations" refers to the local exchange business acquired from Verizon and certain of its subsidiaries after giving effect to the Spinco Merger.*
- *"Telecom Group" refers to FairPoint, exclusive of our acquired Northern New England operations.*
- *"Verizon New England" refers to the local exchange business of Verizon New England Inc. in Maine, New Hampshire and Vermont and the customers of Verizon and its subsidiaries' (other than Celco Partnership) related long distance and Internet service provider business in those states prior to the Spinco Merger.*
- *"Consolidated" refers to Consolidated Communications Holdings, Inc., a Delaware corporation.*

#### Our Business

We are a leading provider of advanced communications services to business, wholesale and residential customers within our service territories. We offer our customers a suite of advanced services including Ethernet, Session Initiation Protocol Trunking ("SIP-Trunking"), hosted Primary Branch Exchange ("hosted PBX"), managed services, data center colocation services, high capacity data transport and other IP-based services over our fiber-based network, in addition to Internet access, high-speed data ("HSD") and local and long distance voice services. Our service territory spans 17 states where we are the incumbent communications provider primarily serving rural communities and small urban markets. Many of our local exchange carriers ("LECs") have served their respective communities for more than 80 years. As of December 31, 2016, we operated with approximately 306,600 broadband subscribers, approximately 15,700 Ethernet circuits and approximately 366,100 residential voice lines.

We own and operate an extensive fiber-based Ethernet network with more than 22,000 miles of fiber optic cable, including approximately 18,000 miles of fiber optic cable in Maine, New Hampshire and Vermont, giving us capacity to support more HSD services and extend our fiber reach into more communities across the region. The IP/Multiple Protocol Label Switched ("IP/MPLS") network architecture of our fiber-based network allows us to provide Ethernet, transport and other IP-based services with the highest level of reliability at a lower cost of service. This fiber-based Ethernet network also supplies critical infrastructure for wireless carriers serving the region as their bandwidth needs increase, driven by mobile data from smartphones, tablets and other wireless devices. As of December 31, 2016, we provide cellular transport, also known as backhaul, through over 1,900 mobile Ethernet backhaul connections. We have fiber connectivity to approximately 1,300 cellular communications towers in our service footprint.

We were incorporated in New York in 1991 and reincorporated in Delaware in 1993 and grew through acquisitions. In March 2008, we completed the acquisition of the Northern New England operations from Verizon through the Spinco Merger. This acquisition significantly expanded our geographic platform in Maine, New Hampshire and Vermont.

#### Transformation of our Business

We have transformed our network and are aligning our communications services to meet changing customer preferences and communications requirements. Over the past few years, we have made significant capital investments in our fiber-based Ethernet network to expand our business service offerings to meet the growing data needs of our business customers and to increase broadband speeds and capacity in our consumer markets. We have also focused our sales and marketing efforts on these advanced data solutions. Specifically, we built and launched high capacity Ethernet services to allow us to meet the capacity needs of our business customers as well as supply high capacity infrastructure to our wholesale customers.

Business and wholesale customers have a growing demand for bandwidth and are converting from services such as Asynchronous Transfer Mode ("ATM") and Frame Relay and dedicated transport using T-1s to Ethernet-based products. Businesses are also looking to take advantage of the flexibility of voice services via Voice over Internet Protocol ("VoIP"). Residential customer trends have shown an increasing adoption and demand for higher speed broadband services while traditional voice services are giving way to wireless and alternative carriers. Our plan is to continue to add advanced data products and services that meet our



business and wholesale customers' needs while providing higher speed HSD options, attractive pricing features, appealing bundle offers and excellent customer service to our residential customer segment.

We have been successful in meeting the needs of our wireless carrier customers through our Fiber to the Tower ("FTTT") initiative. We have seen an increase in fiber backhaul from wireless carriers since late 2010 and now have approximately 1,300 cell towers served with fiber across our footprint. Our extensive fiber network of approximately 18,000 miles of fiber optic cable in Maine, New Hampshire and Vermont is a competitive advantage in delivering FTTT services.

We believe ongoing regulatory reforms in Maine, New Hampshire and Vermont will serve to promote fair competition among communications services providers in that region. We continue to believe that there is a significant organic growth opportunity within these business markets given our extensive fiber network and IP-based product suite combined with our relatively low business market share in these areas.

### **Proposed Merger with Consolidated Communications Holdings, Inc.**

On December 3, 2016, FairPoint Communications entered into an Agreement and Plan of Merger (the "Merger Agreement") with Consolidated and Falcon Merger Sub, Inc., a newly formed Delaware corporation and wholly-owned subsidiary of Consolidated ("Merger Sub"), which provides for, among other things, a business combination whereby Merger Sub will merge with and into FairPoint Communications, with FairPoint Communications as the surviving entity (the "Merger"). As a result of the Merger, the separate corporate existence of Merger Sub will cease, and FairPoint Communications will survive as a wholly owned subsidiary of Consolidated. Consolidated is a leading business and broadband communications provider throughout its 11-state service area.

If the Merger is completed, under the terms of the Merger Agreement, stockholders of FairPoint Communications will receive 0.7300 shares of common stock of Consolidated for each share of FairPoint Communications common stock that they own immediately before this transaction. The Merger is expected to close around the middle of 2017 and is subject to standard closing conditions, including federal and state regulatory approvals and the approval of both Consolidated's and FairPoint Communications' stockholders.

### **Generation of Revenue**

We offer a broad portfolio of services to meet the communications and technology needs of our customers, including bundling of services designed to simplify our customers' purchasing and management processes. Our basic offerings are outlined below.

See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report for more information regarding our revenue sources and financial results.

### **Data and Internet Services**

We believe data and Internet services are the cornerstone of our growth strategy for our business customers who require more advanced data solutions and our wholesale customers who experience capacity demands from their end users for higher speed services. We offer an extensive array of high capacity data services including: optical, Ethernet, IP services, Ethernet virtual circuit technology for cellular backhaul and private line special access services. We work with large businesses and carriers to deliver network capacity to meet their specific needs, including migrating networks from time division multiplexing to Ethernet-based high capacity circuits. Our portfolio also includes hosted PBX service over our Ethernet network. This service provides a cloud based voice offering for business customers. The service leverages our softswitch platform and uses a set of approved vendors for on-site hardware and maintenance support. Hosted PBX service allows us to continue to expand the services we offer to business customers, while leveraging our Ethernet network.

We offer internet access to both consumer and business customers through a variety of technologies leveraging both copper and fiber infrastructure, including digital subscriber line ("DSL"), dedicated fiber and lit buildings throughout our footprint. Certain of these services provide speeds up to 1 gigabit per second. In select markets, we also offer cable modem internet service, "Fiber to the Home" and wireless internet access.

Our data center colocation services offer businesses and public entities a physically secure, reliable location equipped with network connections to manage off-site disaster recovery, computing, storage and other IT equipment. Our customer data centers are strictly controlled, secured environments with the necessary power, cooling and connectivity resiliency to provide customer business continuity. These data centers enable organizations to quickly and cost-effectively scale and consolidate their IT systems to meet demand without incurring construction or excess staffing costs while maintaining control over management of both equipment and data.



## *Voice Services*

**Local Calling Services.** Local calling services enable the local customer to originate and receive an unlimited number of calls within a defined "exchange" area. Local calling services include basic local lines and local private lines. We provide local calling services to residential and business customers, generally for a fixed monthly charge and service charges for special calling features. In a LEC's territory, the amount that we can charge a customer for local service is generally determined by proceedings involving the appropriate state regulatory authorities.

**Long Distance Services.** We offer dedicated long distance services within our service areas on our network and through resale agreements with national interexchange carriers.

**9-1-1 Services.** We are a full service 9-1-1 provider and in the past three years have installed and now maintain two turn-key, state of the art statewide next-generation emergency 9-1-1 systems. These systems, located in Maine and Vermont, have processed over a million calls relying on the caller's location information for routing. Next-generation emergency 9-1-1 systems are an improvement over traditional 9-1-1 and provide the foundation to handle future communication modes such as texting and video.

## *Access*

**Network Transport Services.** We offer network transport services to wholesale customers for their use in connecting end users to the interexchange networks of the wholesale customer. These network transport services include high speed digital services, which are primarily Ethernet-based services provisioned over fiber and copper facilities, and special access services, which are primarily DS-1 and DS-3 services.

**Network Switched Access Service.** Network switched access service enables long distance companies to utilize our local network to originate or terminate intrastate and interstate communications. Network switched access charges relate to long distance, or toll calls, that typically involve more than one company in the provision of telephone service, as well as to the termination of interexchange private line services. Since toll calls and private line services are generally billed to the customer originating the call or ordering the private line service, a mechanism is required to compensate each company providing services relating to the service. This mechanism is the access charge and we bill access charges to long distance companies and other customers for the use of our facilities to access the customer, as described below. Network switched access compensation is subject to the Federal Communications Commission ("FCC") CAF/intercarrier compensation ("ICC") Order (referred to hereafter as the "CAF/ICC Order"), as described below in "Regulatory and Legislative." Under the rules adopted in 2011, network switched access revenues are expected to continue to decline, but on a more predictable basis with fewer disputes.

**Interstate Access Charges.** We generate interstate access revenue when an interstate long distance call is originated by a customer in one of our exchanges to a customer in another state, or when such a call is terminated to a customer in one of our exchanges. We also generate interstate access revenue when an interexchange carrier orders special access to connect interexchange private line services, such as HSD services, to a customer in one of our local exchanges. We bill interstate access charges in the same manner as we bill intrastate access charges as described below; however, interstate access charges are regulated and approved by the FCC instead of the state regulatory authority.

**Intrastate Access Charges.** We generate intrastate access revenue when an intrastate long distance call involving an interexchange carrier is originated by a customer in one of our exchanges to a customer in another exchange in the same state, or when such a call is terminated to a customer in one of our local exchanges. We also generate intrastate access revenue when an interexchange carrier orders special access to connect interexchange private line services to a customer in one of our local exchanges. The interexchange carrier pays us an intrastate access fee for either terminating or originating the communication. We bill access charges relating to such service through our carrier access billing system and receive the access payment from the interexchange carrier. Access charges for intrastate services are regulated and approved by the state regulatory authority and are also subject to the rate transitions ordered by the FCC in its CAF/ICC order.

## *Regulatory Funding*

We receive certain federal and state government funding that we classify as regulatory funding, which is further described in "Regulatory and Legislative" below, including: CAF Phase II support effective January 1, 2015 to build and operate broadband services; CAF Phase II transition funding (scheduled to phase down over three years); CAF Phase I frozen support (for Kansas and Colorado in 2015 and until a reverse auction is completed); CAF funding under the CAF/ICC Order and universal service fund support from certain states in which we operate.

From time to time we advocate for modifications or interpretations of state and federal regulations that could provide additional support funding to us for serving high cost areas. We do not know if any additional revenue will result from these advocacy efforts



or, if so, when or how much additional revenue may be available.

### ***Other Services***

We seek to capitalize on our LECs' local presence and network infrastructure by offering enhanced services to customers, including special purpose projects on behalf of third parties, video services (including cable television and video-over-DSL) and directory services, among others.

***Special Purpose Projects.*** Upon request from customers, we provide project-based implementation support services. These services are provided on a time and materials basis at the customer location as part of a larger FairPoint solution. This capability allows us to better serve our customers and assist in filling resource gaps they may encounter when implementing new communications plans.

### ***Our Markets***

We operate 83% of our total residential voice lines in Maine, New Hampshire and Vermont. We also provide local service in portions of Alabama, Colorado, Florida, Georgia, Illinois, Kansas, Massachusetts, Missouri, New York, Ohio, Oklahoma, Pennsylvania, Virginia and Washington. Within these 17 states, most of our LECs operate as the incumbent local exchange carrier ("ILEC").

### **Sales and Marketing**

With approximately 18,000 miles of fiber optic cable and 93% of our central offices enabled for Ethernet services we offer the largest such network in northern New England. Combined with our copper network, our infrastructure reaches approximately 95% of businesses in Maine, New Hampshire and Vermont. By investing in a dense, high-performing, scalable network, FairPoint has bandwidth and transport capacity to support enhanced applications, including fiber-based mobile and cloud-based communications, such as small cell wireless backhaul technology, VoIP, data storage, managed services and disaster recovery. Our marketing approach emphasizes the benefits of our advanced network while utilizing customer-oriented, locally-focused messages that resonate by community and by customer segment.

Our focus on the individual communities we serve in our 17 state footprint stems from the expertise of approximately 2,500 employees who predominantly work and live in the markets where we provide service, as well as our belief that many customers in our territory prefer to do business locally. We view our visible local presence as a competitive differentiator because it enables a prompt and locally relevant approach to opportunities and challenges in sales and service, operations, and marketing. As a result, we often leverage the heritage of the LECs in our service areas and the brand recognition that our long history of service provides.

We tailor our marketing offers, messaging and tactics to be effective and efficient for each customer audience using both call center and direct sales channels. Residential customers, who make up the largest part of our customer base, are directed to customer sales and service call centers based in the markets we serve. As we seek continued growth in business services, we leverage local call centers for sales and service efficiency among our small-office and home-office clientele, as well as a direct sales force that is trained to develop advanced, customized voice and data solutions. The direct sales force that focuses on small and medium businesses dedicates representatives to exclusive geographic territories and encourages involvement in the local business community during and after hours. The direct sales force that focuses on large and enterprise business utilizes both a geographic territory assignment and a named account program. The government, education and wholesale teams utilize a named account approach, focusing on specific new and existing customers.

We maintain teams of local sales support staff and experienced sales engineers who can design the right solution for each organization and guide new customers during the pre- and post-sales process. Support teams are customized based on account size and product set, and dedicated representatives are on call to answer questions, troubleshoot if necessary, and serve as a conduit to much broader resources, options and support, including our in-market Network Operations Center. We also place an emphasis on customer satisfaction and retention, with certain representatives focusing on maintaining existing customer relationships.

### **Information Technology and Support Systems**

We have a customer-focused approach to information technology ("IT") which allows for efficient business operations and supports revenue growth. Our approach is to simplify and standardize processes in order to optimize the benefits of our back-office and operation support systems. Specifically, our "simplify and optimize" initiative targets the reduction of redundant and manual processes to reduce cycle times, improve efficiency and deliver enhanced customer service.

Our back-office and operations support systems are a combination of integrated off-the-shelf packages that have been customized to support our operations. Both our Northern New England and Telecom Group access billing operations are supported by outsourced third-party platforms.



Our systems are supported by a combination of employees and contractors. Our internal IT group supports data center operations, data network operations, internal help desk, desktop support and phases of the systems development life cycle. We use professional services firms for the majority of software development and maintenance.

### **Network Architecture and Technology**

Rapid and significant changes in technology continue in the communications industry. Our success depends, in part, on our ability to anticipate and adapt to technological changes. With this in mind, we continue to evolve and expand our advanced fiber-based Ethernet network in our Northern New England operations, which is an IP/MPLS network operating on a fiber transport infrastructure that has approximately 18,000 miles of fiber optic cable. This network is the largest IP/MPLS based network in northern New England. We have made significant investments in our fiber optic network to expand our business service offerings to meet the growing needs of our customers and to increase broadband speeds and capacity in our consumer markets. We expect to continue to invest in expanding the reach of our fiber network to connect directly to customers' premises, cellular towers and data centers. We monitor the fiber-based Ethernet network utilization and augment capacity as needed to avoid network problems. We believe this network architecture will enable us to efficiently respond to these technological changes.

Our fiber-based network transport systems in our Northern New England operations and our Telecom Group are a combination of Synchronous Optical Network, Dense Wave Division Multiplexing and Ethernet transport capable of satisfying customer demand for high speed bandwidth transport services. This system supports advanced services, including carrier Ethernet services and legacy data products, such as Frame Relay and ATM, facilitating delivery of advanced services as demand warrants.

In our LEC markets, DSL-enabled access technology has been deployed to provide significant broadband capacity to our customers. As of December 31, 2016, all of our central offices are capable of providing broadband services through DSL technology, cable modem and/or wireless broadband.

Our LEC network consists of 93 host central offices and 412 remote central offices, all with digital switches. Approximately 99% of our central offices are served by fiber optic facilities, which we own. The primary interconnection with other incumbent carriers is also fiber optic. Our outside plant consists of both fiber optic and copper distribution networks.

### **Competition**

The communications industry is comprised of companies involved in the transmission of voice, data and video communications over various media and through various types of technologies. The competitive environment continues to intensify as consumers and businesses are provided more options for a variety of services, pricing and service quality. Presently, there are four predominant types of local telephone service providers, or carriers, in the communications industry: ILECs, CLECs, cable companies and wireless carriers. ILECs, which the majority of our 32 LECs operate as, were the traditional monopoly providers of the local telephone service prior to the passage of the Telecommunications Act of 1996 (the "1996 Act"). A CLEC is a competitor to local telephone companies that has been granted permission by a state regulatory commission to offer local telephone service in an area already served by an ILEC. CLECs typically offer voice and data services to their customers. Cable companies are the traditional video distribution providers in the market and are now selling packages of voice and data services along with their video services. Wireless competitors also have a significant presence in most markets, offering local and long distance voice services, along with mobile data offerings. As a result, competition in local exchange service areas for voice and data services has increased and is expected to continue to increase from these competitors.

Overall, we face intense competition from a variety of sources for our voice and data services in most of the areas we now serve, many of whom have greater resources and access to capital, and we expect that such competition will continue to intensify in the future. This competition has had an adverse impact on our access lines, broadband subscribers and revenues.

Regulations and technology change quickly in the communications industry, and these changes have historically had, and are expected to continue in the future to have, a significant impact on competitive dynamics. For instance, the ubiquity of wireless networks, coupled with technology changes, such as VoIP and data-driven devices (e.g., smartphones and computer tablets), is creating increased competition and technology substitution, a trend we expect will continue for the foreseeable future. Public monies in the form of stimulus funds to build broadband networks are also providing a new source of competition for us. In addition, many of our competitors have access to larger workforces or have substantially greater name-brand recognition and financial, technological and other resources than we do. Moreover, some of our competitors, including wireline, wireless and cable, have formed and may continue to form strategic alliances to offer bundled services in our service areas.

We estimate that, as of December 31, 2016, most of the customers that we serve have access to voice, network transport, video services and Internet services through a cable company. Increasingly, both CLECs and cable companies have begun to penetrate the market for high capacity circuits for large businesses and carriers, including interexchange and wireless providers.



In most of our service areas, we face competition from wireless carriers for voice and mobile data services. A large portion of households in the United States have moved to a wireless only model. Wireless carriers, particularly those that provide unlimited wireless service plans with no additional fees for long distance, offer customers a substitution service for our access lines and are becoming an increasing threat to our local voice line business. In addition, wireless companies continue to expand their high-speed Internet offerings, which have resulted in more intense competition for our high-speed Internet customers. Additionally, traditional wireline applications, such as home security systems, are now moving to IP-based models, leveraging an Internet connection in place of a traditional phone line. Although there are unique benefits of our wireline phone service, such as land lines remaining active in the event of a home power outage, we expect continued migration to IP-based and wireless voice services.

We are actively addressing our competitive environment with a multi-faceted approach to increase our market share. This approach is comprised of acquisition programs and new product introductions, retention programs, win-back and upsell initiatives.

Our relatively low current market share provides us the opportunity to both win back business customers who have left for another carrier as well as acquire new business. In order to better address the needs of our customers and prospects, we segment them across specific channels. Our focus for residential customers is to drive increasing penetration of high speed data customers. We are upgrading our access infrastructure to provide higher speed internet access services via high capacity copper and fiber facilities to more customers and communities each year. We are focusing on promotional programs that allow us to differentiate from cable operators, including price lock and multi-year discount programs. We believe bundled services continue to provide value to customers and, as such, we package our services in a range of price points.

In the business and government segments, our fiber-based network with approximately 18,000 miles of fiber, allows us to deliver Ethernet and fiber based data services typically ranging from 1 megabit per second to 1 gigabit per second. Along with our high capacity data services, we offer competitively priced voice services through VoIP or time division multiplexing ("TDM"). Our three contiguous state footprint in northern New England, allows businesses with multi-state locations to work with one local vendor. Our geographic coverage and extensive fiber network is an attractive feature for our wholesale customers, such as wireless carriers seeking cell tower backhaul services, and national carriers seeking middle and last mile solutions.

We have a multi-channel retention team, responsible for developing and executing customer retention programs across all areas of FairPoint. In addition, we have initiated proactive programs to address customers coming off of promotions and term contracts. Through early intervention, we expect to reduce churn and retain customers longer.

See "Regulatory and Legislative" below and "Item 1A. Risk Factors" included elsewhere in this Annual Report for more information regarding the competition that we face.

## **Employees**

As of December 31, 2016, we employed approximately 2,500 employees, approximately 1,500 of whom were covered by 13 collective bargaining agreements. Our agreements with the International Brotherhood of Electrical Workers ("IBEW") and the Communications Workers of America ("CWA") in northern New England covering approximately 1,300 employees in the aggregate expire in August 2018.

## **Intellectual Property**

We believe we own or have the right to use all of the intellectual property that is necessary for the operation of our business as we currently conduct it.

## **Regulatory and Legislative**

We are generally subject to common carrier regulation primarily by federal and state governmental agencies. At the federal level, the FCC generally exercises jurisdiction over common carriers, such as us, to the extent those carriers provide, originate or terminate interstate or international communications. State regulatory commissions generally exercise jurisdiction over common carriers to the extent those carriers provide, originate or terminate intrastate telecommunications. In addition, pursuant to the Telecommunications Act of 1996, which amended the Communications Act of 1934 (as amended, the "Communications Act"), state and federal regulators share responsibility for implementing and enforcing the domestic pro-competitive policies introduced by that legislation.

We are required to comply with the Communications Act, which requires, among other things, that common carriers offer communications services at just and reasonable rates and on terms and conditions that are not unreasonably discriminatory. The Communications Act also contains requirements intended to promote competition in the provision of local services and lead to deregulation as markets become more competitive.

The FCC's CAF/ICC Order (as defined herein and sometimes referred to in the industry as the "Transformation Order") modified regulation for us beginning January 1, 2012. Effective January 1, 2012, the FCC eliminated the rural/non-rural distinction among ILECs and treats ILECs as either price cap or rate-of-return. Effective January 1, 2012, all of our ILECs are treated as price cap companies for CAF purposes, including the Telecom Group rate-of-return companies. However, the Telecom Group rate-of-return companies continue to be treated as rate-of-return for regulation of interstate switched and special access services. In addition, the FCC has preempted certain state regulation over our ILECs, including capping all state originating and terminating switched access charges and reducing terminating state switched access charges beginning July 1, 2012, in a two-year transition to make state switched access charges equal to interstate switched access charges. Starting July 1, 2014, all terminating usage rates have begun to transition to zero over the following four to seven years. As usage rates decrease under the FCC transition rules, resulting in decreased intercarrier compensation, carriers are allowed to increase end user access recovery charges to offset a substantial portion of the revenue losses. The impact of these changes for 2016 is described further below. However, in the long run, we are uncertain of the ultimate impact as federal and state regulations continue to evolve.

#### *Overview of FCC CAF/ICC Order to Reform Universal Service and Intercarrier Compensation*

On March 16, 2010, the FCC submitted the National Broadband Plan ("NBP") to the United States Congress. The NBP is a plan to bring high-speed Internet services to the entire country, including remote and high-cost areas. In accordance with the NBP, the FCC commenced several rulemakings that concern, among other things, reforming high-cost and low-income programs to promote universal service to make those funds more efficient while promoting broadband communications in areas that otherwise would be unserved and to address changes to interstate access charges and other forms of ICC.

On November 18, 2011, the FCC released its comprehensive landmark order to modify the nationwide system of universal support and the ICC system (the "CAF/ICC Order"). In this order, the FCC replaced all existing USF for price cap carriers with its CAF. The intent of CAF is to bring high-speed affordable broadband services to all Americans. The CAF/ICC Order fundamentally reforms the ICC process that governs how communications companies bill one another for exchanging traffic, gradually phasing down these charges.

In conjunction with the CAF/ICC Order, the FCC adopted a Notice of Proposed Rulemaking to deal with related matters, including but not limited to: (i) the actual cost model to be adopted for CAF Phase II funding, (ii) treatment of originating access charges, (iii) modifications to CAF for rate-of-return ILECs, (iv) development of CAF Phase II for mobility, (v) CAF Phase II competitive bidding rules, (vi) remote areas funding and (vii) IP to IP interconnection issues. In its Order released December 18, 2014, the FCC stated its intention to extend its offer of CAF Phase II support to price cap carriers in early 2015 and to implement the CAF Phase II program for price cap carriers during 2015. On April 29, 2015, the FCC released a Public Notice extending the offer of CAF Phase II funding to price cap carriers, as described in more detail below. As of year-end 2016, the FCC has issued competitive bidding guidelines but has not finalized rules for the competitive bidding process. It is not known how these rules may impact us.

**CAF Phase I and Phase II Support.** Pursuant to the CAF/ICC Order, beginning in 2012, we started receiving monthly CAF Phase I frozen support, which is based on and equal to all forms of USF high-cost support we received during 2011. This support was considered transitional funding while the FCC developed its CAF Phase II program. FCC rules required that if we continued receiving CAF Phase I frozen support beyond 2012, which we have, we would have specific broadband spending obligations starting in 2013, which we did and have met. According to the FCC rules, in 2013, we were required to spend, and did spend, one-third of the frozen support to "build and operate broadband-capable networks used to offer the provider's own retail broadband service in areas substantially unserved by an unsubsidized competitor." According to the FCC rules, in 2014, we were required to spend, and did spend, two-thirds of the frozen support to "build and operate broadband-capable networks used to offer the provider's own retail broadband service in areas substantially unserved by an unsubsidized competitor." For the CAF Phase I frozen support we receive, this spending obligation increased to 100% of the frozen support received in 2015 and subsequent years to "build and operate broadband-capable networks used to offer the provider's own retail broadband service in areas substantially unserved by an unsubsidized competitor." We were in compliance with the 2016 spending obligation and expect to be in compliance in 2017.

In a Public Notice released on April 29, 2015, the FCC extended an offer of CAF Phase II support to price cap carriers to fund the building and operation of voice and broadband-capable services in their service territories. In this Public Notice, the FCC offered \$38.2 million of annual funding to us for six years in return for providing broadband services to a specified number of locations in eligible census blocks specified by the FCC. This compares with \$39.3 million in annual CAF Phase I frozen funding that we received in 2014. On August 18, 2015, we announced our acceptance of \$37.4 million in annual CAF Phase II support, which was effective retroactive to January 1, 2015. This includes support in all our operating states except Colorado and Kansas where we declined the offered CAF Phase II support.

The specific obligations associated with CAF Phase II funding include the obligation to serve approximately 105,000 locations in approximately 16,000 census blocks by December 31, 2020 (with interim milestones of 40%, 60% and 80% completion by



December 2017, 2018 and 2019, respectively); to provide broadband service to those locations with speeds of 10 megabits per second down and 1 megabit per second up; to achieve latency of less than 100 milliseconds; to provide data of at least 100 gigabytes per month; and to offer pricing reasonably comparable to pricing in urban areas.

For the two states where we declined CAF Phase II support, we will continue to receive CAF Phase I frozen support until such time as the FCC conducts a competitive bidding process. We expect the FCC to conduct the competitive bidding process during 2017. The FCC has determined that price cap carriers declining CAF Phase II support can participate in the competitive bidding process along with any other interested carriers. As of December 31, 2016, the FCC has not yet adopted final rules governing the competitive bidding process.

In addition, there is a three year transition for price cap carriers that choose to accept model-based support in states where the accepted support is less than the CAF Phase I frozen support. The determination of transition funding is made at the state level. From January 1, 2015 to July 31, 2015, and as prescribed by the FCC, such carriers received 100% of the difference between the annualized amount of CAF Phase II support that they accepted and the amount of CAF Phase I frozen support that they received in 2014. Beginning August 1, 2015, transitional funding stepped down to 75% of that amount and on August 1, 2016 transitional funding stepped down to 50% of the difference. On August 1, 2017 transitional funding steps down to 25% of the difference. Transitional support will terminate as of July 31, 2018, after which time carriers will receive only CAF Phase II support.

As prescribed by the FCC's transitional plan and the transitional funding calculation, we have recognized or expect to recognize transitional funding, in addition to the \$37.4 million annual CAF Phase II funding, based on the following schedule:

- January 1, 2015 - July 31, 2015: \$824,000 per month in transitional funding
- August 1, 2015 - July 31, 2016: \$618,000 per month in transitional funding
- August 1, 2016 - July 31, 2017: \$412,000 per month in transitional funding
- August 1, 2017 - July 31, 2018: \$206,000 per month in transitional funding
- August 1, 2018 and after: no transitional funding

**FCC Rules for ICC Process.** The CAF/ICC Order reformed rules associated with local, state toll and interstate toll traffic exchanged among communications carriers including ILECs, CLECs, cable companies, wireless carriers and VoIP providers. The revised rules, the majority of which were effective beginning July 1, 2012, establish separate rules for price cap carriers and rate-of-return carriers. Although the FCC order treats our rate-of-return carriers (including companies operating under average schedules) as price cap carriers for CAF funding, it treats them as rate-of-return carriers for purposes of ICC reform. For both price cap and rate-of-return carriers, the FCC established a multi-year transition of terminating traffic compensation to "bill and keep", or zero compensation. For both price cap and rate-of-return carriers, the FCC required carriers to establish fiscal year 2011 ("FY2011") baseline compensation, which was the amount of relevant compensation billed during the period beginning October 1, 2010 and ending September 30, 2011, and collected by March 31, 2012. This FY2011 revenue was used as a starting point for revenue for the transitional period, which is six years for price cap operations and nine years for rate-of-return operations. For each FairPoint ILEC, the FY2011 baseline revenue is reduced by a specified percent during each year of the transition, resulting in a target revenue for each tariff year of the transitional period. At the same time, the FCC rules require reductions in ICC rates for specified services and jurisdictions. As the recoverable revenue declines and the rates decline, any target revenue which will not be covered by ICC revenue can be recovered, in part, from end users through an access recovery charge ("ARC"). Price cap ILECs are permitted to implement monthly end user ARCs with five annual increases of no more than \$0.50 for residential/single-line business consumers, for a total monthly ARC of no more than \$2.50 in the fifth year; and no more than \$1.00 (per month) per line for multi-line business customers, for a total of \$5.00 (per month) per line in the fifth year, provided that: (1) any such residential increases would not result in regulated residential end user rates that exceed the \$30.00 residential rate ceiling; and (2) any multi-line business customer's total subscriber line charge ("SLC") plus ARC does not exceed \$12.20. Rate-of-return ILECs are permitted to implement monthly end user ARCs with six annual increases of no more than \$0.50 (per month) for residential/single-line business consumers, for a total ARC of no more than \$3.00 in the sixth year; and no more than \$1.00 (per month) per line for multi-line business customers for a total of \$6.00 (per month) per line in the sixth year, provided that: (1) such increases would not result in regulated residential end user rates that exceed the \$30.00 Residential Rate Ceiling; and (2) any multi-line business customer's total SLC plus ARC does not exceed \$12.20. We began billing the ARC charges for our price cap and rate of return companies in July 2012 as outlined by the rules above. If the combination of ICC and ARC revenue is not sufficient to cover the targeted revenue, then additional funding will be provided by the CAF in certain circumstances, though there is no guarantee that the ILEC will be made whole.

#### *Access Charges*

Our local exchange subsidiaries receive compensation from long distance communications providers for the use of our subsidiaries' network to originate and terminate state and interstate interexchange traffic. With respect to interstate traffic, the FCC regulates the prices we may charge for this purpose, referred to as access charges, as a combination of flat monthly charges paid by end users, usage sensitive charges paid by long distance carriers and recurring monthly charges for use of dedicated facilities paid by long distance carriers. Intrastate access charges are regulated by the state commissions. The amount of access charge



revenue that we will receive is subject to change. The FCC has adopted, in its CAF/ICC Order, a plan to resolve certain billing disputes related to ICC and to transition all terminating state and interstate ICC to zero over a six or nine year period for price cap and rate-of-return companies, respectively.

The FCC's CAF/ICC Order significantly changes the existing rates for access charges, which, combined with the increase in competition, have generally caused the aggregate amount of switched access charges paid by long distance carriers to decrease over time. The FCC, in a separate proceeding, is considering whether to modify price cap rules as they apply to special access and whether to restrict some of the pricing flexibility enjoyed by price cap ILECs, which includes some of our Northern New England operations. We cannot predict what changes, if any, the FCC may eventually adopt and the effect that any of these changes may have on our business.

### *Universal Service Regulation*

**Universal Service Fund Support.** We benefit indirectly from support to low-income users under the Lifeline and Linkup universal service programs. Effective April 1, 2012, the Linkup program was eliminated for all low-income subscribers except for Native Americans. Currently Linkup pays 100% of the non-recurring installation charges, not to exceed \$100.00, associated with establishment of local telecommunications service for qualified subscribers in Tribal areas. Also effective April 1, 2012, there were major reforms to the Lifeline program. Prior to the changes, Lifeline credits were based on four tiers of support. The first three tiers of federal support were replaced by a flat credit of \$9.25 per month. The fourth tier, which relates to Native Americans, is unchanged. In addition, the FCC established revised eligibility criteria effective April 1, 2012. The revised eligibility criteria established in 2012 resulted in a reduction in lines eligible for Lifeline credits. The FCC order required the Universal Service Administration Company to establish a national database, now known as the National Lifeline Accountability Database (NLAD), which is used to eliminate duplicate funding. The elimination of duplicate support could result in fewer customers choosing us for Lifeline service, with the potential that a portion of our Lifeline customers may prefer to use other carriers for this service.

**Universal Service Contributions.** Federal universal service programs are currently funded through a surcharge on interstate and international end user telecommunications revenues. Declining long distance revenues, the popularity of service bundles that include local and long distance services, and the growth in size of the fund, due primarily to increased funding to competitive ETCs, all prompted the FCC to consider alternative means for collecting this funding. As an interim step, the FCC has ordered that providers of certain VoIP services must contribute to federal universal service funding. The FCC also increased the percentage of revenues subject to federal universal service contribution obligations that wireless providers may use as their methodology for funding universal service. We cannot predict whether the FCC or Congress will require modification to any of the universal service contribution rules, or the ultimate impact that any such modification might have on us or our customers.

### *Local Service Competition*

The 1996 Act provides, in general, for the removal of barriers to market entry in order to promote competition in the provision of local communications and information services. As a result, competition in our local exchange service areas will continue to increase from CLECs, wireless providers, cable companies, Internet service providers, electric companies and other providers of network services. Many of these competitors have a significant market presence and brand recognition, which could lead to more competition and a greater challenge to our future revenue growth.

Under the 1996 Act, all LECs, including both ILECs and CLECs, are required to: (i) allow others to resell their services, (ii) ensure that customers can keep their telephone numbers when changing carriers, referred to as local number portability, (iii) ensure that competitors' customers can use the same number of digits when dialing and receive nondiscriminatory access to telephone numbers, operator service, directory assistance and directory listing, (iv) ensure competitive access to telephone poles, ducts, conduits and rights of way and (v) compensate competitors for the cost of completing calls to competitors' customers from the other carrier's customers.

In addition to these obligations, ILECs are subject to additional requirements to: (i) interconnect their facilities and equipment with any requesting telecommunications carrier at any technically feasible point, (ii) unbundle and provide nondiscriminatory access to certain network elements, referred to as unbundled network elements ("UNEs"), including some types of local loops and transport facilities, at regulated rates and on nondiscriminatory terms and conditions, to competing carriers that would be "impaired" without them, (iii) offer their retail services for resale at wholesale rates, (iv) provide reasonable notice of changes in the information necessary for transmission and routing of services over the ILEC's facilities or in the information necessary for interoperability and (v) provide, at rates, terms and conditions that are just, reasonable and nondiscriminatory, for the physical co-location of equipment necessary for interconnection or access to UNEs at the ILEC's premises. Competitors are required to compensate the ILEC for the cost of providing these services. On December 28, 2015, the FCC granted forbearance from some UNE requirements, finding that ILECs may no longer be required to offer bundled access to a 64-kps-voice channel when they replace copper loops with fiber. This is intended to facilitate copper replacement but we cannot predict whether we will benefit from this rule change.



Our Telecom Group rural operations are exempt from the ILEC requirements until the applicable rural carrier receives a bona fide request for these additional services and the applicable state authority determines that the request is not unduly economically burdensome, is technically feasible and is consistent with the universal service objectives set forth in the 1996 Act. This exemption is effective for all of the Telecom Group operations, except in Florida where the legislature has determined that all ILECs are required to provide the additional services as prescribed in the 1996 Act. Loss of a rural exemption by one or more of the Telecom Group operating companies could be achieved if the state commission grants such a petition filed by a competitor. Loss of the rural exemption would potentially expose the operation to additional local competition.

### *Long Distance Operations*

The FCC has required that ILECs that provide interstate long distance services originating from their local exchange service territories must do so in accordance with "non-structural separation" rules. These rules have required that our long distance affiliates (i) maintain separate books of account, (ii) not own transmission or switching facilities jointly with the local exchange affiliate and (iii) acquire any services from their affiliated LEC at tariffed rates, terms and conditions. Our Northern New England operations, which are Bell Operating Companies, are subject to a different set of rules allowing them to offer both long distance and local exchange services in the regions where they operate as Bell Operating Companies, subject to certain conditions with which we comply. Not all of our competitors must comply with these requirements. Therefore, these requirements may put us at a competitive disadvantage in the interstate long distance market.

### *Other Obligations under Federal Law*

We are subject to a number of other statutory and regulatory obligations at the federal level. For example, the Communications Assistance for Law Enforcement Act ("CALEA") requires telecommunications carriers to modify equipment, facilities and services to allow for authorized electronic surveillance based on either industry or FCC standards. Under CALEA and other federal laws, we may be required to provide law enforcement officials with call records, content or call identifying information, pursuant to an appropriate warrant or subpoena.

The FCC limits how carriers may use or disclose customer proprietary network information ("CPNI") and specifies what carriers must do to safeguard CPNI provided to third parties. Congress, as well as some state legislatures, has enacted legislation to criminalize the unauthorized sale of call detail records and to further restrict the manner in which carriers make such information available.

The Communications Act requires all ILECs to provide competing providers of telecommunications services access to poles, ducts, conduits and rights-of-way at regulated rates. In December 2015, the FCC decided to forbear from enforcing this requirement with respect to newly deployed entrance facility conduit on commercial property. We must continue providing access where we have existing facilities.

In addition, if we seek in the future to acquire companies that hold FCC authorizations, in most instances we will be required to seek approval from the FCC prior to completing those acquisitions. Similarly, if we seek to dispose of facilities or discontinue services, in most cases we must obtain prior FCC approval. The FCC has broad authority to condition, modify, cancel, terminate or revoke operating authority for failure to comply with applicable federal laws or rules, regulations and policies of the FCC. Fines or other penalties also may be imposed for such violations.

### *Broadband and Internet Regulation*

A Verizon petition asking the FCC to forbear from applying common carrier regulation to certain broadband services sold by LECs primarily to larger business customers was deemed granted by operation of law on March 19, 2006 when the FCC did not deny the petition by the statutory deadline. The U.S. Court of Appeals for the District of Columbia Circuit has rejected a challenge to that outcome. The forbearance deemed granted to Verizon has been extended to our Northern New England operations by the FCC in its order approving the Spinco Merger. In October 2007, the FCC stated its intention to define more precisely the scope of forbearance obtained by Verizon, but it has not yet done so. On October 4, 2011, tw telecom, inc. filed a petition with the FCC asking it to reverse the forbearance granted to Verizon by operation of law on March 19, 2006. Comments have been filed in this proceeding by us and other parties. A similar petition was filed by a group of competing LECs on November 2, 2012 and comments have been filed with the FCC. The FCC may issue an order on either or both of these petitions at any time. We do not know how this will be resolved or the impact it may have on the Company if the FCC should reverse, eliminate or modify the forbearance granted to Verizon in 2006.

The FCC has imposed particular regulatory obligations on IP-based telephony. It has concluded that interconnected VoIP providers must comply with CALEA; provide enhanced 9-1-1 emergency calling capabilities; comply with certain disability access requirements; comply with the FCC's rules protecting the privacy of customer information; provide local number portability; and pay regulatory fees. The FCC has preempted some state regulation of VoIP.

There have been on-going discussions among policy makers concerning "net neutrality." The FCC released a statement of net neutrality principles favoring customer choice of content and services available over broadband networks. It has adopted open Internet access rules applicable to all broadband Internet access providers. On January 14, 2014, the United States Circuit Court of Appeals for the District of Columbia (the "D.C. Circuit") vacated portions of the FCC's December 21, 2010 Report and Order in the Matter of Preserving the Open Internet (GN Docket 09-191) (the "Open Internet Order"). In its decision, the D.C. Circuit vacated the FCC's anti-blocking and anti-discrimination rule related to Internet Service Providers, finding the FCC had failed to explain the basis of its authority in the Open Internet Order.

The FCC adopted new regulations governing "Broadband Internet Access Services" at its February 26, 2015 Open Meeting (the "Order"). "Broadband Internet access service" is now classified as a "telecommunications service" under Title II of the Communications Act. The Order prohibits "unjust and unreasonable practices" by broadband Internet access providers. The Order prohibits broadband Internet access providers from blocking access to legal content, applications, services and non-harmful devices. It prohibits broadband Internet access providers from impairing or degrading lawful Internet traffic on the basis of content, applications, services or non-harmful devices. It also prohibits broadband Internet access providers from favoring some lawful Internet traffic over other lawful traffic in exchange for consideration and from prioritizing their own content or services over those of unaffiliated entities. Other than paid prioritization which is prohibited, broadband Internet access providers are allowed to engage in reasonable network management practices. Broadband services that do not flow over the public Internet are exempt from these rules. The Order allows consumer complaints to be brought to the FCC under Title II of the Communications Act. The Title II classification could bolster universal service support for broadband services by classifying broadband services as telecommunications services and therefore subject to universal service fees assessed on telecommunications services.

In addition, several bills have been introduced in Congress to modify the FCC's rules or restrict the FCC's authority to regulate net neutrality and broadband Internet access services.

We cannot predict what impact, if any, new laws or rules may have on our business, financial condition, results of operations, liquidity or the market price of our outstanding securities or if Congress will enact legislation otherwise addressing net neutrality issues.

### ***State Regulation***

The local service rates and intrastate access charges of substantially all of our telephone subsidiaries are regulated by state regulatory commissions which typically have the power to grant and revoke authority for authorizing companies to provide telecommunications services. In some states, our intrastate long distance rates are also subject to state regulation. States typically regulate local service quality, billing practices and other aspects of our business as well. As described above, intrastate access charges are subject to the transition plan established in the recent CAF/ICC Order.

Most state commissions have traditionally regulated LEC pricing through cost-based rate-of-return regulation. In recent years, however, state legislatures and regulatory commissions in most of the states in which our telephone companies operate have either reduced the regulation of LECs or have announced their intention to do so and we expect this trend will continue. Such relief may take the form of mandatory deregulation of particular services or rates; or it may consist of optional alternative forms of regulation ("AFOR"), which may involve price caps or other flexible pricing arrangements. Some of these deregulatory measures are described in greater detail below. We believe that some AFOR plans allow us to offer new and competitive services faster than under the traditional regulatory regimes.

### ***Regulatory and Legislative for Vermont***

Effective April 6, 2016, we entered into an Incentive Regulation Plan ("IRP") governing our Vermont service territory within our Northern New England operations. The IRP includes retail service quality reporting requirements. The new IRP is similar to our previous IRP which expired on April 5, 2016 and we believe the IRP has allowed our Northern New England operations' retail rates in Vermont to compete with those competitive carriers under a relatively level regulatory scheme, while preserving certain regulatory protections for consumers seeking basic voice services in areas where competition may not be adequate. This IRP allows the same regulatory flexibility in our Telecom Group retail operations in Vermont and is scheduled to expire on December 31, 2019. On August 10, 2015, we concluded a retail service quality investigation by entering into a Memorandum of Understanding ("MOU") between us and the Vermont Department of Public Service ("VDPS"), which was approved by the Vermont Public Service Board ("VPSB") on December 18, 2015. In accordance with the August 10, 2015 MOU and the December 18, 2015 VPSB Order, on February 16, 2016, we requested the VPSB to open a new investigation to evaluate the appropriateness of certain service quality metrics and to determine whether customer service quality metrics should apply in the future to customers with access to an alternative telecommunications provider. This investigation is in progress and any outcome from this investigation will be incorporated into the new IRP, if necessary.

On July 15, 2016, the VPSB opened a rulemaking proceeding to consider amending VPSB Rule 3.706(D)(1) regarding the rental calculation for pole attachments. The rulemaking is in its early stages, and neither a schedule nor scope of this rulemaking has been determined.

### ***Regulatory and Legislative for Maine***

Under the Maine Public Utilities Commission ("MPUC") rules (Chapter 201), which went into effect August 1, 2014, the MPUC may open an investigation regarding the failure to meet any of the established SQI benchmarks and has the authority to impose penalties. The MPUC opened an investigation into our failure to meet some third quarter 2014 SQI benchmarks and subsequently opened an investigation into the fourth quarter of 2014 and then with respect to each of the quarterly periods in 2015. On March 29, 2016, the MPUC consolidated the investigations of the six quarters into one investigation. On September 14, 2016, a hearing examiner for the MPUC issued a report recommending that the MPUC find that FairPoint had failed to meet SQI benchmarks for the period under review and impose a \$500,000 penalty as allowed by statute, and provided until October 7, 2016 for comments or exceptions to be filed by interested parties. This recommendation did not constitute MPUC action. The Company promptly filed a motion to implement adjudicatory procedures prior to entry of any final order. After the Company's motion to implement adjudicatory procedures was briefed by the parties, the Hearing Examiner issued an order on November 30, 2016 granting the Company's motion in part and permanently withdrawing the Examiner's September 14, 2016 report. A case schedule was established by the Hearing Examiner, and a hearing is currently scheduled to begin May 11, 2017.

During 2014, we filed a rate case with the MPUC seeking increases in rates for POLR customers and seeking Maine Universal Service Fund ("MUSF") support for unrecovered costs associated with our obligation to provide POLR service to high cost areas. The MPUC allowed increases to the end user POLR rates, but denied MUSF support to us.

On April 13, 2016, LD 466, An Act to Increase Competition and Ensure Robust information and Telecommunications Market, was passed into law and became effective on July 28, 2016. The new law removes the regulation on POLR service in the most competitive municipalities on a phased in approach. The seven largest municipalities were deregulated effective August 28, 2016 (the POLR rate is grandfathered for one year), followed by five communities every six months until reaching a total of 22. These 22 municipalities represent approximately one third of the population and POLR customers. LD 466 provides a path forward for additional municipalities to be deregulated upon petitioning the PUC. Also included in the law is the removal of POLR tariffs statewide.

Reporting of service quality will be required only in the areas of the state where POLR is still required and will be filed and treated as confidential. The number of SQI reporting metrics has been reduced and the benchmarks are less stringent than under previous Commission rules. The Commission is empowered to investigate failures to meet a service quality requirement. If the Commission concludes after investigation that the failure to meet a service quality requirement is due to factors within the control of the price cap ILEC, the Commission shall, by order, impose such steps as the Commission determines necessary to meet the requirement. If the provider fails to comply with the order, the Commission shall impose a penalty in an amount sufficient to ensure compliance with that order.

### ***Local Government Authorizations***

We may be required to obtain from municipal authorities permits for street opening and construction or operating franchises to install and expand facilities in certain communities. If we more fully enter into video markets, municipal franchises may be required for us to operate as a cable television provider. Some of these franchises may require the payment of franchise fees. We have historically obtained municipal franchises as required. In some areas, we will not need to obtain permits or franchises because the subcontractors or electric utilities with which we will have contracts already possess the requisite authorizations to construct or expand our networks. In association with the American Recovery and Reinvestment Act of 2009 and other federal government programs, there may be an increase in our requirements associated with road move requests pursuant to new funding for roads. It is not certain whether funding will be available to us for this potential obligation.

### ***Environmental Regulations***

Like all other local telephone companies, our 32 LECs are subject to federal, state and local laws and regulations governing the use, storage, disposal of and exposure to hazardous materials, the release of pollutants into the environment and the remediation of contamination. As an owner of real property, we may be subject to environmental laws that impose liability for the entire cost of cleanup at contaminated sites, regardless of fault or the lawfulness of the activity that resulted in contamination. We believe, however, that our operations are in substantial compliance with applicable environmental laws and regulations.

**Reorganization**

On October 26, 2009, the Company and substantially all of its direct and indirect subsidiaries filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code. These cases were jointly administered under the caption *In re FairPoint Communications, Inc.* in the United States Bankruptcy Court for the Southern District of New York. On January 24, 2011, the Company substantially consummated its reorganization through a series of transactions contemplated by its Third Amended Joint Plan of Reorganization Under Chapter 11 of the United States Code (the "Plan").

**Other Information**

We make available free of charge on our website, [www.fairpoint.com](http://www.fairpoint.com), our reports on Forms 10-K, 10-Q and 8-K and all amendments to such reports as soon as reasonably practicable after we electronically file such material with, or furnish such material to, the SEC. Our filings with the SEC are available to the public over the Internet at the SEC's website at [www.sec.gov](http://www.sec.gov), or at the SEC's Public Reference Room located at 100 F Street, N.E., Washington, DC 20549. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the Public Reference Room.

**ITEM 1A. RISK FACTORS**

Any of the following risks could materially adversely affect our business, consolidated financial condition, results of operations, liquidity and/or the market price of our outstanding securities. The risks described below are not the only risks facing us. Additional risks and uncertainties not currently known to us or that we currently consider immaterial may also materially and adversely affect our business operations.

**Risks Related to the Merger with Consolidated Communications Holdings, Inc.**

*The announcement and pendency of the Merger may have a material adverse effect on our business.*

Uncertainty about the effect of the Merger on our employees, suppliers, customers and other parties may have a material adverse effect on our business. Although we intend to take steps designed to reduce any adverse effects, these uncertainties could impair our ability to retain and motivate key personnel and could cause customers, suppliers and others that deal with us to defer entering into contracts, or making other decisions, concerning doing business with us or seek to change existing business relationships with us. The pursuit of the Merger and the preparation for the integration may place a significant burden on our management and internal resources. In addition, we have diverted, and will continue to divert, significant management resources towards the completion of the Merger. The diversion of management's attention away from day-to-day business concerns and any difficulties encountered in the transition and integration process could adversely affect our financial results. In addition, the Merger Agreement restricts us from taking certain actions without the consent of Consolidated. These uncertainties and restrictions could disrupt or adversely affect our business and prevent us from pursuing otherwise attractive business opportunities that may arise prior to the completion of the Merger or termination of the Merger Agreement.

FairPoint Communications, the members of our board of directors, Consolidated and Merger Sub have been named as defendants in a lawsuit brought by a purported stockholder of FairPoint Communications challenging the Merger and seeking, among other things, to enjoin the defendants from consummating the Merger on the agreed-upon terms or to rescind the Merger if it is completed, in addition to damages. Additional lawsuits challenging the Merger may be filed, which may name us and/or our board of directors as defendants. We cannot assure you as to the outcome of such lawsuits, including the amount of costs associated with defending any such claim or any other liabilities that may be incurred in connection with the litigation of any such claim. One of the conditions to the closing of the Merger is the absence of any order, injunction or other legal restraint by a court or other governmental entity of competent jurisdiction that prevents the consummation of the Merger. Accordingly, if any plaintiff in any lawsuit is successful in obtaining an injunction prohibiting the parties from completing the Merger on the agreed-upon terms, such an injunction may delay the consummation of the Merger in the expected timeframe, or may prevent the Merger from being consummated altogether. Whether or not any plaintiff's claim is successful, this type of litigation may result in significant costs and diverts management's attention and resources, which could adversely affect the operation of our business.

*There may be unexpected delays in the completion of the Merger, or the Merger may not be completed at all.*

The Merger is currently expected to close around the middle of 2017, assuming that all of the conditions in the Merger Agreement are satisfied or waived. Certain events may delay the completion of the Merger or result in a termination of the Merger Agreement. Some of these events are outside the control of either party. In particular, completion of the Merger requires approval by

the stockholders of each of FairPoint Communications and Consolidated. If the required vote of the stockholders of FairPoint Communications is not obtained at the FairPoint Communications stockholder meeting (including any adjournments or

postponements thereof) at which the Merger has been voted upon, either we or Consolidated may terminate the Merger Agreement. In addition, if the required vote of the stockholders of Consolidated is not obtained by September 30, 2017, then either we or Consolidated may terminate the Merger Agreement. We may incur significant additional costs in connection with any delay in completing the Merger or the termination of the Merger Agreement, in addition to significant transaction costs, including legal, financial advisory, accounting and other costs we have already incurred.

We can neither assure you that the conditions to the completion of the Merger will be satisfied or waived or that any adverse change, effect, event, circumstance, occurrence or state of facts that could give rise to the termination of the Merger Agreement will not occur, and we cannot provide any assurances as to whether or when the Merger will be completed.

*Failure to complete the Merger in a timely manner or at all could negatively affect our stock price and future business and financial results.*

Delays in completing the Merger or the failure to complete the Merger at all could negatively affect our future business and financial results, and, in that event, the market price of our common stock may decline significantly, particularly to the extent that the current market price reflects a market assumption that the Merger will be completed. If the Merger is not completed for any reason, we will be subject to several risks, including the diversion of management focus and resources from operational matters and other strategic opportunities while working to implement the Merger, any of which could materially adversely affect our business, financial condition, results of operations and the value of our stock price. A failed transaction may result in negative publicity and a negative impression of us in the investment community. Further, any disruptions to our business resulting from the announcement and pendency of the Merger, including any adverse changes in our relationships with our customers, suppliers and employees, could continue or accelerate in the event of a failed transaction. In addition, if we do not complete the Merger, we may be required to pay a termination fee of \$18.9 million under certain circumstances set forth in the Merger Agreement.

In addition, we have incurred, and will continue to incur, significant costs, expenses and fees for professional services and other transition costs in connection with the Merger. We will be required to pay such costs relating to the transaction whether or not the Merger is consummated.

*The completion of the Merger is subject to the receipt of consents, approvals, and clearances from regulatory entities, which may impose conditions that could have an adverse effect on us or could cause either Consolidated or FairPoint Communications to abandon the Merger.*

The Merger requires certain consents, approval, and clearances from regulatory entities, including approval from the FCC and approval of regulatory authorities in a number of the states in which we and Consolidated operate. Regulatory entities may oppose the Merger or impose certain requirements or obligations as conditions for their approval or in connection with their review, which may be materially adverse to us, Consolidated, or the combined company. Regulatory approvals of the Merger may not be obtained on a timely basis or at all, and such approvals may include conditions that could delay the completion of the Merger, could lessen or eliminate the anticipated potential benefits of the Merger, or could result in the abandonment of the Merger.

*We will incur significant transaction and Merger-related transition costs.*

We have incurred and expect that we will continue to incur significant costs in connection with completing the Merger and integrating the operations of the two companies. Some of these costs are payable regardless of whether the transaction is completed. If the Merger is not completed, we will not receive any benefit from these expenditures.

#### **Risks Related to our Common Stock and Our Substantial Indebtedness**

*The price of our common stock may be volatile and may fluctuate substantially, which could negatively affect holders of our common stock.*

The market price of our common stock may fluctuate widely as a result of various factors including, but not limited to, period-to-period fluctuations in our operating results, the volume of sales of our common stock, the limited number of holders of our common stock and the resulting limited liquidity in our common stock, dilution, developments in the communications industry, the failure of securities analysts to cover our common stock, changes in financial estimates by securities analysts, short interests in our common stock, competitive factors, regulatory developments, labor disruptions, economic and other external factors, general market conditions and market conditions affecting the stock of communications companies in general. Communications companies have, in the past, experienced extreme volatility in the trading prices and volumes of their securities, which has often been unrelated to operating performance. High levels of market volatility may have a significant adverse effect on the market price of our common stock. In

addition, in the past, securities class action litigation has often been instituted against companies following periods of volatility in their stock prices. This type of litigation could result in substantial costs and divert management's attention and

resources, which could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our common stock.

*We have substantial indebtedness which could have a negative impact on our financing options and liquidity position and prevent us from fulfilling our financial obligations.*

As of December 31, 2016, our total gross indebtedness was approximately \$918.5 million (including \$2.5 million of capital leases) and \$61.1 million was available for borrowing under the Revolving Facility (as defined in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Debt"), net of \$13.9 million outstanding letters of credit. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Debt" included elsewhere in this Annual Report for more information, including maturities. Our substantial indebtedness could have important consequences including:

- making it more difficult for us to satisfy our financial obligations;
- requiring us to dedicate a significant portion of our cash flow from operations to paying the principal of and interest on our indebtedness, thereby limiting the availability of our cash flow to fund future capital expenditures, working capital and other corporate purposes;
- limiting our ability to obtain additional financing in the future for working capital, capital expenditures or acquisitions;
- limiting the amount of dividends we could pay to our stockholders;
- limiting our ability to refinance our indebtedness on terms acceptable to us or at all;
- restricting us from engaging in strategic transactions or causing us to make non-strategic divestitures;
- limiting our flexibility in planning for, or reacting to, changes in our business and the communications industry generally;
- placing us at a competitive disadvantage compared with competitors that have a less significant debt burden; and
- making us more vulnerable to economic downturns and limiting our ability to withstand competitive pressures.

Our ability to continue to fund our debt service requirements and to reduce our indebtedness may be affected by general economic, financial market, competitive, legislative and regulatory factors, among other things. An inability to fund our debt service requirements, reduce our indebtedness or satisfy debt covenant requirements could have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

In addition, our borrowings under our Credit Agreement (as defined in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Debt") bear interest at a variable rate based on a British Bankers Association LIBOR rate ("LIBOR"), subject to a floor of 1.25%. We have entered into interest rate swap agreements that effectively fix the interest rate on a combined notional amount of \$170.0 million of these borrowings; these agreements were effective September 30, 2015. If the relevant LIBOR increases above the level of the floor, the interest payments on our variable rate debt will increase and adversely affect our cash flow. Conversely, while LIBOR remains below 1.25%, we may incur interest costs above market rates. While our interest rate swap agreements and any future agreements we enter into may limit our exposure to higher interest rates, these agreements may not offer complete protection from this risk.

*We may incur significant additional amounts of debt, which could further exacerbate the current risks associated with our substantial indebtedness.*

We may incur substantial additional indebtedness in the future. Although the indenture governing our 8.75% senior secured notes due 2019 (the "Indenture") and our Credit Agreement contain restrictions on the incurrence of additional indebtedness, these restrictions are subject to a number of significant qualifications and exceptions and, under certain circumstances, the amount of indebtedness that could be incurred in compliance with these restrictions could be substantial. If new debt is added to our existing debt levels, the related risks that we now face could increase.

*To operate and expand our business, service our indebtedness and meet our other cash needs, we will require a significant amount of cash, which may not be available to us. We may not be able to generate sufficient cash to repay or refinance our indebtedness at maturity or otherwise or to fund our operations, and may be forced to take other actions to satisfy such obligations, which may not be successful.*

Our ability to make payments on, or repay or refinance, our indebtedness, to fund our operations and to fund planned capital expenditures, unanticipated capital expenditures and other cash needs will depend largely upon our financial condition and operating performance, including our ability to execute on our business plan. Our future operating performance, to a certain extent, is subject to general economic, financial, competitive, legislative, regulatory and other factors, such as any pension contributions required by the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), that are beyond our control. For example, the



minimum amount of pension contributions that we are required to make, which may be substantial, are determined under ERISA.

Our ability to borrow additional amounts, including under the Revolving Facility, if necessary to meet our cash needs, will depend on our ability to remain in compliance with the covenants contained in our debt agreements. If our operating results are not adequate to meet the financial ratio tests in our debt agreements or if we are unable to generate sufficient cash to service our debt requirements, we will be required to restructure or refinance our existing indebtedness, which we may not be able to accomplish under such circumstances on commercially reasonable terms or at all. If we are unable to refinance our debt or obtain new financing under these circumstances, we may have to consider other options, including without limitation:

- sales of assets;
- reduction or delay of capital expenditures, strategic acquisitions, investments and alliances;
- obtaining additional capital; or
- negotiations with our lenders to restructure or refinance the applicable debt.

Our ability to restructure or refinance our indebtedness may depend on the condition of the capital markets and our financial condition at such time, and any such restructuring and/or refinancing may come with higher interest rates and more onerous covenants. These alternative measures may not be successful and may not permit us to meet our scheduled debt service obligations.

An inability to generate sufficient cash from operations to repay or refinance our indebtedness at maturity or otherwise or to fund our operations could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

***Our debt agreements contain restrictions that limit our flexibility in operating our business.***

The Credit Agreement and the Indenture contain various covenants that limit our ability to engage in specified types of transactions. These covenants, under certain circumstances, limit us and our restricted subsidiaries' ability to, among other things:

- incur additional indebtedness;
- pay dividends on, repurchase or make distributions in respect of our capital stock or make other restricted payments;
- make certain investments;
- sell certain assets;
- create or incur liens;
- enter into sale and leaseback transactions;
- consolidate, merge, sell or otherwise dispose of all or substantially all of our assets; and
- enter into certain transactions with our affiliates.

A breach of any of these covenants could result in a default under the Credit Agreement or the Indenture. In addition, any debt agreements we enter into in the future may further limit our ability to enter into certain types of transactions. A breach of any of these covenants could result in a default under one or more of these agreements, including as a result of cross default provisions. Such default may allow the creditors to accelerate the related debt and may result in the acceleration of any other debt to which a cross-acceleration or cross-default provision applies.

In addition, the restrictive covenants in the Credit Agreement require us to maintain specified financial ratios and to satisfy other financial condition tests. Our ability to meet those financial ratios and tests depends on our ongoing financial and operating performance, which, in turn, is subject to economic conditions and to financial, market, and competitive factors, many of which are beyond our control. See "Item 7. Management's Discussion and Analysis of Financial Conditions and Results of Operations — Liquidity and Capital Resources" included elsewhere in this Annual Report for more information regarding the Credit Agreement and the Indenture.

***FairPoint Communications is a holding company and depends upon the cash flows of its operating subsidiaries to service its indebtedness and meet its other cash flow needs.***

FairPoint Communications is a holding company and conducts no operations. Accordingly, its cash flow and its ability to make payments on, or repay or refinance, its indebtedness and to fund planned capital expenditures and other cash needs will depend largely upon the cash flows of its operating subsidiaries and the distribution of cash by those subsidiaries to it through repayment of loans, dividends, management fees or otherwise. Distributions to FairPoint Communications from its subsidiaries will depend on their respective operating results and will be subject to restrictions under, among other things:

- the laws of their jurisdiction of organization;
- the rules and regulations of state and federal regulatory authorities;
- agreements of those subsidiaries, including agreements governing their indebtedness, if any; and
- regulatory orders.

FairPoint Communications' subsidiaries have no obligation, contingent or otherwise, to make funds available, whether in the form of loans, dividends or other distributions, to it. Any inability to receive distributions from its subsidiaries could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

*Limitations on our ability to use NOL carryforwards, and other factors requiring us to pay cash to satisfy our tax liabilities in future periods, may affect our ability to fund our operations, make capital expenditures and repay our indebtedness.*

Effective December 31, 2011, our NOLs were substantially reduced by the recognition of gains on the discharge of certain debt pursuant to the Plan. In addition, our emergence from bankruptcy resulted in an ownership change for federal income tax purposes under Section 382 of the Internal Revenue Code of 1986, as amended (the "Code"). This followed previous ownership changes resulting from our initial public offering in February 2005, which resulted in an "ownership change" within the meaning of the United States federal income tax laws addressing NOL carryforwards, alternative minimum tax credits and other similar tax attributes. Moreover, the Spinco Merger resulted in a further ownership change for these purposes. As a result of these ownership changes, there are specific limitations on our ability to use these NOL carryforwards and other tax attributes from periods prior to our emergence from bankruptcy. Furthermore, additional limitations on the use of NOLs could arise in the future if a 50% or more change in ownership as defined under the Code were to occur. Although we do not expect that these limitations will materially affect our United States federal and state income tax liability in the near term, it is possible in the future if we were to generate taxable income in excess of the limitation on usage of NOL carryforwards that these limitations could limit our ability to utilize the carryforwards and, therefore, result in an increase in our United States federal and state income tax payments over the amount we otherwise would have, had we not experienced an ownership change. In addition, in the future we will be required to pay cash to satisfy our tax liabilities when all of our NOL carryforwards have been used or have expired. Limitations on our usage of NOL carryforwards, and other factors requiring us to pay cash taxes, would reduce the amount available to fund our operations, make capital expenditures and service our indebtedness in the future, which could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

*Concentration of ownership among stockholders may prevent new or current investors from influencing significant corporate decisions.*

Based on Schedules 13D and 13G filed by the respective holders, as of February 27, 2017, there are some institutional holders who own 5% or more of our outstanding common stock. As a result, these stockholders may be able to exercise significant control over all matters requiring stockholder approval, including the Merger, the election of directors, amendment of our certificate of incorporation and approval of corporate transactions and could gain significant control over our management and policies as a result thereof.

*Future sales or the possibility of future sales of a substantial amount of our common stock may depress the price of our common stock.*

Future sales, or the availability for sale in the public market, of substantial amounts of our common stock could adversely affect the prevailing market price of our common stock and could impair our ability to raise capital through future sales of equity securities. The market price of our common stock could decline as a result of sales of a large number of shares of our common stock in the market or the perception that these sales could occur. These sales, or the possibility that these sales may occur, may also make it more difficult for us to obtain additional capital by selling equity securities in the future at a time and at a price that we consider appropriate.

As of February 27, 2017, we had 27,266,570 shares of common stock outstanding. All such shares are freely traded except for any shares of our common stock that may be held or acquired by our directors, executive officers, employee insiders and other affiliates, as that term is defined in the Securities Act, which will be restricted securities under the Securities Act. Restricted securities may not be sold in the public market unless the sale is registered under the Securities Act or an exemption from registration is available. In addition, Angelo Gordon & Co., L.P. ("Angelo Gordon") and entities advised by Angelo Gordon have certain registration rights with respect to the common stock they hold or may acquire in the future.

We may issue shares of our common stock, or other securities, from time to time as consideration for future acquisitions and investments. In the event any such acquisition or investment is significant, the number of shares of our common stock, or the



number or aggregate principal amount, as the case may be, of other securities that we may issue may in turn be significant. We may also grant registration rights covering these shares or other securities in connection with any such acquisitions and investments.

### **Risks Related to Our Business**

*We provide services to customers over access lines, and since we have been losing access lines, if our efforts to mitigate this decline and transition to alternative revenue is not successful, our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities may be materially adversely affected.*

We, along with the communications industry in general, have experienced a decline in access lines and network access revenues and will be further unfavorably impacted in the long-term by the FCC's recent CAF/ICC Order on intercarrier compensation. See "Risks Relating to Our Regulatory Environment" for specific risks associated with the impact of regulatory reform. We generate revenue primarily by delivering voice and data services over access lines. During the years ended December 31, 2016 and 2015, we continued to experience access line loss. These losses resulted mainly from competition, including competition from bundled offerings by cable companies, the use of alternate technologies, including wireless, as well as challenging economic conditions and the offering of DSL services.

We expect to continue to experience net access line losses. Our strategy of providing broadband and advanced data services, such as Ethernet over fiber and copper plant, may not be sufficient to offset the revenue impact of continued access line loss. Our inability to retain access lines and successfully offset such losses with alternative revenue could adversely affect our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

*We provide access services to other communications companies, and if these companies were to find alternative means of providing services, become insolvent or experience substantial financial difficulties, our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities may be materially adversely affected.*

We originate and terminate calls on behalf of long distance carriers and other interexchange carriers over our network in exchange for payment of switched access charges. Interstate and intrastate access charges represented approximately 29% of our total revenues during the twelve months ended December 31, 2016. Terminating switched access rates are scheduled to decline under the FCC's recent CAF/ICC Order. See "Risks Relating to Our Regulatory Environment" for specific risks associated with the impact of regulatory reform. We may not be successful in offsetting these declines through regulatory replacement mechanisms or operational means. Further, should one or more of these carriers find alternative means of providing services, loss of revenues from these carriers could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities. In addition, should one or more of the carriers that we do business with become insolvent or experience substantial financial difficulties, our inability to timely collect access charges from them could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

*We are subject to competition that may materially adversely impact our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.*

We face intense competition from a variety of sources for our voice, network transport and Internet services in nearly all of the areas we now serve. Regulations and technology change quickly in the communications industry and changes in these factors historically have had, and in the future may have, a significant impact on competitive dynamics. In most of our service areas, we currently face competition from wireless carriers for voice services and increasingly for Internet services. As technology and economies of scale have improved, competition from wireless carriers has increased and is expected to further increase. We also face increasing competition from wireline and cable television companies for our voice and Internet services. We estimate that most of the customers that we serve have access to voice, network transport and Internet services through a cable television company. Wireline and cable television companies have the ability to bundle their services, which has and is expected to continue to intensify the competition we face from these providers. VoIP providers, Internet service providers and satellite companies also compete with our services and such competition has increased and is expected to continue to increase in the future. In addition, many of our competitors have access to a larger workforce and have substantially greater name-brand recognition and financial, technological and other resources including, in the case of cable television providers, free advertising on their video services.

In addition, consolidation and strategic alliances within the communications industry and the development of new technologies have had and may continue to have an effect on our competitive position. We cannot predict the number of competitors that will emerge, particularly in light of possible regulatory or legislative actions that could facilitate or impede market entry, but increased competition from existing and new entities could have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.



Competition may lead to loss of revenues and profitability as a result of numerous factors, including:

- loss of customers (given the likelihood that when we lose customers for local service, we will also lose them for all related services);
- reduced network usage by existing customers who may use alternative providers for voice and data services;
- reductions in the prices we charge to meet competition; and
- increases in marketing expenditures and discount and promotional campaigns to incent customers to choose our services.

*Price increases or price retention for certain products and customers may result in an acceleration of access line losses or an unanticipated decline in our growth-oriented products, which may materially adversely affect our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.*

From time to time, we expect to implement price increases for certain products and customers. Although we intend for the price increase to provide a net revenue benefit, it is possible that customers will disconnect at a faster rate than they otherwise would have, which could negate the benefit of the price increase. Additionally, a weaker economic environment can result in increased demand by our customers for price reductions at the same or better level of service. In some of our more competitive markets, we may need to offer more favorable terms to our customers for contract renewal, which could result in reduced profitability. Despite continuous efforts by our sales force to retain customers, we cannot provide assurance that we will be able to renew customers dissatisfied with our contract renewal terms.

*We may not be able to successfully integrate new technologies, respond effectively to customer requirements or provide new services.*

Rapid and significant changes in technology and new service introductions occur frequently in the communications industry and industry standards evolve continually, including but not limited to a transition in the industry from primarily voice products to data services. We cannot predict the effect of these changes on our competitive position, profitability or the industry. Technological developments may reduce the competitiveness of our networks and require unbudgeted upgrades or the procurement of additional products that could be expensive and time consuming. In addition, new products and services arising out of technological developments may reduce the attractiveness of our existing services. If we fail to adapt successfully to technological changes or obsolescence or fail to obtain access to important new technologies, we could lose customers and be limited in our ability to attract new customers and sell new services to our existing customers, which could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

*The geographic concentration of our operations in Maine, New Hampshire and Vermont make our business susceptible to local economic and regulatory conditions and consumer trends, and an economic downturn, recession or unfavorable regulatory action in any of those states may materially adversely affect our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.*

Our service territory spans 17 states. As of December 31, 2016, 83% of our total residential voice lines were located in Maine, New Hampshire and Vermont (including certain of our Telecom Group service companies). As a result of this geographic concentration, our financial results will depend significantly upon economic conditions and consumer trends in these markets. Deterioration in economic conditions in any of these markets could result in a further decrease in demand for our services and resulting loss of access line equivalents which could have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

In certain areas of our service territory, the need for our services is seasonal (including either winter or summer), which may result in revenue fluctuations quarter over quarter. While we attempt to forestall seasonal disconnects or seasonal suspends, some revenue fluctuations continue to occur and once a customer disconnects or suspends, he or she may not return as a customer.

In addition, if state regulators or legislators in Maine, New Hampshire or Vermont were to take an action that is adverse to our operations in those states, we could suffer greater harm from that action than we would from action in other states because of the concentration of our operations in those states.

*We may need to defend ourselves against claims that we infringe upon others' intellectual property rights or may need to seek third-party licenses to expand our product offerings.*

From time to time, we receive notices from third parties or are named in lawsuits filed by third parties claiming we have infringed or are infringing upon their intellectual property rights. We may receive similar notices or be involved in similar lawsuits in the future. Responding to these claims may require us to expend significant time and money defending our use of affected technology, may require us to enter into licensing agreements requiring license payments that we would not otherwise have to pay



or may require us to pay damages. If we are required to take one or more of these actions, our operating expenses may increase. In addition, in responding to these claims, we may be required to stop selling or redesign one or more of our products or services, which could significantly and adversely affect the way we conduct business.

Similarly, from time to time, we may need to obtain the right to use certain patents or other intellectual property from third parties to be able to offer new products and services. If we cannot license or otherwise obtain rights to use any required technology from a third party on reasonable terms, our ability to offer new products and services may be restricted, made more costly or delayed.

*We depend on third party providers for certain of our billing functions, IT services, including network support and improvements, and for the provision of our long distance and bandwidth services.*

We have agreements with outside service providers to perform a portion of our billing functions and for our provision of long distance and bandwidth services. We also rely on certain third parties for IT services, including network support and improvements.

If these service providers are unable to adequately perform such services or if one of them experiences a significant degradation or failure with respect to such services, it could result in disruptions in our billing, IT systems and/or long distance and bandwidth services. Service failures could also result in internal controls deficiencies, which could adversely impact our overall control assessment of internal control in accordance with the Sarbanes-Oxley Act of 2002. Furthermore, if these agreements are terminated for any reason, we may be unable to find an alternative service provider in a timely manner or on terms acceptable to us, and may be unable ourselves to perform the services they provide.

With respect to the agreements governing our long distance and bandwidth services, these agreements are based, in part, on our estimate of future supply and demand and may contain minimum volume commitments. If we overestimate demand, we may be forced to pay for services we do not need. If we underestimate demand, we may need to acquire additional capacity on a short-term basis at unfavorable prices, assuming additional capacity is available. If additional capacity is not available, we may not be able to meet this demand. In addition, if we cannot meet any minimum volume commitments, we may be subject to underutilization charges, termination charges or rate increases.

If any of the foregoing events occur with respect to our third-party providers, our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities could be materially adversely affected.

*A network disruption could cause delays or interruptions of service, including for 9-1-1 service, which could cause us to lose customers, engage in litigation, incur fines or otherwise adversely impact our business.*

To be successful, we will need to continue to provide our customers with reliable and uninterrupted service over our expanded network. Disruptions in our service could occur as a result of events that are beyond our control. Some of the risks to our network and infrastructure include:

- physical damage to our transmission network including poles, cable and access lines;
- widespread power surges or outages;
- software defects in critical systems;
- capacity limitations resulting from changes in our customers' usage patterns;
- human error; and
- damage intentionally inflicted upon the network or our other infrastructure.

From time to time, in the ordinary course of business, we have experienced and in the future may experience short disruptions in our service due to factors such as cable damage, inclement weather and service failures of our third-party service providers. We could experience more significant disruptions in the future. In addition, certain portions of our network may lack adequate redundancy to allow for expedient recovery of service to affected customers. Disruptions may cause interruptions in service or reduced capacity for customers, either of which could cause us to lose customers, engage in litigation and incur fines and/or expenses or capital expenditures, which could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

*Any failure or inadequacy of our IT infrastructure could harm our business.*

A major failure or inadequacy of our IT infrastructure could harm our business. The capacity, reliability and security of our internal IT hardware and software infrastructure are important to the operation of our current and future business, which would suffer in the event of major system failures. Our inability to expand or upgrade our IT hardware and software infrastructure could

have adverse consequences, which could include the delayed implementation of new service offerings, increased acquisition integration costs, service or billing interruptions, the issuance of service quality credits, and the diversion of development resources. If any of the foregoing events occur with respect to our IT infrastructure, our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities could be materially adversely affected.

*Increases in broadband usage may cause network capacity limitations, resulting in service disruptions, reduced capacity or slower transmission speeds for customers.*

Video streaming services and peer-to-peer file sharing applications use significantly more bandwidth than traditional Internet activity such as web browsing and email. As use of these newer services continues to grow, our high-speed Internet customers will likely use much more bandwidth than in the past. If this occurs, we could be required to make significant capital expenditures to increase network capacity in order to avoid service disruptions, service degradation or slower transmission speeds for our customers. Alternatively, we may choose to implement network management practices to reduce the network capacity available to bandwidth-intensive activities during certain times in areas experiencing congestion, which could negatively affect our ability to retain and attract customers in affected markets. While we believe demand for these services may drive high-speed Internet customers to pay for faster broadband speeds, we may not be able to recover the costs of the necessary network investments. This could result in an adverse impact to our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

*A cyber-attack that bypasses our IT and/or network security systems causing an IT and/or network security breach may lead to unauthorized use or disabling of our network, theft of customer data, unauthorized use or publication of our intellectual property and/or confidential business information and could harm our competitive position or otherwise adversely affect our business.*

Attempts by others to gain unauthorized access to organizations' IT systems or network elements are becoming more sophisticated and are sometimes successful. These attempts include covertly introducing malware to companies' computers and networks, impersonating authorized users, or "hacking" into systems. We seek to detect and investigate all security incidents and to prevent their recurrence, but, in some cases, we might be unaware of an incident or its magnitude and effect. Significant network security failures could result in the theft, loss, damage, unauthorized use or publication of our intellectual property and/or confidential business information; the theft, loss, damage, unauthorized use or publication of our customers' personally identifiable information, intellectual property and/or confidential business information; the unauthorized use or disabling of our network elements; or damage to our reputation among customers and the public. These consequences could harm our competitive position, subject us to additional regulatory scrutiny, expose us to litigation, reduce the value of our investment in research and development and other strategic initiatives or otherwise adversely affect our business. To the extent that any security breach results in inappropriate disclosure of our customers' or licensees' confidential information, we may incur liability as a result.

*Natural catastrophes or terrorism may damage our network or adversely affect the financial markets.*

A major earthquake, hurricane, tornado, winter storm, flood, fire, terrorist attack, cyber-attack or other similar disruption could damage our network, network operations centers, call centers, data centers, central offices, corporate headquarters or other facilities. Such an event could interrupt our services, adversely affect service quality, overwhelm customer support and ultimately harm our business and reputation. Although we have implemented measures that are designed to mitigate the effects of such events, we cannot predict all of the potential impacts of such events. We maintain insurance coverage for some of these events; however, the potential liabilities associated with these events could exceed the insurance coverage we maintain. Our inability to operate our networks or operate key systems as a result of such events, even for a limited period of time, may result in significant expenses or loss of customers and associated revenue.

Even if the major event does not directly impact us, these events could more broadly cause consumer confidence and spending to decrease or result in increased volatility in the United States and world financial markets and economy, which would adversely affect our business.

***Our actual operating results may differ significantly from our guidance.***

From time to time, we have released and may continue to release guidance regarding our future performance that represents our management's best estimates as of the date the guidance is provided. This guidance, which consists of forward-looking statements, is prepared by our management and is qualified by, and subject to, the assumptions and the other information contained or referred to in the release. Our guidance is not prepared with a view toward compliance with the published guidelines of the American Institute of Certified Public Accountants, and neither our independent registered public accounting firm nor any other independent expert or outside party compiles or examines the guidance and, accordingly, no such person expresses any opinion or any other form of assurance with respect thereto.

Guidance is based upon a number of assumptions and estimates that, while presented with numerical specificity, are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond our control and are based upon specific assumptions with respect to future business decisions, some of which will change. We generally state possible outcomes as high and low ranges which are intended to provide a sensitivity analysis as variables are changed but are not intended to represent our actual results which could fall outside of the suggested ranges. The principal reason that we release this data is to provide a basis for our management to discuss our business outlook with analysts and investors. Notwithstanding this, we do not accept any responsibility for any projections or reports published by any such outside analysts or investors.

Guidance is necessarily speculative in nature, and it can be expected that some or all of the assumptions or the guidance furnished by us will not materialize or will vary significantly from actual results. Accordingly, our guidance is only an estimate of what management believes is realizable as of the date the guidance is provided. Actual results may differ from the guidance and the differences may be material. Investors should also recognize that the reliability of any forecasted financial data diminishes the farther in the future that the data is forecast. In light of the foregoing, users of this guidance are urged to put the guidance in context and not to place undue reliance on any such guidance.

Any inability to successfully implement our operating strategy or the occurrence of any of the events or circumstances discussed therein could result in the actual operating results being different than the guidance, and such differences may be material.

***Our success will depend on our ability to attract and retain qualified management and other personnel.***

Our success depends upon the talents and efforts of our senior management team. The loss of any member of our senior management team, due to retirement or otherwise, and the inability to attract and retain highly qualified technical and management personnel in the future, could have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

***Our ability to successfully manage reductions in our workforce could have a material adverse impact on our results of operations.***

Reductions in our workforce could adversely impact our ability to operate effectively and, therefore, could adversely impact our customer service, result in higher regulatory penalties and/or reduce our ability to achieve our operational goals.

***A significant portion of our workforce is represented by labor unions and therefore subject to collective bargaining agreements. If disputes arise, or if we are unable to successfully renegotiate these agreements at an appropriate time or on terms acceptable to us, workers subject to these agreements could engage in work stoppages or other concerted activities, which could materially adversely impact our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.***

As of December 31, 2016, approximately 1,500 of our approximately 2,500 employees were covered by 13 collective bargaining agreements. After ratification of the collective bargaining agreements on February 22, 2015, our agreements with the IBEW and the CWA in northern New England expire in August 2018. Disputes with regard to the terms of any of these agreements or our potential inability to negotiate acceptable contracts with these unions in the future as our current contracts expire could result in, among other things, strikes, work stoppages or other slowdowns by the affected workers. We have experienced work stoppages in the past upon the expiration of collective bargaining agreements. If represented workers were to engage in future work stoppages or other concerted activities, we could experience a significant disruption of our operations, including network disruptions, IT failures, service backlog, internal control failures and/or regulatory compliance issues, and/or higher ongoing labor costs, either of which could have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities. Additionally, future renegotiation of labor agreements or the provisions of such labor agreements could adversely impact our service reliability and significantly increase our costs for healthcare, wages and other benefits, which could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

*The amount we are required to contribute to our qualified pension plans and post-employment benefit plans is impacted by several factors that are beyond our control and changes in those factors may result in a significant increase in future cash contributions.*

We sponsor two qualified defined benefit pension plans covering certain employees that will provide them benefit payments, if eligible, after their retirement. These qualified pension plans are subject to funding requirements determined under ERISA and the Code. Required pension contributions may be impacted by several factors, including fluctuations in the discount rate used to calculate the funding target, unfavorable differences in actual experience relative to the assumptions used to determine the liabilities in these plans, the performance of the pension plan asset portfolio and the number of retirees in the qualified pension plan covering non-represented employees who elect to receive lump sum distributions. Unfavorable fluctuations or adverse changes in any of these factors are beyond our control and may diminish the funded status of our pension plans, thereby significantly increasing the contributions we are required to make under ERISA and the Code.

The represented employees pension plan was closed to new participants and benefits under the prior formula were frozen as of October 14, 2014. Future benefit accruals for service on and after February 22, 2015 are at 50% of prior rates and are capped at 30 years of total credited service. Of our projected benefit obligation for our pension plans, approximately 9% reflects the non-represented employees.

Non-represented employees covered by the non-represented employees pension plan have the option to elect to receive their accrued vested benefit in the form of a lump sum payment. Represented employees covered by the represented employees pension plan are no longer able to elect to receive their accrued vested benefit in the form of a lump sum effective with the expiration of the collective bargaining agreements with the IBEW and the CWA on August 2, 2014. As the discount rate used to calculate lump sum payments are currently lower than the discount rate used to calculate the actuarial liabilities in the non-represented employee pension plan, the value of a lump sum payment exceeds the actuarial liability for the participant, which creates an actuarial loss in the pension plan for non-represented employees when paid. As such, a lump sum payment depletes the plan's assets more than the corresponding reduction in the plan's liability, which thereby reduces the funded status of the plan. If a significant number of eligible non-represented employees retire and elect to receive their accrued vested benefit in the form of a lump sum payment, which is beyond our control, the qualified pension plan covering these participants may experience a significant reduction in its funded status, which could materially increase future required contributions. During the year ended December 31, 2016, we recognized \$0.6 million in plan settlement expense as the cumulative amount of lump sums paid during 2016 exceeded the expected service and interest cost for 2016.

During the year ended December 31, 2016, we experienced income on qualified pension plan assets totaling approximately 7.5%. However, during the year ended December 31, 2015, we experienced actual losses on qualified pension plan assets totaling approximately 1.9%. The actuarially-determined funded status of our pension plans is dependent on the market value of the assets held by each plan. As such, a significant decline in the market value of the pension plans' assets could result in us having to make additional contributions to these plans.

Legislation enacted in 2014 changed the method for determining the discount rate used for calculating a qualified pension plan's unfunded liability for ERISA and Code purposes, which improved our pension plans' funded status on an ERISA basis. There are no assurances of any future legislation to provide similar relief or to extend the benefits of relief provided by this legislation. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Pension Contributions and Post-Employment Benefit Plan Expenditures" included elsewhere in this Annual Report.

We also sponsor a post-employment benefit plan that provides medical, dental and life insurance benefits to eligible non-represented employees and former represented employees and, in some instances, to their spouses and families. The level of contributions required from us under these plans is dependent on the number of eligible retirees that elect coverage under the plan and the level and cost of health services used by those eligible retirees, each of which are beyond our control. Inflation in medical and dental costs in the future will increase future contributions. Effective August 28, 2014, active represented employees are no longer eligible for this post-employment benefit plan. Upon ratification of the collective bargaining agreements on February 22, 2015 and for 30 months thereafter, active represented employees who retire and meet the eligibility requirements and their spouses are eligible to receive certain monthly reimbursements of medical insurance premiums for healthcare plans until the retired employee reaches age 65 or dies. As a result of these factors, the payments we are required to make in relation to the above may also increase.

Increasing cash requirements to fund benefits under our qualified pension and post-employment benefit plans and the represented employee limited reimbursement arrangement may impact our liquidity position and limit our operational flexibility. These future cash requirements could have a material adverse impact on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

See note (11) "Employee Benefit Plans" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report for further information.

*Our long-lived assets and non-amortizable intangible assets may become impaired in the future.*

At December 31, 2016, in addition to our net property, plant and equipment of \$1,024.4 million, we have net amortizable intangible assets of \$34.3 million and non-amortizable intangible assets of \$41.6 million. Amortizable long-lived assets must be reviewed for impairment whenever indicators of impairment exist. Non-amortizable long-lived assets are required to be reviewed for impairment on an annual basis or more frequently whenever indicators of impairment exist. Indicators of impairment could include, but are not limited to:

- an inability to perform at levels that were forecasted;
- a permanent decline in market capitalization;
- implementation of restructuring plans;
- changes in industry trends; and/or
- unfavorable changes in our capital structure, cost of debt, interest rates or capital expenditures levels.

Situations such as these could result in an impairment that would require a material non-cash charge to our results of operations and could have a material adverse effect on our consolidated results of operations.

*Our operations require substantial capital expenditures.*

We require significant capital expenditures to maintain, upgrade and enhance our network facilities and operations. While we have historically been able to fund capital expenditures from cash generated from operations and borrowings under the Revolving Facility, the other risk factors described in this section could materially reduce cash available from operations or significantly increase our capital expenditure requirements, and these outcomes may result in our inability to fund the necessary level of capital expenditures to maintain, upgrade or enhance our network. This could adversely affect our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

*We are exposed to risks relating to evaluations of internal control systems required by Section 404 of the Sarbanes-Oxley Act.*

As a public reporting company, we are required to comply with the Sarbanes-Oxley Act and the related rules and regulations of the SEC, including accelerated reporting requirements and expanded disclosures regarding evaluations of internal control systems. With respect to internal control over financial reporting, standards established by the Public Company Accounting Oversight Board define a material weakness as a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. If our management identifies one or more material weaknesses in internal control over financial reporting in the future in accordance with the annual assessments and quarterly evaluations required by the Sarbanes-Oxley Act, we will be unable to assert that our internal controls are effective which could result in sanctions or investigation by regulatory authorities. In addition, any such material weakness could result in material misstatements in our financial statements, prevent us from providing timely financial statements or meeting our reporting requirements both with the SEC and under our debt obligations and cause investors to lose confidence in our reported financial information.

**Risks Relating to Our Regulatory Environment**

*"Net neutrality" and broadband Internet access service legislation or regulation could limit our ability to operate our broadband business profitably and to manage our broadband facilities efficiently.*

In order to continue to provide quality high-speed data service at attractive prices and to offer new services, we believe we need the continued flexibility to respond to changing consumer uses and demands, to manage bandwidth usage efficiently and to continue to invest in our networks. In 2010, the FCC adopted "net neutrality" regulations that curtailed our operational flexibility. A federal appeals court vacated these rules in January 2014, after which the FCC adopted new regulations governing "Broadband Internet Access Services" at its February 26, 2015 Open Meeting (the "Order"). "Broadband Internet access service" will now be classified as a "telecommunications service" under Title II of the Communications Act. The Order prohibits "unjust and unreasonable practices" by broadband Internet access providers. The Order prohibits broadband Internet access providers from blocking access to legal content, applications, services and non-harmful devices. It prohibits broadband Internet access providers from impairing or degrading lawful Internet traffic on the basis of content, applications, services or non-harmful devices. It also prohibits broadband Internet access

providers from favoring some lawful Internet traffic over other lawful traffic in exchange for consideration and from prioritizing their own content or services over those of unaffiliated entities. Other than paid prioritization

which is prohibited, broadband Internet access providers are allowed to engage in reasonable network management practices, though it is not currently known what such practices will be defined to include. Broadband services that do not flow over the public Internet are exempt from these rules. The Order allows consumer complaints to be brought to the FCC under Title II of the Communications Act.

We cannot predict what impact, if any, these rules may have on our business, financial condition, results of operations, liquidity or the market price of our outstanding securities or whether Congress will modify these rules through pending legislative proposals.

*We are subject to significant regulation that could change in a manner adverse to us.*

We operate in a heavily regulated industry. Laws and regulations applicable to us and our competitors may be, and have been, challenged in the courts and could be changed by Congress or regulators. In addition, the following factors could have a significant impact on us:

***Risk of loss or reduction in revenues associated with regulated filings, rules or tariffs.*** A portion of our revenues comes from intrastate and interstate network access charges, which are paid to us by interexchange carriers for originating and terminating communications traffic. See "Item I. Business—Regulatory and Legislative" included elsewhere in this Annual Report.

As described in "Item I. Business—Regulatory and Legislative," we have accepted most of the CAF Phase II support offered to us during 2015. We risk not being able to fulfill the obligations of the CAF Phase II program, which includes specific location requirements and technical obligations associated with speed, latency, data provision and pricing. These requirements and obligations may prove costly to implement. Failure to timely implement our CAF Phase II obligations by the interim milestones (40%, 60% and 80% of locations built out by December, 2017, 2018 and 2019, respectively) may result in a portion of funds being delayed at each interim milestone. Failure to build out at least 50% of locations required by an interim milestone may result in a loss of all funds and therefore this continuing revenue stream.

The CAF/ICC Order fundamentally reforms the ICC system that governs how communications companies bill one another for terminating traffic, gradually phasing out these charges. Additional reforms have been proposed. The reforms adopted by the FCC in its order will significantly change the access charge system and, if not offset by a revenue replacement mechanism, could potentially result in a significant decrease in or elimination of access charges. Regulatory developments of this type could materially adversely affect our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

***Risk of re-regulation of wholesale network services provided to retail and wholesale customers.*** Pursuant to forbearance from the regulation of high-speed interstate services that was deemed granted to Verizon in 2006 and transferred to us by the FCC in its order approving the Spinco Merger, we offer high-speed interstate services on a deregulated basis. The FCC has initiated a proceeding to investigate potential changes to the regulation of special access services. Several parties filed petitions in 2011 and 2012 asking the FCC to reverse the 2006 forbearance granted to Verizon. The FCC has issued a comprehensive data request to gather granular information from all providers of special access-like high speed services and this data request was completed in February 2015. The purpose of the data request is to provide the FCC with information that can be used to evaluate competition for special access-like services. It is not clear what actions, if any, the FCC will take in these proceedings. Orders resulting from these proceedings could adversely affect pricing and regulation of these services.

The FCC also is considering changes to its rules governing who contributes to the USF support mechanisms, and on what basis. Any changes in the FCC's rules governing the manner in which entities contribute to the USF could have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

***Risk of loss of statutory exemption from burdensome interconnection rules imposed on ILECs.*** Our rural LECs generally are exempt from the more burdensome requirements of the 1996 Act governing the rights of competitors to interconnect to ILEC networks and to utilize discrete network elements of the incumbent's network at favorable rates. To the extent state regulators decide that it is in the public interest to extend some or all of these requirements to our rural LECs, we may be required to provide UNEs to competitors in our rural telephone company areas. As a result, more competitors could enter our traditional telephone markets than are currently expected, which could have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

***Risks posed by costs of regulatory compliance.*** Regulations create significant compliance and administrative costs for us. Our subsidiaries that provide intrastate services are generally subject to certification, tariff filing and other ongoing regulatory requirements by state regulators. Our interstate and intrastate access services are currently provided in accordance with tariffs filed with the FCC and state regulatory authorities, respectively. Challenges in the future to our tariffs by regulators or third parties or delays in obtaining certifications and regulatory approvals could cause us to incur substantial legal and administrative expenses,



and, if successful, these challenges could adversely affect the rates that we are able to charge our customers, which could have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

Our acceptance of CAF Phase II funding through the FCC's universal service program requires that we satisfy specific broadband service obligations in locations approved by the FCC within deadlines established by the FCC. If we fail to meet these deadlines, or our broadband service fails to satisfy FCC performance standards, we could be subject to penalties, refunds and other enforcement action by the FCC. In the two states where we declined CAF Phase II support, we cannot predict whether competitors will win a competitive bid for support in our service territories.

In addition, our Northern New England operations are subject to regulations not applicable to our rural operations, including but not limited to requirements relating to interconnection, the provision of UNEs, and the other market-opening obligations set forth in the 1996 Act. In approving the transfer of authorizations to us in the Spincor Merger, the FCC determined that our non-rural operations would be subject to the same regulatory requirements that currently apply to Bell Operating Companies. The FCC also stated that we would be entitled to the same regulatory relief that Verizon New England had obtained in the region. Any changes made in connection with these obligations or relief could increase our non-rural operations' costs or otherwise have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities. Moreover, we cannot predict the precise manner in which the FCC will apply the Bell Operating Company regulatory framework to us.

Our business also may be affected by legislation and regulation imposing new or greater obligations related to open Internet access, assisting law enforcement, bolstering homeland security, pole attachments, minimizing environmental impacts, protecting customer privacy or addressing other issues that affect our business. We cannot predict whether or to what extent the FCC might modify its rules or what compliance with those new rules might cost. Similarly, we cannot predict whether or to what extent federal or state legislators or regulators might impose new network access, security, environmental or other obligations on our business.

***Risk of losses from rate reduction.*** Our LECs that operate pursuant to intrastate rate-of-return regulation are subject to state regulatory authority over their intrastate telecommunications service rates. State review of these rates could lead to rate reductions, which in turn could have a material adverse effect on our business, financial condition, results of operations, liquidity and/or the market price of our outstanding securities.

For a more thorough discussion of the regulatory issues that may affect our business, see "Item 1. Business—Regulatory and Legislative" included elsewhere in this Annual Report.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

Not applicable.

**ITEM 2. PROPERTIES**

We own or lease all of the properties material to our business. Our headquarters is located in Charlotte, North Carolina, in a leased facility. We also have administrative offices, maintenance facilities, rolling stock, central office and remote switching platforms, and transport and distribution network facilities in each of the 17 states in which we operate our LECs. Our facilities are generally located in or near the communities served by our LECs. Auxiliary battery or other non-utility power sources are located at each central office to provide uninterrupted service in the event of an electrical power failure. Transport and distribution network facilities include fiber optic backbone and copper wire distribution facilities, which connect customers to remote switch locations or to the central office and to points of presence or interconnection with the long distance carriers. These facilities are located on land pursuant to permits, easements or other agreements. Our rolling stock includes service vehicles, construction equipment and other required maintenance equipment.

We believe each of our respective properties is suitable and adequate for the business conducted thereon, is being appropriately used consistent with past practice and has sufficient capacity for the present intended purposes.

**ITEM 3. LEGAL PROCEEDINGS**

See the information under (i) "Legal Proceedings" in note (18) "Commitments and Contingencies" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" and (ii) "Class Action Complaint" in note (20) "Subsequent Events" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report, which we incorporate herein by reference.

From time to time, we are also subject to other legal and regulatory proceedings in the ordinary course of business. While management presently believes that the ultimate outcome of these proceedings, individually and in the aggregate, will not materially harm our financial position, cash flows, or overall trends in results of operations, legal proceedings are inherently uncertain, and unfavorable rulings could, individually or in aggregate, have a material adverse effect on our business, financial condition, or operating results.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

## PART II

**ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES****General Market Information, Holders and Dividends**

Our common stock is listed on the Nasdaq Capital Market (the "Nasdaq") under the symbol "FRP" and began trading on January 25, 2011.

The following table sets forth, for the periods indicated, the high and low sales prices per share of our common stock as reported on the Nasdaq. The stock price information is based on published financial sources.

<b>Year Ended December 31, 2016</b>	<b>High</b>	<b>Low</b>
First quarter	\$ 16.29	\$ 12.69
Second quarter	15.53	12.81
Third quarter	16.40	13.04
Fourth quarter	19.60	14.66

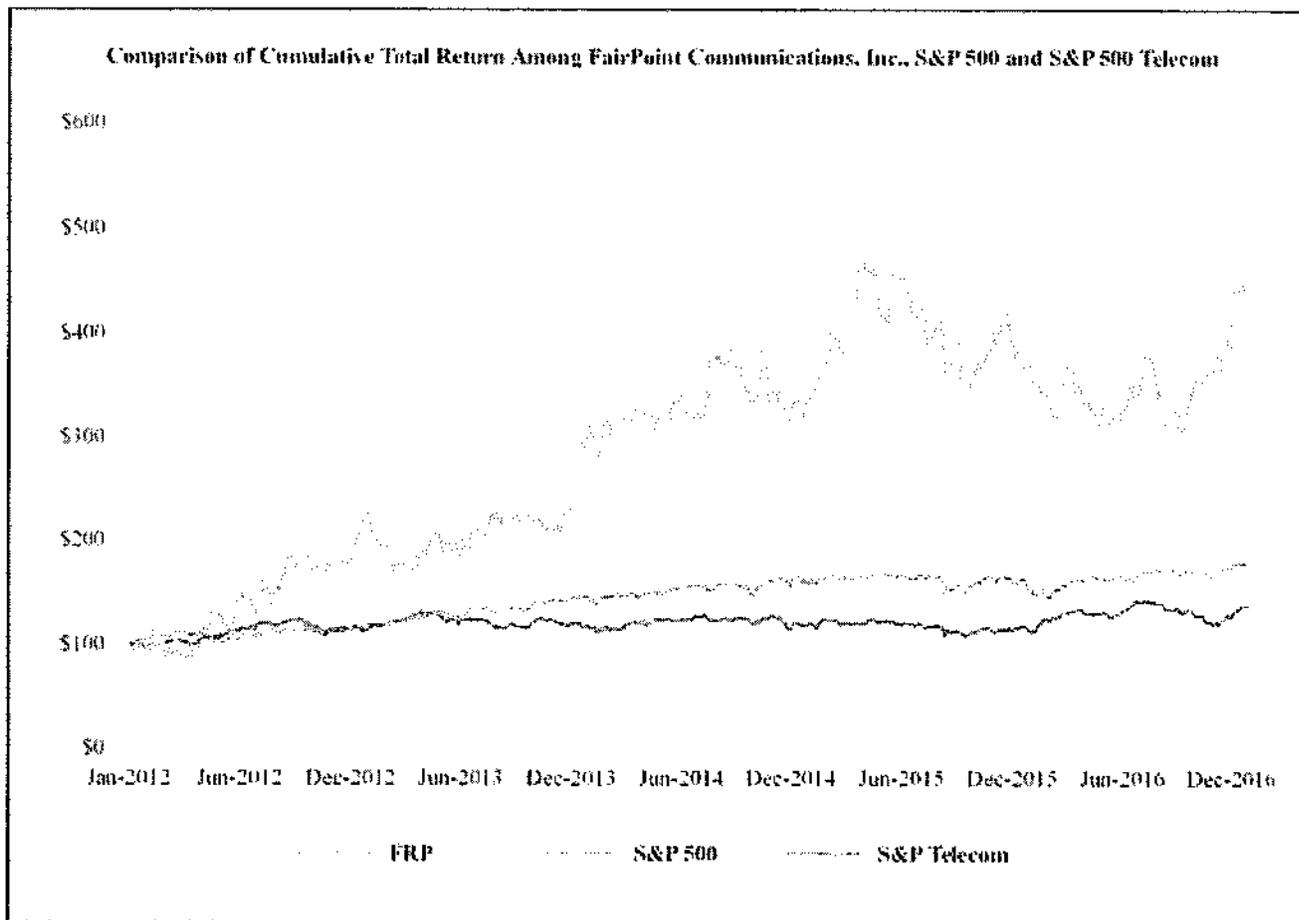
<b>Year Ended December 31, 2015</b>	<b>High</b>	<b>Low</b>
First quarter	\$ 18.08	\$ 13.51
Second quarter	20.98	17.24
Third quarter	19.07	14.93
Fourth quarter	18.87	14.56

No dividends were declared on any class of our common stock during the fiscal years 2016 or 2015. We currently do not pay any cash dividends on shares of our common stock and have no plans to pay cash dividends. Any determination to pay dividends in the future will be at the discretion of our board of directors and will depend upon limitations imposed by our results of operations, financial condition, contractual restrictions relating to indebtedness, restrictions imposed by applicable law and other factors our board of directors may deem relevant at the time.

As of February 27, 2017, there were approximately 174 holders of record of our common stock.

**Performance Graph**

Set forth below is a line graph comparing the cumulative total stockholder return on shares of our common stock against (i) the cumulative total return of all companies listed on the S&P 500 and (ii) the cumulative total return of the S&P 500 Telecom sector. The period compared commences on January 1, 2012 and ends on December 31, 2016. This graph assumes that \$100 was invested on January 1, 2012 in our common stock and in each of the market index and the sector index at the closing price for FairPoint Communications and the respective indices, and that all cash distributions were reinvested.



**Securities Authorized for Issuance under Equity Compensation Plans**

The table below provides information as of December 31, 2016 concerning securities authorized for issuance under our equity compensation plans. As of December 31, 2016, the FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan (the "Long Term Incentive Plan") was the only equity compensation plan under which securities of FairPoint Communications were authorized for issuance. The Board of Directors of the Company approved the Long Term Incentive Plan on March 14, 2014 and the stockholders of the Company approved it on May 12, 2014. The Long Term Incentive Plan, prior to its amendment and restatement, was approved by the United States Bankruptcy Court for the Southern District of New York in connection with our emergence from bankruptcy. For a description of the material features of the Long Term Incentive Plan, see note (16) "Stock-Based Compensation" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

Plan Category	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights <sup>(1)</sup>	(b) Weighted average exercise price of outstanding options, warrants and rights	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) <sup>(2)</sup>
Equity compensation plans approved by our stockholders	2,171,470	\$ 15.87	1,423,409
<b>Total</b>	<b>2,171,470</b>	<b>\$ 15.87</b>	<b>1,423,409</b>

- (1) Includes 2,171,470 options to purchase shares of common stock under the Long Term Incentive Plan, of which 1,184,859 options were issued prior to the amendment and restatement of the Long Term Incentive Plan on May 12, 2014 with a weighted average exercise price of \$16.88.
- (2) Each stock option granted reduces the availability under the Long Term Incentive Plan by one share. Prior to the amendment and restatement of the Long Term Incentive Plan on May 12, 2014, each restricted stock award granted reduced the availability under the Long Term Incentive Plan by one share. On or after May 12, 2014, each restricted stock award granted reduces the availability by 1.35 shares. Upon the exercise of each stock option or vesting of each restricted share award, one new share of common stock will be issued.

### Repurchase of Equity Securities

Under the Long Term Incentive Plan, employees may elect to have us withhold shares to satisfy minimum statutory federal, state and local tax withholding obligations arising from the vesting of restricted stock. When we withhold these shares, we are required to remit to the appropriate taxing authorities the market price of the shares withheld, which could be deemed a purchase of shares by us on the date of withholding.

### ITEM 6. SELECTED FINANCIAL DATA

The summary financial data presented below represents portions of our consolidated financial statements and are not complete. The following financial information should be read in conjunction with "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and notes thereto contained in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report. Historical results are not necessarily indicative of future performance or results of operations. Amounts are in thousands, except operating metrics, per share data and units.

	Years Ended December 31,				
	2016	2015	2014	2013	2012
<b>Results of Continuing Operations:</b>					
Revenues	\$ 824,443	\$ 859,465	\$ 901,396	\$ 939,354	\$ 973,649
Operating expenses	595,098	689,873	994,670	1,052,540	1,155,632
Income/(loss) from operations	229,345	169,592	(93,274)	(113,186)	(181,983)
Interest expense	82,697	80,718	80,371	78,675	67,610
Net income/(loss)	\$ 104,095	\$ 90,416	\$ (136,319)	\$ (103,494)	\$ (153,294)
Income/(loss) per share from continuing operations:					
Basic	\$ 3.88	\$ 3.39	\$ (5.15)	\$ (3.95)	\$ (5.90)
Diluted	3.84	3.35	(5.15)	(3.95)	(5.90)
Cash dividends per share	\$ —	\$ —	\$ —	\$ —	\$ —
Weighted average shares outstanding:					
Basic	26,854	26,652	26,449	26,190	25,987
Diluted	27,119	26,973	26,449	26,190	25,987
<b>Financial Position (at period end):</b>					
Cash, excluding restricted cash <sup>(1)</sup>	\$ 34,924	\$ 26,560	\$ 37,587	\$ 42,700	\$ 23,203
Total assets	1,230,835	1,322,526	1,452,371	1,574,547	1,714,874
Total long-term debt	904,770	906,545	908,641	911,021	955,889
Total stockholders' deficit	(54,077)	(1,489)	(600,284)	(309,196)	(317,813)
<b>Operating Data (at period end):</b>					
Broadband subscribers	306,624	311,130	319,915	328,183	324,850
Ethernet circuits	15,691	14,507	12,614	9,501	5,945
Residential voice lines	366,111	409,852	466,682	527,010	585,845
<b>Summary of Cash Flows:</b>					
Net cash provided by operating activities	\$ 134,252	\$ 112,001	\$ 121,063	\$ 171,085	\$ 192,775
Net cash used in investing activities	(118,460)	(115,871)	(118,363)	(95,951)	(144,307)
Net cash used in financing activities	(7,428)	(7,157)	(7,813)	(55,637)	(42,615)
Capital expenditures	117,050	116,159	119,489	128,298	145,066

(1) Cash excludes aggregate restricted cash of \$0.7 million, \$0.7 million, \$0.6 million, \$1.2 million and \$7.5 million at December 31, 2016, 2015, 2014, 2013 and 2012, respectively.

## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with our consolidated financial statements and the notes thereto in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report. The following discussion includes certain forward-looking statements. For a discussion of important factors, including the continuing development of our business, actions of regulatory authorities and competitors and other factors which could cause actual results to differ materially from the results referred to in the forward-looking statements, see "Item 1A. Risk Factors" and "Cautionary Note Regarding Forward-Looking Statements" included elsewhere in this Annual Report. Our discussion and analysis of financial condition and results of operations are presented in the following sections:

- Overview
- Executive Summary
- Proposed Merger with Consolidated Communications Holdings, Inc.
- Labor Matters
- Regulatory and Legislative
- Basis of Presentation
- Results of Operations
- Non-GAAP Financial Measures
- Liquidity and Capital Resources
- Off-Balance Sheet Arrangements
- Summary of Contractual Obligations
- Critical Accounting Policies and Estimates
- New Accounting Standards
- Inflation

### Overview

We are a leading provider of advanced communications services to business, wholesale and residential customers within our service territories. We offer our customers a suite of advanced services including Ethernet, SIP-Trunking, hosted PBX, managed services, data center colocation services, high capacity data transport and other IP-based services over our fiber-based network, in addition to Internet access, HSD and local and long distance voice services. Our service territory spans 17 states where we are the incumbent communications provider primarily serving rural communities and small urban markets. Many of our LECs have served their respective communities for more than 80 years. As of December 31, 2016, we operated with approximately 306,600 broadband subscribers, approximately 15,700 Ethernet circuits and approximately 366,100 residential voice lines.

We own and operate an extensive fiber-based Ethernet network with more than 22,000 miles of fiber optic cable, including approximately 18,000 miles of fiber optic cable in Maine, New Hampshire and Vermont, giving us capacity to support more HSD services and extend our fiber reach into more communities across the region. The IP/MPLS network architecture of our fiber-based network allows us to provide Ethernet, transport and other IP-based services with the highest level of reliability at a lower cost of service. This fiber-based Ethernet network also supplies critical infrastructure for wireless carriers serving the region as their bandwidth needs increase, driven by mobile data from smartphones, tablets and other wireless devices. As of December 31, 2016, we provide cellular transport, also known as backhaul, through over 1,900 mobile Ethernet backhaul connections. We have fiber connectivity to approximately 1,300 cellular communications towers in our service footprint.

### Executive Summary

Our mission is to empower businesses, consumers and communities with advanced data, IT and voice services by leveraging our network, technology and operational expertise to exceed their expectations. Our vision includes operating and technology platforms that will meet our customers' technology needs by providing them with reliable and secure connections and ready access to what matters most to them.

Our executive management team is focused on utilizing our network assets, our outstanding operating platform and our proven ability to develop and deploy market-driven products to build brand awareness, aid in generating new revenue and sustain existing revenue. We will enhance our network to bring new services and more robust technologies to our markets, enable effective and secure technology to ensure our product and service offerings remain competitive, and provide excellent customer service to create a loyal customer base, all while maintaining a sharp focus on managing costs.

Our objective is to transform our revenue by continuing to add advanced data products and services such as Ethernet, high capacity data transport and other IP-based services over our fiber-based network in addition to HSD services, to minimize our dependence on voice access lines. Communications companies, including us, continue to experience a decline in access lines due to increased competition from wireless carriers, cable television operators and CLECs and increased availability of alternative communications services, including wireless and voice over IP ("VoIP"). We will continue our efforts to retain customers to mitigate the loss of voice access lines through bundled packages, including video and other value added services. We believe access lines as a measure of the business are increasingly less meaningful measures of trend and are being replaced by revenue generating broadband subscribers and Ethernet circuits.

Over the past few years, we have made significant capital investments in our fiber-based Ethernet network to expand our business service offerings to meet the growing data needs of our customers and to increase broadband speeds and capacity in our consumer markets. We have also focused our sales and marketing efforts on these advanced data solutions. Specifically, within the last few years, we built and launched high capacity Ethernet services to allow us to meet the capacity needs of our business customers as well as supply high capacity infrastructure to our wholesale customers. In the past year, Ethernet demand has remained strong amid increased price pressure. We continue to see a market trend, largely led by cable companies, of reduced Ethernet prices to business and wholesale customers. We continue to see growth in Ethernet units and speeds amid declining prices in the market. Ethernet high-capacity transport data services are our flagship product and are laying the foundation not only for new business but also for additional IP-based advanced services in the future.

We believe that our extensive fiber network, with more than 22,000 miles of fiber optic cable, including approximately 18,000 miles of fiber optic cable in northern New England and approximately 1,300 cellular communications towers currently served with fiber, puts us in an excellent position to serve the cellular backhaul needs in our markets. We further believe the bandwidth needs of cellular backhaul will grow with the continued adoption of bandwidth-intensive technology. As a result, we expect to see wireless carriers developing new technologies as demand increases on existing fiber-connected towers, including the use of "small cell" architecture. By satisfying additional demand for bandwidth, both traditionally and through new and evolving technology, we expect to partially offset the decline we have seen, and expect to continue to see, in legacy wholesale offerings, including TDM transport services, DS1s, DS3s and wholesale switched access.

Coupled with recent regulatory reform in the states of Maine, New Hampshire and Vermont that will serve to promote fair competition among communications service providers in the region, we believe that there is a significant organic growth opportunity within the business and wholesale markets given our extensive fiber network and IP-based product suite, combined with our relative low market share in these areas.

#### **Proposed Merger with Consolidated Communications Holdings, Inc.**

On December 3, 2016, FairPoint Communications entered into the Merger Agreement with Consolidated and Merger Sub, which provides for, among other things, a business combination whereby Merger Sub will merge with and into FairPoint Communications, with FairPoint Communications as the surviving entity. As a result of the Merger, the separate corporate existence of Merger Sub will cease, and FairPoint Communications will survive as a wholly owned subsidiary of Consolidated. Consolidated is a leading business and broadband communications provider throughout its 11-state service area.

If the Merger is completed, under the terms of the Merger Agreement, stockholders of FairPoint Communications will receive 0.7300 shares of common stock of Consolidated for each share of FairPoint Communications common stock that they own immediately before this transaction. The Merger is expected to close around the middle of 2017 and is subject to standard closing conditions, including federal and state regulatory approvals and the approval of both Consolidated's and FairPoint Communications' stockholders. The required waiting period under the HSR Act was terminated on January 11, 2017.

For the year ended December 31, 2016, we recognized \$4.5 million of merger related expenses, primarily for legal and financial advisory costs.

The award agreements under the Long Term Incentive Plan provide that upon the occurrence of a change in control, unvested benefits will be accelerated and vest in full.

## Labor Matters

Two of our collective bargaining agreements in northern New England were ratified on February 22, 2015 by their respective unions. Members of these two labor unions initiated a work stoppage on October 17, 2014 and returned to work on February 25, 2015. The respective collective bargaining agreements expire in August 2018. For the year ended December 31, 2015, we recognized \$48.9 million of labor negotiation related expenses, primarily for contracted services, contingent workforce expenses (including training) and legal, communications and public relations expenses.

See notes (11) "Employee Benefit Plans" and (12) "Income Taxes" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report for further information, as well as "Results of Operations" herein.

## Regulatory and Legislative

We are generally subject to common carrier regulation primarily by federal and state governmental agencies. At the federal level, the FCC generally exercises jurisdiction over common carriers, such as us, to the extent those carriers provide, originate or terminate interstate or international communications. State regulatory commissions generally exercise jurisdiction over common carriers to the extent those carriers provide, originate or terminate intrastate telecommunications. In addition, pursuant to the Communications Act, state and federal regulators share responsibility for implementing and enforcing the domestic pro-competitive policies introduced by that legislation.

We are required to comply with the Communications Act which requires, among other things, that common carriers offer communications services at just and reasonable rates and on terms and conditions that are not unreasonably discriminatory. The Communications Act also contains requirements intended to promote competition in the provision of local services and lead to deregulation as markets become more competitive.

For a detailed description of the federal and state regulatory environment in which we operate and the FCC's recently promulgated CAF/ICC Order and other recent regulatory changes, as well as the effects and potential effects of such regulation on us, see "Item 1. Business—Regulatory and Legislative" included elsewhere in this Annual Report. The impact of these changes for 2016 is described further below. However, in the long run, we are uncertain of the ultimate impact as federal and state regulations continue to evolve.

## Basis of Presentation

We view our business of providing data, voice and communications services to business, wholesale and residential customers as one reportable segment.

## Results of Operations

The following table sets forth our consolidated operating results reflected in our consolidated statements of operations for the years ended December 31, 2016, 2015 and 2014, respectively. The comparisons of financial results are not necessarily indicative of future results (in thousands, except for operating metrics):

	Years Ended December 31,		
	2016	2015	2014
<b>Revenues:</b>			
Voice services	\$ 297,441	\$ 323,412	\$ 362,491
Access	239,761	256,617	267,938
Data and Internet services	187,268	178,620	175,490
Regulatory funding	51,411	53,818	45,556
Other	48,562	46,998	49,921
<b>Total revenues</b>	<b>824,443</b>	<b>859,465</b>	<b>901,396</b>
<b>Operating expenses:</b>			
Cost of services and sales, excluding depreciation and amortization	389,316	430,308	440,979
Other post-employment benefit and pension (benefit)/expense	(213,760)	(170,338)	75,282
Selling, general and administrative expense, excluding depreciation and amortization	197,239	206,046	257,627
Depreciation and amortization	222,303	223,819	220,678
Reorganization related expense	—	38	104
<b>Total operating expenses</b>	<b>595,098</b>	<b>689,873</b>	<b>994,670</b>
<b>Income/(loss) from operations</b>	<b>229,345</b>	<b>169,592</b>	<b>(93,274)</b>
<b>Other income/(expense):</b>			
Interest expense	(82,697)	(80,718)	(80,371)
Other, net	296	485	7,548
<b>Total other expense</b>	<b>(82,401)</b>	<b>(80,233)</b>	<b>(72,823)</b>
<b>Income/(loss) before income taxes</b>	<b>146,944</b>	<b>89,359</b>	<b>(166,097)</b>
Income tax (expense)/benefit	(42,849)	1,057	29,778
<b>Net income/(loss)</b>	<b>\$ 104,095</b>	<b>\$ 90,416</b>	<b>\$ (136,319)</b>

Select Operating Metrics:	As of December 31,		
	2016	2015	2014
Broadband subscribers	306,624	311,130	319,915
Ethernet circuits	15,691	14,507	12,614
Residential voice lines	366,111	409,852	466,682

### Voice Services Revenues

We receive revenues through the provision of local calling services to business and residential customers, generally for a fixed monthly charge and service charges for special calling features. We also generate revenue through long distance services within our service areas on our network and through resale agreements with national interexchange carriers. For the years ended December 31, 2016, 2015 and 2014, residential voice lines in service decreased 10.7%, 12.2% and 11.4% year-over-year, respectively, which directly impacts local voice services revenues and our opportunity to provide long distance services to our customers, resulting in a decrease of minutes of use. The decline in residential voice lines in 2015 and 2014 may have been partially due to the impact of the strike on service levels. Evolving competition, including reduced voice pricing from cable competitors as well as cellular adoption, has contributed to the decrease in residential voice lines. There are very few areas within our northern New England footprint where cable voice service and cellular are not alternatives for our customers. In addition, business voice services revenue also declined in part

because of reduced access lines as businesses shifted from traditional voice products to our Ethernet or other advanced services. We expect the trend of decline in voice lines in service, and thereby a decline in aggregate voice services revenue, to continue as customers continue to turn to the use of alternative communication services as a result of ever-increasing competition.

Effective June 1, 2015, the Performance Assurance Plan ("PAP") that was previously adopted in each of the states of Maine, New Hampshire and Vermont was retired and we began measuring and reporting certain wholesale local service performance results pursuant to the terms of a simplified measurement plan. The new plan, called the Wholesale Performance Plan ("WPP"), was developed collaboratively with CLECs over several years and was approved by the Maine, New Hampshire and Vermont regulatory commissions. Under the WPP, we are subject to significantly fewer performance criteria and our annual service penalty

exposure was reduced from a maximum of \$87 million to a maximum of \$12 million (\$4.75 million in each of Maine and New Hampshire and \$2.5 million in Vermont). A portion of the service credits resulting from these commitments were recorded to voice services revenues; however, the majority were recorded to access revenues.

The following table reflects the primary drivers of year-over-year changes in voice services revenues (dollars in millions):

	Year ended December 31, 2016 vs. December 31, 2015		Year ended December 31, 2015 vs. December 31, 2014			
	Increase (Decrease)	%	Increase (Decrease)	%		
Local voice services revenues, excluding:	\$	(20.6)	\$	(30.8)		
Long distance services revenues		(5.6)		(8.4)		
Increase in accrual of PAP/WPP service credits <sup>(1)</sup>		0.2		0.1		
<b>Total change in voice services revenues</b>	<b>\$</b>	<b>(26.0)</b>	<b>(8)%</b>	<b>\$</b>	<b>(39.1)</b>	<b>(11)%</b>

(1) There was an insignificant amount of PAP/WPP service credits during the year ended December 31, 2016. During the years ended December 31, 2015 and 2014, PAP/WPP service credits resulted in a decrease of \$0.2 million and \$0.3 million, respectively, to local voice services revenues.

### Access Revenues

We receive revenues for the provision of network access through carrier Ethernet based products and legacy access products to end user customers and long distance and other competing carriers who use our local exchange facilities to provide interexchange services to their customers. Network access can be provided to carriers and end users that buy dedicated local and interexchange capacity to support their private networks (i.e. special access) or it can be derived from fixed and usage-based charges paid by carriers for access to our local network (i.e. switched access).

Carriers are migrating from legacy access products, such as DS1, DS3, frame relay, ATM and private line, to carrier Ethernet based products. During the years ended December 31, 2016, 2015 and 2014, wholesale Ethernet circuits grew by 12.3%, 17.1% and 44.4% year-over-year, respectively. These carrier Ethernet based products are more sustainable, but generally, at the outset, have lower average revenue per user of broadband capacity than the legacy products they are replacing, resulting in a decline in access revenues. We expect the decline in access revenues to continue with customer migration. This decline in legacy access products is expected to be partially offset with the increasing need for bandwidth, including cellular backhaul and demand for carrier Ethernet based products, both of which are expected to increase over time. With the entry of cable competitors into the wholesale market, we continue to experience an increased decline in access lines due to this new competition. However, our extensive fiber-based Ethernet network with more than 22,000 miles of fiber optic cable (of which approximately 18,000 miles are in Maine, New Hampshire and Vermont), including approximately 1,300 cellular communications towers currently served with fiber, puts us in a position to grow our revenue base as demand for cellular backhaul and other Ethernet services expands. We also construct new fiber routes to cellular communications towers when the business case presents itself. Additionally, we continue to evaluate new services to provide to carriers, including the selective use of dark fiber and professional services, to continue to meet carrier access needs.

As described above, we adopted a separate PAP for certain services provided on a wholesale basis to CLECs in each of the states of Maine, New Hampshire and Vermont, pursuant to which we are required to issue service credits in the event we are unable to meet the provisions of the respective PAP. These PAPs were retired effective June 1, 2015 and replaced with the WPP. Our maximum exposure to wholesale service credits has been reduced through the implementation of the WPP. The service credits are allocated to access revenues or voice services revenues based on services provided to the wholesale carrier.

In June 2014, Maine established a new POLR SQI standard, which may subject us to future SQI penalties.

The following table reflects the primary drivers of year-over-year changes in access revenues (dollars in millions):

	Year ended December 31, 2016 vs. December 31, 2015		Year ended December 31, 2015 vs. December 31, 2014			
	Increase (Decrease)	%	Increase (Decrease)	%		
Carrier Ethernet services <sup>(1)</sup>	\$	1.6	\$	9.3		
Legacy access services <sup>(2)</sup>		(19.3)		(20.8)		
Decrease in accrual of PAP/WPP service credits <sup>(3)</sup>		0.8		0.2		
<b>Total change in access revenues</b>	<b>\$</b>	<b>(16.9)</b>	<b>(7)%</b>	<b>\$</b>	<b>(11.3)</b>	<b>(4)%</b>

(1) We offer carrier Ethernet services throughout our market to our business and wholesale customers, which include Ethernet virtual circuit technology for cellular backhaul. As of December 31, 2016, we provide cellular transport on our fiber-



based Ethernet network through over 1,900 fiber-to-the-tower connections compared to over 1,900 and 1,700 as of December 31, 2015 and 2014, respectively.

- (2) Legacy access services include products such as DS1, DS3, frame relay, ATM and private line.
- (3) During the years ended December 31, 2016, 2015 and 2014, PAP/WPP service credits resulted in a decrease of \$0.2 million, \$1.0 million and \$1.2 million to access revenues, respectively.

### *Data and Internet Services Revenues*

We receive revenues from monthly recurring charges for the provision of data and Internet services to residential and business customers through DSL technology, fiber-to-the-home technology, retail Ethernet, Internet dial-up, high speed cable modem and wireless broadband.

We have invested in our broadband network to extend the reach and capacity of the network to customers who did not previously have access to data and Internet products and to offer more competitive services to existing customers, including retail Ethernet products. During the years ended December 31, 2016, 2015 and 2014, retail Ethernet circuits grew by 2.8%, 12.4%, and 20.5% respectively. Our broadband subscribers decreased by 1.4%, 2.7% and 2.5% during the years ended December 31, 2016, 2015 and 2014, respectively, which directly impacts data and Internet services revenues. We expect to continue our investment in our broadband network to further grow data and Internet services revenues in the coming years.

The following table reflects the primary drivers of year-over-year changes in data and Internet services revenues (dollars in millions):

	Year ended December 31, 2016 vs. December 31, 2015		Year ended December 31, 2015 vs. December 31, 2014	
	Increase (Decrease)	%	Increase (Decrease)	%
Retail Ethernet services <sup>(1)</sup>	\$ 0.6		\$ 4.9	
Other data and Internet technology based services <sup>(2)</sup>	8.0		(1.8)	
<b>Total change in data and Internet services revenues</b>	<b>\$ 8.6</b>	<b>5%</b>	<b>\$ 3.1</b>	<b>2%</b>

- (1) Retail Ethernet services revenue is comprised of data services provided through E-LAN, E-LINE and E-DIA technology on our fiber-based Ethernet network. During the years ended December 31, 2016, 2015 and 2014, we recognized \$43.0 million, \$42.4 million and \$37.5 million, respectively, of retail Ethernet revenues.

- (2) Includes all other services such as DSL, dial-up, high speed cable modem and wireless broadband.

### *Regulatory Funding Revenues*

We receive certain federal and state government funding that we classify as regulatory funding, which is further described in "Regulatory and Legislative" herein, including: CAF Phase II support effective January 1, 2015 to build and operate broadband services; CAF Phase II transition funding; CAF Phase I frozen support (for Kansas and Colorado and until a reverse auction is completed); CAF funding under the CAF/ICC Order; and universal service fund support from certain states in which we operate. During the years ended December 31, 2016, 2015 and 2014, we recognized \$51.4 million, \$53.8 million and \$45.6 million, respectively, of regulatory funding revenues. The year-over-year changes are primarily due to the timing of CAF Phase II transitional revenue. CAF Phase II support revenue does not include any funding for Colorado and Kansas. We expect the amount of regulatory funding revenue to decline as the amount of CAF Phase II transition funding decreases in 2016 and is phased out through 2018.

### Other Services Revenues

We receive revenues from other services, including special purpose projects on behalf of third parties, video services (including cable television and video-over-DSL), billing and collection, directory services, the sale and maintenance of customer premise equipment and certain other miscellaneous revenues. Other services revenues also include revenue we receive from late payment charges to end users and interexchange carriers. Due to the composition of other services revenues, it is difficult to predict future trends.

The following table reflects the primary drivers of year-over-year changes in other services revenues (dollars in millions):

	Year ended December 31, 2016 vs. December 31, 2015		Year ended December 31, 2015 vs. December 31, 2014	
	Increase (Decrease)	%	Increase (Decrease)	%
Special purpose projects <sup>(1)</sup>	\$ 0.4		\$ (3.8)	
Late payment fees <sup>(2)</sup>	—		0.4	
Other <sup>(3)</sup>	1.2		0.5	
<b>Total change in other services revenues</b>	<b>\$ 1.6</b>	<b>3%</b>	<b>\$ (2.9)</b>	<b>(6)%</b>

- (1) Special purpose projects are completed on behalf of third party requests.
- (2) Late payment fees are related to customers who have not paid their bills in a timely manner.
- (3) Other revenues were primarily attributable to revenue from value added reseller of unified communications, data networking and cabling infrastructure solutions, in addition to fluctuations in directory services, billing and collections and in various other miscellaneous services revenues.

**Supplementary revenue information.** In addition to the revenue information discussed above, we are providing the following additional strategic revenue categorization information. Management believes that providing this additional revenue information will afford better visibility into our revenue trends as a result of product and service evolution within our industry. Management believes these metrics will enhance investors' ability to evaluate our business and assist investors in their understanding of the changing composition of our revenue (in millions).

	Years Ended December 31,		
	2016	2015	2014
<b>Growth (1)</b>			
Broadband (1a)	\$ 141.8	\$ 135.6	\$ 138.7
Ethernet (1b)	98.1	95.9	81.6
Hosted and Advanced Services (1c)	17.9	13.4	12.5
<b>Subtotal Growth</b>	<b>257.8</b>	<b>244.9</b>	<b>232.8</b>
<i>Growth as a % of Total Revenue</i>	<i>31.3%</i>	<i>28.5%</i>	<i>25.8%</i>
<b>Convertible (2)</b>			
Non-Ethernet Special Access (2a)	66.6	79.9	94.7
Business Voice (2b)	119.0	127.7	134.1
Other Convertible (2c)	20.5	23.9	28.9
<b>Subtotal Convertible</b>	<b>206.1</b>	<b>231.5</b>	<b>257.7</b>
<i>Convertible as a % of Total Revenue</i>	<i>25.0%</i>	<i>26.9%</i>	<i>28.6%</i>
<b>Legacy (3)</b>			
Residential Voice (3a)	212.1	226.0	245.6
Switched Access and Other (3b)	65.9	74.7	83.7
<b>Subtotal Legacy</b>	<b>278.0</b>	<b>300.7</b>	<b>329.3</b>
<i>Legacy as a % of Total Revenue</i>	<i>33.7%</i>	<i>35.0%</i>	<i>36.5%</i>
<b>Regulatory funding (4)</b>			
	51.4	53.8	45.5
<i>Regulatory funding as a % of Total Revenue</i>	<i>6.2%</i>	<i>6.3%</i>	<i>5.0%</i>
<b>Miscellaneous (5)</b>			
	31.1	28.6	36.1
<i>Miscellaneous as a % of Total Revenue</i>	<i>3.8%</i>	<i>3.3%</i>	<i>4.1%</i>
<b>Total Revenue</b>	<b>\$ 824.4</b>	<b>\$ 859.5</b>	<b>\$ 901.4</b>

(1) Growth revenue is comprised of products and services that are generally viewed as in-demand by communications consumers over the medium- to long-term and are expected to increase over time.

a) Broadband revenue is comprised of both residential and business customers delivered through DSL, ADSL, VDSL or other similar services.

b) Ethernet revenue includes Ethernet over copper ("EOC") or Ethernet over fiber ("EOF") services delivered to end-users or to wholesalers, who then sell to their end-users.

c) Hosted and Advanced Services includes VoIP and other digital voice services including unified messaging and other IP features as well as revenue generated from our various advanced services including our value added reseller of unified communications, data networking and cabling infrastructure solutions, the next-generation emergency 9-1-1 contracts in several of our service territories as well as data center and managed services.

(2) Convertible revenues are revenues that could move from TDM-based technologies to Ethernet or other advanced services.

a) Non-Ethernet Special Access includes high-capacity circuits. The revenues are primarily comprised of business revenue from T1's, DS3's and SONET products.

b) Business Voice is traditional voice, long distance, ISDN and Centrex services for a business customer.

c) Other Convertible primarily includes Unbundled Network Element ("UNE"), Asynchronous Transfer Mode ("ATM"), Frame Relay, ISDN, Analog Private Line and Internet services such as dial-up.

(3) Legacy revenues are TDM-based voice related consumer revenue largely related to residential customers.

a) Residential Voice is comprised of TDM voice services to residential customers.

b) Switched Access and Other primarily includes Switched Transport, Local Switching, NECA pooling elements and colocation of miscellaneous equipment.

(4) Refer to the definition of "Regulatory Funding Revenues" above.

(5) Miscellaneous is comprised of special purpose projects, late payment fees from our customers and pole rental revenues among other various service revenues.

The primary drivers of the year-over-year changes in the strategic revenue categorization for the year ended December 31, 2016 compared to 2015 were:

- Growth revenue increased \$12.9 million as we experienced growth in broadband revenue as speed upgrades and rate increases helped offset a decline in broadband subscribers as well as increased hosted and advanced services revenue and increased Ethernet revenue due to customer growth.
- Convertible revenue decreased \$25.4 million as customers continued to migrate from non-Ethernet circuits and businesses shifted from traditional voice products to VoIP and hosted products.
- Legacy revenue decreased \$22.7 million resulting from a decline in voice access lines due to fewer lines in service and lower legacy switched access revenue versus a year ago.
- Regulatory funding revenue decreased \$2.4 million primarily due to the timing of CAF Phase II transitional revenue.
- Miscellaneous revenue increased \$2.5 million due to lower PAP/WPP service credits, revenue assurance activities and higher special purpose projects.

The primary drivers of the year-over-year changes in the strategic revenue categorization for the year ended December 31, 2015 compared to 2014 were:

- Growth revenue increased \$12.1 million as we experienced growth in Ethernet while price increases for broadband services and speed upgrades helped offset a decline in broadband subscribers.
- Convertible revenue decreased \$26.2 million as customers migrated from non-Ethernet circuits and businesses shifted from traditional voice products to VoIP and hosted products.
- Legacy revenue decreased \$28.6 million resulting from the loss of voice access lines versus a year ago combined with lower long distance usage.
- Regulatory funding revenue increased \$8.3 million due to our acceptance of CAF Phase II and the corresponding transitional revenue of \$8.8 million associated with that program.
- Miscellaneous revenue decreased \$7.5 million due to higher special purpose projects in the first quarter of 2014 and revenue assurance.

### Cost of Services and Sales

Cost of services and sales includes the following costs directly attributable to a service or product: salaries and wages, benefits (including stock based compensation, but excluding the net periodic benefit cost of other post-employment benefit plans and qualified pension plans), materials and supplies, contracted services, network access and transport costs, customer provisioning costs, computer systems support and cost of products sold. Aggregate customer care costs, which include billing and service provisioning, are allocated between cost of services and sales and selling, general and administrative expenses. We expect the cost of services and sales to fluctuate with revenue and decrease due to lower employee expenses from a reduction in headcount, partially offset by expected merger related expenses in 2017, including increased stock-based compensation expense described in "Proposed Merger with Consolidated Communications Holdings, Inc." herein.

The following table reflects the primary drivers of year-over-year changes in cost of services and sales (dollars in millions):

	Year ended December 31, 2016 vs. December 31, 2015		Year ended December 31, 2015 vs. December 31, 2014	
	Increase (Decrease)	%	Increase (Decrease)	%
Employee expense <sup>(1)</sup>	\$ 2.8		\$ (1.7)	
Labor negotiation related expense <sup>(2)</sup>	(40.3)		1.9	
Severance expense <sup>(3)</sup>	1.0		1.7	
Network and access expense <sup>(4)</sup>	0.9		(10.9)	
Other <sup>(5)</sup>	(5.4)		(1.7)	
<b>Total change in cost of services and sales</b>	<b>\$ (41.0)</b>	<b>(10)%</b>	<b>\$ (10.7)</b>	<b>(2)%</b>

(1) For the years ended December 31, 2016, 2015 and 2014, we recognized \$163.5 million, \$160.7 million and \$162.4 million, respectively, of employee expense as cost of services and sales. The increase for 2016 compared to 2015 is primarily due to the work stoppage described in "Labor Matters" herein partially offset by a reduction in headcount. The decrease for 2015 compared to 2014 is primarily due to the work stoppage described in "Labor Matters" herein as well as a reduction in headcount, partially offset by a decrease in capitalized labor associated with a reduction in labor intensive capital projects in 2015 versus 2014.

(2) Labor negotiation related expense is related primarily to contracted services incurred during the years ended December 31,

2015 and 2014 as a result of the work stoppage described in "Labor Matters" herein.

- (3) For the years ended December 31, 2016, 2015 and 2014, we recognized \$3.7 million, \$2.7 million and \$1.0 million of severance expense, respectively, attributed to the reduction in our workforce.
- (4) Network and access expense continues to decrease primarily due to lower revenue as well as cost management efforts.
- (5) Other cost of services and sales has decreased primarily due to lower provisioning and lower back-office expenses.

#### *Other Post-Employment Benefit and Pension (Benefit)/Expense*

We expect other post-employment benefit and pension (benefit)/expense to increase in 2017 compared to 2016 since the prior service credit was fully amortized during 2016.

The following table reflects the primary drivers of year-over-year changes in other post-employment benefit and pension (benefit)/expense (dollars in millions):

	Year ended December 31, 2016 vs. December 31, 2015		Year ended December 31, 2015 vs. December 31, 2014	
	Increase (Decrease)	%	Increase (Decrease)	%
Other post-employment benefits expense/(benefit) <sup>(1)</sup>	\$ (43.7)		\$ (236.1)	
Pension expense <sup>(2)</sup>	0.3		(9.5)	
<b>Total change in other post-employment benefit and pension (benefit)/expense</b>	<b>\$ (43.4)</b>	<b>25%</b>	<b>\$ (245.6)</b>	<b>(326)%</b>

- (1) The decrease in the 2016 net periodic benefit cost compared to 2015 for our other post-employment benefit plans is primarily attributable to the decrease in amortization expense of the net actuarial loss of \$31.6 million and additional amortization of the net prior service credits of \$4.0 million as well as decreases in service and interest costs resulting from the lower benefit obligation.

The decrease in the 2015 net periodic benefit cost compared to 2014 for our other post-employment benefit plans is primarily attributable to the benefit recognized from amortization of net prior service credits of \$304.6 million partially offset by the amortization expense of the net actuarial loss of \$113.4 million in 2015, a decrease in interest cost resulting from the lower obligation and a decrease in service cost due to elimination of benefits for active represented employees.

At December 31, 2015, we recognized actuarial losses of \$32.8 million, which resulted in a decrease in the amount of actuarial losses being amortized in 2016 compared to 2015. At December 31, 2014, we recognized actuarial losses of \$148.4 million, which resulted in an increase in the amount of actuarial losses being amortized in 2015 compared to 2014. The actuarial gains/losses can be attributed primarily to the change in discount rates.

See note (11) "Employee Benefit Plans" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report for further information on our other post-employment benefit plans.

- (2) The increase in the 2016 net periodic benefit cost compared to 2015 for our qualified pension plans is primarily attributable to a plan curtailment recognized in the third quarter of 2015 as a result of a workforce reduction partially offset by a decrease in service cost, a decrease in the amortization of actuarial losses and an increase in return on assets.

The decrease in the 2015 net periodic benefit cost compared to 2014 for our qualified pension plans is primarily attributable to a decrease in service cost, amortization of prior service credit and a plan curtailment recognized in the third quarter of 2015 as a result of a workforce reduction partially offset by an increase in amortization of actuarial losses. The prior service credit is related to pension bands that were frozen under the terms of the collective bargaining agreements.

The decrease in service cost in 2016 compared to 2015 resulted from a reduction in the projected benefit obligation. The reduction in the projected benefit obligation used to measure service cost in 2016 and 2015 is primarily the result of the collective bargaining agreements described in "Labor Matters" herein.

At December 31, 2015, we recognized actuarial gains of \$31.7 million, which resulted in a decrease in the amount of actuarial losses being amortized in 2016 compared to 2015. At December 31, 2014, we recognized actuarial losses of \$66.7 million, which resulted in an increase in the amount of actuarial losses being amortized in 2015 compared to 2014. The actuarial gains/losses can be attributed primarily to the change in discount rates and the gains/losses incurred on payment of significant lump sums in each of those years.

See note (11) "Employee Benefit Plans" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report for further information on our company-sponsored qualified pension plans.

### ***Selling, General and Administrative Expense***

Selling, general and administrative ("SG&A") expense includes salaries and wages and benefits (including stock based compensation, but excluding the net periodic benefit cost of other post-employment benefit plans and qualified pension plans) not directly attributable to a service or product, bad debt charges, taxes other than income, advertising and sales commission costs, customer billing, call center and information technology costs, professional service fees and rent for administrative space. We expect SG&A expense to increase primarily due to expected merger related expenses in 2017, including increased stock-based compensation expense described in "Proposed Merger with Consolidated Communications Holdings, Inc." herein.

The following table reflects the primary drivers of year-over-year changes in SG&A expense (dollars in millions):

	Year ended December 31, 2016 vs. December 31, 2015		Year ended December 31, 2015 vs. December 31, 2014	
	Increase (Decrease)	%	Increase (Decrease)	%
Employee expense <sup>(1)</sup>	\$ 0.1		\$ (9.1)	
Labor negotiation related expense <sup>(2)</sup>	(7.8)		(26.0)	
Operating taxes	(0.2)		(5.7)	
Bad debt expense <sup>(3)</sup>	(5.2)		(3.4)	
Severance expense <sup>(4)</sup>	(0.2)		0.3	
Merger related expense <sup>(5)</sup>	4.5		—	
Other <sup>(6)</sup>	—		(7.7)	
<b>Total change in SG&amp;A expense</b>	<b>\$ (8.8)</b>	<b>(4)%</b>	<b>\$ (51.6)</b>	<b>(20)%</b>

- (1) For the years ended December 31, 2016, 2015 and 2014, we recognized \$101.9 million, \$101.8 million and \$110.9 million, respectively, of employee expense in SG&A expense. The increase in 2016 compared to 2015 is primarily due to the work stoppage described in "Labor Matters" herein partially offset by a reduction in headcount. The decrease in 2015 compared to 2014 is primarily attributable to the work stoppage described in "Labor Matters" herein and reduction in headcount.
- (2) Labor negotiation related expense is primarily related to contingent workforce expenses as well as communications and public relations, legal and training expenses during the years ended December 31, 2015 and 2014.
- (3) For the years ended December 31, 2016, 2015 and 2014, we recognized \$0.6 million, \$5.8 million and \$9.2 million of bad debt expense, respectively.
- (4) For the years ended December 31, 2016, 2015 and 2014, we recognized \$1.1 million, \$1.3 million and \$1.0 million of severance expense, respectively.
- (5) Merger related expense is primarily related to legal and financial advisory costs during the year ended December 31, 2016 in connection with the Merger described in "Proposed Merger with Consolidated Communications Holdings, Inc." herein.
- (6) The change in other expenses is primarily due to the timing of spending for contracted services and advertising costs.

### ***Depreciation and Amortization***

Depreciation and amortization includes depreciation of our communications network and equipment and amortization of intangible assets. We require significant capital expenditures to maintain, upgrade and enhance our network facilities and operations. We expect our capital expenditures and depreciation expense to remain consistent in the coming years. We expect amortization expense to remain consistent throughout the remainder of our intangible assets' useful lives.

For the years ended December 31, 2016, 2015 and 2014, we recognized \$211.3 million, \$212.8 million and \$209.7 million of depreciation expense, respectively. The decrease in depreciation expense for the year ended December 31, 2016 compared to December 31, 2015 was primarily due to higher retirements than additions. The increase in depreciation expense for the year ended December 31, 2015 compared to December 31, 2014 was primarily due to higher additions than retirements. We recognized \$11.0 million, \$11.0 million and \$11.0 million of amortization expense in the years ended December 31, 2016, 2015 and 2014, respectively.

### Interest Expense

The following table reflects a summary of interest expense recorded during the years ended December 31, 2016, 2015 and 2014, respectively (in millions):

	Years Ended December 31,		
	2016	2015	2014
Credit Agreement Loans (as defined hereinafter)	\$ 48.7	\$ 49.0	\$ 49.5
Notes (as defined hereinafter)	26.3	26.3	26.3
Amortization of debt issue costs	1.2	1.2	1.1
Amortization of debt discount	3.3	3.1	2.9
Interest rate swap agreements	2.4	0.6	—
Other interest expense	0.8	0.5	0.6
<b>Total interest expense</b>	<b>\$ 82.7</b>	<b>\$ 80.7</b>	<b>\$ 80.4</b>

Interest expense increased \$2.0 million (2.5%) in the year ended December 31, 2016 compared to the year ended December 31, 2015 primarily due to interest rate swap agreements, with an effective date of September 30, 2015. Interest expense increased \$0.3 million (0.4%) in the year ended December 31, 2015 compared to the year ended December 31, 2014.

For further information regarding the Credit Agreement Loans and the Notes, see "Liquidity and Capital Resources—Debt" herein and note (8) "Long-term Debt" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

### Other Income, Net

Other income generally includes non-operating gains and losses. During the years ended December 31, 2016, 2015 and 2014, net other income was \$0.3 million, \$0.5 million and \$7.5 million, respectively.

As required by the Plan, the FairPoint Litigation Trust (the "Trust") was created and the Company transferred to the Trust the "Litigation Trust Claims", as defined in the FairPoint Litigation Trust Agreement among the Company, its subsidiaries and the trustee. The Trust thereafter settled the "Litigation Trust Claims" against Verizon Communications Inc. During 2014, we received payment from the settlement proceeds and recorded one-time, non-operating income of \$6.7 million.

### Income Taxes

The Company recorded tax expense on the pre-tax net income for the year ended December 31, 2016 of \$42.8 million and a tax benefit on the pre-tax net income/(loss) for the years ended December 31, 2015 and 2014 of \$1.1 million and \$29.8 million, respectively, which equates to an effective tax rate of 29.2%, (1.2)% and 17.9%, respectively. For 2016, the effective tax rate differs from the 35% federal statutory rate primarily due to a tax benefit associated with a decrease in the valuation allowance offset by tax expense related to state taxes. For 2015, the effective tax rate differs from the statutory rate primarily due to a decrease in the valuation allowance as well as a tax benefit related to state taxes. A tax benefit recorded on pre-tax income for the year ended December 31, 2015 resulted in a negative effective tax rate. For 2014, the effective tax rate differs from the statutory rate primarily due an increase to the valuation allowance offset by a tax benefit related to state taxes.

For further information, see note (12) "Income Taxes" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

## Non-GAAP Financial Measures

We report our financial results in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The table below includes certain non-GAAP financial measures and the adjustments to the most directly comparable GAAP measure used to determine the non-GAAP measures. Management believes that the non-GAAP measures may be useful to investors in understanding period-to-period operating performance and in identifying historical and prospective trends that may not otherwise be apparent when relying solely on GAAP financial measures. In addition, management believes the non-GAAP measures are useful for investors because they enable them to view performance in a manner similar to the method used by the Company's management. Management believes earnings before interest, taxes, depreciation and amortization ("EBITDA"), as adjusted to exclude the effect of items that are further described below ("Adjusted EBITDA"), provides a useful measure of covenant compliance and Unlevered Free Cash Flow (as defined below) may be useful to investors in assessing the Company's ability to generate cash and meet its debt service requirements. The maintenance covenants contained in the Company's credit facility are based on Consolidated EBITDA, which is consistent with the calculation of Adjusted EBITDA below.

For purposes of calculating Adjusted EBITDA (in accordance with the definition of Consolidated EBITDA in our Credit Agreement), costs, expenses and charges related to the renegotiation of labor contracts including, but not limited to, expenses for third-party vendors and losses related to disruption of operations (including any associated penalties under service level agreements and regulatory performance plans) are permitted to be excluded from the calculation. We believe this includes, among others, the costs paid to third-parties for the contingent workforce and service quality penalties due to the disruption of operations. On October 17, 2014, two of our labor unions in northern New England initiated a work stoppage and returned to work on February 25, 2015. As a result, significant union employee and vehicle and other related expenses related to northern New England were not incurred between October 17, 2014 and February 24, 2015 (the "work stoppage period"). Therefore, to assist in the evaluation of the Company's operating performance without the impact of the work stoppage, we estimated the union employee and vehicle and other related expenses using historical data for the work stoppage period that we believe would have been incurred absent the work stoppage ("Estimated Avoided Costs"). Estimated Avoided Costs is a pro forma estimate only. Actual costs absent the strike may have been different. In 2014 and 2015, had our incumbent workforce been in place, actual labor costs during the work stoppage period may have been higher than the \$33 million and \$27 million, respectively, recorded as Estimated Avoided Costs due to significant winter storm activity that increased our service demands; however, those incremental storm-related costs would have been an allowed add back to Adjusted EBITDA under the Credit Agreement. Estimated employee expenses avoided during the work stoppage period include salaries and wages, bonus, overtime, capitalized labor, benefits, payroll taxes, travel expenses and other employee related costs based on a trailing 12-month average calculated per striking employee per day during the work stoppage period less any actual expense incurred. Estimated vehicle fuel and maintenance expense savings, which resulted from the contingent workforce utilizing their own vehicles, for the work stoppage period were estimated based on a trailing 12-month average of historical costs less actual expense incurred. Management believes "Adjusted EBITDA minus Estimated Avoided Costs" and "Unlevered Free Cash Flow minus Estimated Avoided Costs" may be useful to investors in understanding our operating performance without the impact of the two unions' work stoppage in northern New England as described elsewhere in this Annual Report.

The non-GAAP financial measures, as used herein, are not necessarily comparable to similarly titled measures of other companies. Furthermore, these non-GAAP measures have limitations as analytical tools and should not be considered in isolation from, or as an alternative to, net income or loss, operating income, cash flow or other combined income or cash flow data prepared in accordance with GAAP. Because of these limitations, Adjusted EBITDA, Adjusted EBITDA minus Estimated Avoided Costs, Unlevered Free Cash Flow and Unlevered Free Cash Flow minus Estimated Avoided Costs should not be considered as measures of discretionary cash available to invest in business growth or reduce indebtedness. The Company compensates for these limitations by relying primarily on its GAAP results and using the non-GAAP measures only supplementally.

A reconciliation of Adjusted EBITDA, Adjusted EBITDA minus Estimated Avoided Costs, Unlevered Free Cash Flow and Unlevered Free Cash Flow minus Estimated Avoided Costs to net income/(loss) is provided in the table below (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Net income/(loss)	\$ 104,095	\$ 90,416	\$ (136,319)
Income tax expense/(benefit)	42,849	(1,057)	(29,778)
Interest expense	82,697	80,718	80,371
Depreciation and amortization	222,303	223,819	220,678
Pension expense (1a)	8,967	8,635	18,144
Other post-employment benefits expense/(benefit) (1a)	(222,727)	(178,973)	57,138
Compensated absences (1b)	(350)	(1,645)	2,848
Severance	4,863	4,014	2,005
Reorganization costs (1c)	—	38	104
Storm expenses (1d)	—	—	145
Other non-cash items, net (1e)	6,830	8,197	2,537
Labor negotiation related expense (1f)	—	48,933	73,590
All other allowed adjustments, net (1f)	4,312	(170)	(889)
Adjusted EBITDA (1) (4)	253,839	282,925	290,574
Estimated Avoided Costs (3)	—	(27,000)	(33,000)
<b>Adjusted EBITDA minus Estimated Avoided Costs</b>	<b>\$ 253,839</b>	<b>\$ 255,925</b>	<b>\$ 257,574</b>
Adjusted EBITDA (1) (4)	\$ 253,839	\$ 282,925	\$ 290,574
Pension contributions	(15,475)	(14,168)	(28,266)
Other post-employment benefits payments	(5,715)	(5,597)	(5,808)
Capital expenditures	(117,050)	(116,159)	(119,489)
Unlevered Free Cash Flow (2)	115,599	147,001	137,011
Estimated Avoided Costs (3)	—	(27,000)	(33,000)
<b>Unlevered Free Cash Flow minus Estimated Avoided Costs</b>	<b>\$ 115,599</b>	<b>\$ 120,001</b>	<b>\$ 104,011</b>

(1) For purposes of calculating Adjusted EBITDA (in accordance with the definition of Consolidated EBITDA in the Credit Agreement), the Company adjusts net income/(loss) for interest, income taxes, depreciation and amortization, in addition to:

- (a) the add-back of aggregate pension and other post-employment benefits expense,
- (b) the add-back (or subtraction) of the adjustment to the compensated absences accrual to eliminate the impact of changes in the accrual,
- (c) the add-back of costs related to the reorganization, including professional fees for advisors and consultants,
- (d) the add-back of costs and expenses, including those imposed by regulatory authorities, with respect to casualty events, acts of God or force majeure to the extent they are not reimbursed from proceeds of insurance,
- (e) the add-back of other non-cash items, including stock compensation expense, except to the extent they will require a cash payment in a future period, and
- (f) the add-back (or subtraction) of other items, including facility and office closures, expenses related to permitted transactions, labor negotiation related expenses (including losses related to disruption of operations), non-cash gains/losses and non-operating dividend and interest income and other extraordinary gains/losses.

(2) Unlevered Free Cash Flow refers to Adjusted EBITDA (calculated in accordance with the definition of Consolidated EBITDA in the Credit Agreement) minus capital expenditures, cash pension contributions and other post-employment benefits cash payments.

(3) See paragraphs preceding the table above for information regarding the calculation of this non-GAAP measure.

(4) On October 16, 2014, we received payment from the Trust settlement proceeds and recorded one-time, non-operating income of \$6.7 million, which is included in the calculation of Adjusted EBITDA. For further information regarding this payment, see "Results of Operations—Other Income" included herein.

## Liquidity and Capital Resources

### Overview

Our current and future liquidity is dependent upon our operating results. We expect that our primary sources of liquidity will be net cash provided by operating activities, cash on hand and funds available under the Revolving Facility. Our short-term and long-term liquidity needs arise primarily from:

- (i) interest and principal payments on our indebtedness;
- (ii) capital expenditures;
- (iii) working capital requirements as may be needed to support and grow our business; and
- (iv) contributions to our qualified pension plans and payments under our other post-employment benefit plans.

Based on our current and anticipated levels of operations and conditions in our markets, we believe that cash on hand, the Revolving Facility and net cash provided by operating activities will enable us to meet our working capital, capital expenditure, debt service and other funding requirements for at least the next 12 months. We were in compliance with the maintenance covenants contained in the Credit Agreement (as defined hereinafter in "Debt—February 2013 Refinancing") through the end of 2016 and expect to remain in compliance for 2017.

### Cash Flows

Cash at December 31, 2016 totaled \$34.9 million compared to \$26.6 million at December 31, 2015, excluding restricted cash of \$0.7 million and \$0.7 million, respectively. During 2016, cash flows from operations of \$134.3 million, which included outflows due to the scheduled semi-annual interest payments on the Notes and the payment of 2015 annual performance bonuses, were partially offset by cash outflows largely associated with \$117.1 million of capital expenditures. During 2015, cash flows from operations of \$112.0 million, which included outflows due to the scheduled semi-annual interest payments on the Notes and the payment of 2014 annual performance bonuses, were partially offset by cash outflows largely associated with \$116.2 million of capital expenditures.

The following table sets forth our consolidated cash flow results reflected in our consolidated statements of cash flows (in millions):

Net cash flows provided by (used in):	Years Ended December 31,		
	2016	2015	2014
Operating activities	\$ 134.3	\$ 112.0	\$ 121.1
Investing activities	(118.5)	(115.9)	(118.4)
Financing activities	(7.4)	(7.1)	(7.8)
<b>Net increase/(decrease) in cash</b>	<b>\$ 8.4</b>	<b>\$ (11.0)</b>	<b>\$ (5.1)</b>

**Operating activities.** Net cash provided by operating activities is our primary source of funds. Net cash provided by operating activities for 2016 increased \$22.3 million compared to 2015, primarily due to lower labor negotiation related expenses, lower operating expenses, partially offset by a reduction in revenues.

Net cash provided by operating activities for 2015 decreased \$9.1 million compared to 2014, primarily due to increased labor negotiation related expenses and a reduction in revenues partially offset by lower operating expenses as well as lower cash pension contributions.

**Investing activities.** Net cash used in investing activities for 2016 increased \$2.6 million compared to 2015. Capital expenditures were \$117.1 million, \$116.2 million and \$119.5 million for the years ended December 31, 2016, 2015 and 2014, respectively. In addition, we completed an immaterial business acquisition during 2016. Net cash used in investing activities for 2015 decreased \$2.5 million compared to 2014.

**Financing activities.** Net cash used in financing activities for 2016 increased \$0.3 million compared to 2015, primarily due to increased repayments of capital lease obligations. Net cash used in financing activities for 2015 decreased \$0.7 million compared to 2014, primarily due to a reduction in repayments of capital lease obligations.

### Pension Contributions and Post-Employment Benefit Plan Expenditures

During the year ended December 31, 2016, we contributed \$16.5 million to our Company sponsored qualified defined benefit pension plans and funded benefit payments of \$5.7 million under our post-employment benefit plans.



On August 8, 2014, the Highway and Transportation Funding Act (the "Act") was signed into law. This Act contained a pension funding stabilization provision which allows pension plan sponsors to use higher discount rate assumptions when determining the funded status and, accordingly, the funding obligations for its pension plans.

The provisions of the Act resulted in our 2016 minimum required pension plan contribution being lower than it would have been in the absence of this stabilization provision. We believe that the intent of the stabilization provision is to alter the timing of pension plan contributions, not to reduce the long-term funding of pension plans. Accordingly, the relief we will receive as a result of the stabilization provision may be temporary in nature in that our near-term minimum required contributions will be less than they otherwise would have been without the passage of this Act and will increase in the medium to long-term.

In 2017, we expect our aggregate cash pension contributions and cash post-employment benefit payments to be approximately \$24 million. See "Item 1A. Risk Factors—The amount we are required to contribute to our qualified pension plans and post-employment benefit plans is impacted by several factors that are beyond our control and changes in those factors may result in a significant increase in future cash contributions."

### *Capital Expenditures*

We require significant capital expenditures to maintain, upgrade and enhance our network facilities and operations. In 2016, our net capital expenditures totaled \$117.1 million, compared to \$116.2 million in 2015. We anticipate that we will fund future capital expenditures through cash flows from operations and cash on hand (including amounts available under the Revolving Facility). In 2017, capital expenditures are expected to be between \$110 million to \$115 million. Our capital expenditures in the coming years will be impacted by our CAF Phase II elections as further described in "Regulatory and Legislative" herein.

### *Debt*

**February 2013 Refinancing.** On February 14, 2013 (the "Refinancing Closing Date"), we completed the refinancing of our old credit agreement (the "Refinancing"). In connection with the Refinancing, we (i) issued \$300.0 million aggregate principal amount of 8.75% senior secured notes due in 2019 (the "Notes") in a private offering exempt from registration under the Securities Act pursuant to an indenture that we entered into on the Refinancing Closing Date (the "Indenture") and (ii) entered into a new credit agreement (the "Credit Agreement"), dated as of the Refinancing Closing Date. The Credit Agreement provides for a \$75.0 million revolving credit facility, including a sub-facility for the issuance of up to \$40.0 million in letters of credit (the "Revolving Facility"), and a \$640.0 million term loan facility (the "Term Loan" and, together with the Revolving Facility, the "Credit Agreement Loans"). On the Refinancing Closing Date, we used the proceeds of the Notes offering, together with \$640.0 million of borrowings under the Term Loan and cash on hand to (i) repay principal of \$946.5 million outstanding on the old term loan, plus approximately \$7.7 million of accrued interest and (ii) pay approximately \$32.6 million of fees, expenses and other costs related to the Refinancing.

**The Credit Agreement.** In connection with the Refinancing, we entered into the Credit Agreement, which provides for the \$75.0 million Revolving Facility, including a sub-facility for the issuance of up to \$40.0 million in letters of credit, and the \$640.0 million Term Loan. The principal amount of the Term Loan and commitments under the Revolving Facility may be increased by an aggregate amount up to \$200.0 million, subject to certain terms and conditions specified in the Credit Agreement. The Term Loan will mature on February 14, 2019 and the Revolving Facility will mature on February 14, 2018, subject in each case to extensions pursuant to the terms of the Credit Agreement. As of December 31, 2016, we had \$61.1 million, net of \$13.9 million of outstanding letters of credit, available for borrowing under the Revolving Facility.

**Interest Rates and Fees.** Interest on borrowings under the Credit Agreement Loans accrue at an annual rate equal to either LIBOR or the base rate, in each case plus an applicable margin. LIBOR is the per annum rate for an interest period of one, two, three or six months (at our election), with a minimum LIBOR floor of 1.25% for the Term Loan. The base rate for any date is the per annum rate equal to the greatest of (x) the federal funds effective rate plus 0.50%, (y) the rate of interest publicly quoted from time to time by The Wall Street Journal as the United States "Prime Rate" and (z) LIBOR with an interest period of one month plus 1.00%. The applicable margin for the Term Loan is (a) 6.25% per annum with respect to term loans bearing interest based on LIBOR or (b) 5.25% per annum with respect to term loans bearing interest based on the base rate. The applicable rate for the Revolving Facility is, initially, (a) 5.50% with respect to revolving loans bearing interest based on LIBOR or (b) 4.50% per annum with respect to revolving loans bearing interest based on the base rate, in each case subject to adjustment based on our consolidated total leverage ratio, as defined in the Credit Agreement. We are required to pay a quarterly letter of credit fee on the average daily amount available to be drawn under letters of credit issued under the Revolving Facility equal to the applicable rate for revolving loans bearing interest based on LIBOR plus a fronting fee of 0.125% per annum on the average daily amount available to be drawn under such letters of credit. In addition, we are required to pay a quarterly commitment fee on the average daily unused portion of the Revolving Facility, which is 0.50% initially, subject to reduction to 0.375% based on our consolidated total leverage ratio. In the third quarter of 2013, we entered into interest rate swap agreements with a combined notional amount of \$170.0 million with three counterparties that are effective for a two year period beginning on September 30, 2015 and maturing on September



30, 2017. Each respective swap agreement requires us to pay a fixed rate of 2.665% and provides that we will receive a variable rate based on the three month LIBOR rate, subject to a minimum LIBOR floor of 1.25%. Amounts payable by or due to us will be net settled with the respective counterparties on the last business day of each fiscal quarter, commencing December 31, 2015. For further information regarding these agreements, see note (9) "Interest Rate Swap Agreements" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

*Security Guarantors.* All obligations under the Credit Agreement, together with certain designated hedging obligations and cash management obligations, are unconditionally guaranteed on a senior secured basis by certain subsidiaries of FairPoint Communications (the "Subsidiary Guarantors") and secured by a first-priority lien on substantially all personal property of FairPoint Communications and the Subsidiary Guarantors, subject to certain exclusions set forth in the related security documents, pari passu with the lien securing the obligations under the Notes.

*Mandatory Repayments.* We are required to make quarterly repayments of the Term Loan in a principal amount equal to \$1.6 million during the term of the Credit Agreement, with such repayments being reduced based on the application of mandatory and optional prepayments of the Term Loan made from time to time. In addition, mandatory repayments are due under the Credit Agreement with (i) a percentage, initially equal to 50% and subject to reduction to 25% in subsequent fiscal years based on our consolidated total leverage ratio, of our excess cash flow, as defined in the Credit Agreement, (ii) the net cash proceeds of certain asset dispositions, insurance proceeds and condemnation awards and (iii) issuances of debt not permitted to be incurred under the Credit Agreement. No premium is required in connection with prepayments. We did not make any optional or mandatory prepayments under the Credit Agreement, excluding mandatory quarterly repayments discussed above, during the years ended December 31, 2016 and 2015. In addition, we were not required to make an excess cash flow payment for fiscal year 2016.

*Covenants.* The Credit Agreement contains customary representations and warranties and affirmative and negative covenants for a transaction of this type, including two financial maintenance covenants: (i) a consolidated interest coverage ratio and (ii) a consolidated total leverage ratio. The Credit Agreement also contains a covenant limiting the maximum amount of capital expenditures that we and our subsidiaries may make in any fiscal year.

*Events of Default.* The Credit Agreement also contains customary events of default.

*The Notes.* On the Refinancing Closing Date, we issued \$300.0 million in aggregate principal amount of the Notes pursuant to the Indenture in a private offering exempt from registration under the Securities Act.

The terms of the Notes are governed by the Indenture. The Notes are senior secured obligations of FairPoint Communications and are guaranteed by the Subsidiary Guarantors. The Notes and the guarantees thereof are secured by a first-priority lien on substantially all personal property of FairPoint Communications and the Subsidiary Guarantors, subject to certain exclusions set forth in the related security documents, pari passu with the lien securing the obligations under the Credit Agreement. The Notes will mature on August 15, 2019 and accrue interest at a rate of 8.75% per annum, which is payable semi-annually in arrears on February 15 and August 15 of each year.

Notes redeemed after February 15, 2016 and prior to February 15, 2017 may be redeemed at 104.375% of the aggregate principal amount; Notes redeemed on or after February 15, 2017 and prior to February 15, 2018 may be redeemed at 102.188% of the aggregate principal amount; and Notes redeemed on or after February 15, 2018 may be redeemed at their par value.

The holders of the Notes have the ability to require us to repurchase all or any part of the Notes if we experience certain kinds of changes in control or engage in certain asset sales, in each case at the repurchase prices and subject to the terms and conditions set forth in the Indenture.

The Indenture contains certain covenants which are customary with respect to non-investment grade debt securities, including limitations on our ability to incur additional indebtedness, pay dividends on or make other distributions or repurchase our capital stock, make certain investments, enter into certain types of transactions with affiliates, create liens and sell certain assets or merge with or into other companies. These covenants are subject to a number of important limitations and exceptions.

The Indenture also provides for customary events of default, including cross defaults to other specified debt of FairPoint Communications and certain of its subsidiaries.

#### **Off-Balance Sheet Arrangements**

As of December 31, 2016 and December 31, 2015 we had \$13.9 million and \$14.2 million, respectively, in outstanding letters of credit under the Revolving Facility and \$4.1 million and \$4.0 million, respectively, of surety bonds. We do not have any other off-balance sheet arrangements other than our operating lease obligations, which are not reflected on our balance sheet. See "—Summary of Contractual Obligations" for further detail.



### Summary of Contractual Obligations

The following table discloses aggregate information about our contractual obligations as of December 31, 2016 and the periods in which payments are due (in thousands):

Contractual Obligations	Payments due by period				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-term debt obligations, including current maturities <sup>(a)</sup>	\$ 916,000	\$ 6,400	\$ 909,600	\$ —	\$ —
Interest payments on long-term debt obligations <sup>(b)</sup>	170,375	75,763	94,612	—	—
Capital lease obligations, including current maturities	3,034	1,279	1,475	280	—
Operating lease obligations	17,759	6,644	7,519	2,857	739
Purchase obligations <sup>(c)</sup>	19,524	13,471	5,822	231	—
Other long-term liabilities <sup>(d)</sup>	269,070	25,569	20,833	15,715	206,953
<b>Total contractual obligations</b>	<b>\$ 1,395,762</b>	<b>\$ 129,126</b>	<b>\$ 1,039,861</b>	<b>\$ 19,083</b>	<b>\$ 207,692</b>

- (a) Long-term debt obligations exclude outstanding letters of credit totaling \$13.9 million under the Revolving Facility at December 31, 2016. For more information, *see* note (8) "Long-term Debt" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.
- (b) Interest payments represent cash payments on the long-term debt, including payments associated with interest rate swaps, while excluding amortization of capitalized debt issuance costs.
- (c) Purchase obligations represent commitments for maintenance and support of network equipment and software, which we consider to be material.
- (d) Other long-term liabilities primarily include our qualified pension and post-employment benefit obligations, and deferred tax liabilities. For more information, *see* notes (11) "Employee Benefit Plans" and (12) "Income Taxes" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report. In addition,
- (i) The balance excludes \$3.8 million of reserves for uncertain tax positions, including interest and penalties, that were included in deferred tax liabilities at December 31, 2016 for which we are unable to make a reasonably reliable estimate as to when cash settlements with taxing authorities will occur;
  - (ii) The balance includes the current portion of our post-employment benefit obligations of \$7.1 million presented in the current portion of other accrued liabilities at December 31, 2016; and
  - (iii) Our 2017 pension contribution is expected to be approximately \$18 million and has been reflected as due in less than one year. Our actual contribution could differ from this estimation. Due to uncertainties in the pension funding calculation, the amount and timing of any other pension contributions are unknown and therefore the remaining accrued pension obligation has been reflected as due in more than 5 years.

### Critical Accounting Policies and Estimates

As disclosed in note (2) "Significant Accounting Policies" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report, the preparation of our financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions about future events that affect the amounts reported in our consolidated financial statements and accompanying notes. Actual results could differ significantly from those estimates. We believe that the following discussion addresses our most critical accounting policies, which are those that are most important to the portrayal of our financial condition and results of operations and require management's most difficult, subjective and complex judgments. Our critical accounting policies as of December 31, 2016 are as follows:

- Revenue recognition;
- Allowance for doubtful accounts;
- Accounting for qualified pension and other post-employment benefits;
- Accounting for income taxes;
- Depreciation of property, plant and equipment;
- Stock-based compensation; and

- Valuation of long-lived assets and indefinite-lived intangible assets.

**Revenue Recognition.** We recognize service revenues based upon usage of our local exchange network and facilities and contract fees. Fixed fees for voice services, Internet services and certain other services are recognized in the month the service is provided. Revenue from other services that are not fixed fee or that exceed contracted amounts is recognized when those services are provided. Non-recurring customer activation fees, along with the related costs up to, but not exceeding, the activation fees, are deferred and amortized over the customer relationship period. SQI penalties and certain PAP/WPP service credits are recorded as a reduction to revenue.

We recognize certain revenues pursuant to various cost recovery programs from state and federal USF, CAF/ICC and from revenue sharing agreements with other LECs administered by the National Exchange Carrier Association ("NECA"). Revenues are calculated based on our investment in our network and other network operations and support costs. We have historically collected revenues recognized through this program; however, adjustments to estimated revenues in future periods are possible. These adjustments could be necessitated by adverse regulatory developments with respect to these subsidies and revenue sharing arrangements, changes in the allowable rates of return, the determination of recoverable costs and/or decreases in the availability of funds in the programs due to increased participation by other carriers.

We make estimated adjustments, as necessary, to revenue and accounts receivable for billing errors, including certain disputed amounts. If circumstances related to these adjustments change or our knowledge evolves, our estimate of the recoverability of our accounts receivable could be further reduced from the levels provided in our consolidated financial statements.

**Allowance for Doubtful Accounts.** In evaluating the collectability of our accounts receivable, we assess a number of factors, including a specific customer's or carrier's ability to meet its financial obligations to us, the length of time the receivable has been past due and historical collection experience. Based on these assessments, we record both specific and general reserves for uncollectible accounts receivable to reduce the related accounts receivable to the amount we ultimately expect to collect from customers and carriers. If circumstances change or economic conditions worsen such that our past collection experience is no longer relevant, our estimate of the recoverability of our accounts receivable could be further reduced from the levels reflected in our accompanying consolidated balance sheet.

**Accounting for Qualified Pension and Other Post-employment Benefits.** Certain of our employees participate in our qualified pension plans and other post-employment benefit plans. In the aggregate, the projected benefit obligations of the qualified pension plans exceed the fair value of their respective assets and the post-employment benefit plans do not have plan assets, resulting in expense. Significant qualified pension and other post-employment benefit plan assumptions, including the discount rate used, the long-term rate-of-return on plan assets, and medical cost trend rates are periodically updated and impact the amount of benefit plan income, expense, assets and obligations reflected in our consolidated financial statements. The actuarial assumptions we used in determining our qualified pension and post-employment benefit plans obligations may differ materially from actual results due to changing market and economic conditions, higher or lower withdrawal rates or longer or shorter life spans of participants. While we believe that the assumptions used are appropriate, differences in actual experience or changes in assumptions might materially affect our financial position or results of operations.

Our qualified pension and post-employment benefit liabilities are highly sensitive to changes in the discount rate. We currently estimate that a movement of 1% in the discount rate would change our December 31, 2016 qualified pension plan benefit obligations by approximately 17%. We currently estimate that a 1% fluctuation in the discount rate would change our December 31, 2016 post-employment benefit obligations by approximately 12%.

The post-employment benefit obligations are also highly sensitive to the medical trend rate assumption. A 1% increase in the medical trend rate assumed for post-employment benefits at December 31, 2016 would result in an increase in the post-employment benefit obligations of approximately \$10.1 million and a 1% decrease in the medical trend rate assumed at December 31, 2016 would result in a decrease in the post-employment benefit obligations of approximately \$8.4 million.

For additional information on our qualified pension and post-employment benefit plans, see note (11) "Employee Benefit Plans" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

**Accounting for Income Taxes.** Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management



determines its estimates of future taxable income based upon the scheduled reversal of deferred tax liabilities and tax planning strategies. The Company establishes valuation allowances for deferred tax assets when it is estimated to be more likely than not that the tax assets will not be realized.

FairPoint Communications files a consolidated income tax return with its subsidiaries. All intercompany transactions and accounts have been eliminated in consolidation.

**Depreciation of Property, Plant and Equipment.** We recognize depreciation on property, plant and equipment principally on the composite group remaining life method and straight-line composite rates. This method provides for the recognition of the cost of the remaining net investment in telephone plant, less anticipated net salvage value (if any), over the remaining asset lives. When an asset is retired, the original cost, net of salvage value, is charged against accumulated depreciation and no immediate gain or loss is recognized on the disposition of the asset. Under this method, we review depreciable lives periodically and may revise depreciation rates when appropriate. The Company utilizes straight-line depreciation for its non-telephone property, plant and equipment.

Periodically, the Company reviews the estimated remaining useful lives of its group asset categories to address continuing changes in technology, competition and the Company's overall reduction in capital spending and increased focus on more efficient utilization of its existing assets.

**Stock-based Compensation.** Compensation expense for share-based awards made to employees and directors are recognized based on the estimated fair value of each award over the award's vesting period. We estimate the fair value of share-based payment awards on the date of grant using one of the following: an option-pricing model for stock options; the closing market value of our stock for restricted stock and non-market performance share awards; and the Monte Carlo valuation model for market performance share awards. We expense the value of the portion of the award that is ultimately expected to vest over the requisite service period in the statement of operations. We assess the probability of achievement of the performance conditions for the non-market performance share awards at each period-end.

We utilize the Black-Scholes option pricing model to calculate the fair value of our stock option grants and the Monte Carlo valuation method to estimate the fair value of the market portion of the performance share awards. The key assumptions used include the expected life of the stock option, the expected dividend rate, the risk-free interest rate, expected volatility and potential total shareholder return outcomes. The expected life of the stock options granted represents the period of time that the options are expected to be outstanding. The risk-free interest rates are based on United States Treasury yields in effect at the date of grant consistent with the expected life. The expected volatility used in the Black-Scholes option pricing model reflects our historical volatility. Our assumptions of these key inputs, in addition to our assumption made about the portion of the awards that will ultimately vest, requires subjective judgment.

For additional information on share-based awards, including key assumptions used in calculating the grant date fair values, see note (16) "Stock-Based Compensation" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

**Valuation of Long-lived Assets and Indefinite-lived Intangible Assets.** We review our long-lived assets, which include our amortizable intangible assets, for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. In addition, we review non-amortizable intangible assets for impairment on at least an annual basis as of the first day of the fourth quarter of each year, or more frequently whenever indicators of impairment exist. Indicators of impairment could include, but are not limited to:

- an inability to perform at levels that were forecasted;
- a decline in planned revenues;
- a permanent decline in market capitalization;
- implementation of restructuring plans;
- changes in industry trends; and/or
- unfavorable changes in our capital structure, cost of debt, interest rates or capital expenditures levels.

Our only material non-amortizable intangible asset is the FairPoint trade name. An annual quantitative impairment analysis was performed on October 1, 2016. We assess the fair value of our trade name utilizing the relief from royalty method. If the carrying amount of our trade name exceeds its estimated fair value, the asset is considered impaired. For this annual impairment review, we made certain assumptions including an estimated royalty rate, long-term growth rate, effective tax rate and discount rate and applied these assumptions to projected future cash flows, exclusive of cash flows associated with wholesale and other revenues not generated through brand recognition. As of October 1, 2016, the estimated fair value exceeded the carrying value;

therefore, an impairment was not necessary. However, future changes in one or more of our assumptions discussed above may result in the recognition of an impairment loss.

For additional information on our FairPoint trade name, see note (6) "Other Intangible Assets" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

#### **New Accounting Standards**

For details of recent Accounting Standards Updates and our evaluation of their adoption on our consolidated financial statements, see note (4) "Recent Accounting Pronouncements" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

#### **Inflation**

There are cost of living adjustment clauses in certain of the collective bargaining agreements covering our labor union employees. Considerable fluctuations in cost of living due to inflation could result in an adverse effect on our operations.

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to market risk in the normal course of our business operations due to ongoing investing and funding activities, including those associated with the variable interest rate in our Credit Agreement and our qualified pension plan assets. Market risk refers to the potential change in fair value of a financial instrument as a result of fluctuations in interest rates, fixed income securities and equity prices. We do not hold or issue derivative instruments, derivative commodity instruments or other financial instruments for trading or speculative purposes. Our primary market risk exposures are interest rate risk and investment risk as follows:

**Interest Rate Risk - Long-Term Debt.** We are exposed to interest rate risk, primarily as it relates to the variable interest rates we are charged under credit agreements to which we are a party. As of December 31, 2016, our interest rate risk exposure was attributable to the Credit Agreement, which includes the Term Loan and the Revolving Facility, each of which is subject to variable interest rates. We use our variable rate debt, in addition to fixed rate debt, to finance our operations and capital expenditures and believe it is prudent to limit the variability of our interest payments on our variable rate debt. To meet this objective, from time to time, we may enter into interest rate derivative agreements to manage fluctuations in cash flows resulting from interest rate risk.

As of December 31, 2016, we were party to interest rate swap agreements in connection with borrowings under the Credit Agreement covering a combined notional amount of \$170.0 million. These agreements were effective on September 30, 2015. Accordingly, on December 31, 2016, only \$446.0 million principal balance of the Term Loan was subject to interest rate risk. Interest payments on the Term Loan are subject to a LIBOR floor of 1.25%. As a result, while LIBOR remains below 1.25%, we incur interest at above market rates. To the extent that LIBOR remains below 1.25%, we are buffered from the full financial impact of interest rate risk; however, as LIBOR rises, a change in interest rates could materially affect our consolidated financial statements. For example, with the principal balance of the Term Loan as of December 31, 2016, a 1% increase in the interest rate above the LIBOR floor of 1.25% would unfavorably impact interest expense and pre-tax earnings by approximately \$4.5 million on an annual basis.

For further information regarding the Credit Agreement, see "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources," and note (8) "Long-Term Debt" and note (9) "Interest Rate Swap Agreements" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

**Interest Rate and Investment Risk - Pension Plans.** We are exposed to risks related to the fair value of our pension plan assets and the discount rate used to value our pension plan liabilities and the amount of lump-sum payments made to certain participants. Our pension plan assets consist of a portfolio of fixed income securities, equity securities and cash. Changes in the fair value of this portfolio can occur due to changes in interest rates and the general economy. In addition, interest rates are a primary factor in the determination of our actuarially determined liabilities and, if applicable, the amount of the accrued benefit paid in the form of a lump-sum to a pension plan retiree when requested. Our qualified pension plan assets have historically funded a large portion of the benefits paid under our qualified pension plans. Lower returns on plan assets, decreases in the fair value of plan assets and lower discount rates could negatively impact the funded status of our pension plans and we may be required to make larger contributions to our pension plans than currently anticipated. Due to uncertainties in the pension funding calculation, the amount and timing of pension contributions are unknown other than as disclosed in this Annual Report. For activity in our qualified pension plan assets, see note (11) "Employee Benefit Plans" to our consolidated financial statements in "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report.

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA****INDEX TO FINANCIAL STATEMENTS**

	<u>Page</u>
<b>FAIRPOINT COMMUNICATIONS, INC. AND SUBSIDIARIES:</b>	
Report of Management on Internal Control Over Financial Reporting	58
Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting	59
Report of Independent Registered Public Accounting Firm	60
Report of Independent Registered Public Accounting Firm	61
<b>CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2016, 2015 AND 2014:</b>	
Consolidated Balance Sheets as of December 31, 2016 and December 31, 2015	62
Consolidated Statements of Operations for the Years Ended December 31, 2016, 2015 and 2014	63
Consolidated Statements of Comprehensive Income/(Loss) for the Years Ended December 31, 2016, 2015 and 2014	64
Consolidated Statements of Stockholders' Deficit for the Years Ended December 31, 2016, 2015 and 2014	65
Consolidated Statements of Cash Flows for the Years Ended December 31, 2016, 2015 and 2014	66
Notes to Consolidated Financial Statements	67

### Report of Management on Internal Control Over Financial Reporting

We, the management of FairPoint Communications, Inc., are responsible for establishing and maintaining adequate internal control over financial reporting of the Company. Management has evaluated internal control over financial reporting of the Company as of December 31, 2016 using the criteria for effective internal control established in *Internal Control-Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Based on such evaluation, management determined that the Company's internal control over financial reporting was effective as of December 31, 2016.

BDO USA, LLP, our independent registered public accounting firm who audited the financial statements included in this Annual Report, has issued an attestation report on the Company's internal control over financial reporting. This report appears on the following page.

/s/ Paul H. Sunu

**Paul H. Sunu**

Chief Executive Officer

/s/ Karen D. Turner

**Karen D. Turner**

Executive Vice President and Chief Financial Officer

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
FairPoint Communications, Inc.  
Charlotte, North Carolina

We have audited FairPoint Communications, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). FairPoint Communications, Inc. and subsidiaries' management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, FairPoint Communications, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of FairPoint Communications, Inc. and subsidiaries as of December 31, 2016, and the related consolidated statements of operations, comprehensive income (loss), stockholders' deficit, and cash flows for the year then ended and our report dated March 6, 2017 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP

Atlanta, Georgia  
March 6, 2017

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
FairPoint Communications, Inc.  
Charlotte, North Carolina

We have audited the accompanying consolidated balance sheet of FairPoint Communications, Inc. and subsidiaries as of December 31, 2016 and the related consolidated statements of operations, comprehensive income (loss), stockholders' deficit, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of FairPoint Communications, Inc. and subsidiaries at December 31, 2016, and the consolidated results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), FairPoint Communications, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control - Integrated Framework (2013) issued by Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria) and our report dated March 6, 2017 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP

Atlanta, Georgia  
March 6, 2017

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders of FairPoint Communications, Inc. and subsidiaries

We have audited the accompanying consolidated balance sheet of FairPoint Communications, Inc. and subsidiaries as of December 31, 2015, and the related consolidated statements of operations, comprehensive income (loss), stockholders' deficit and cash flows for each of the two years in the period ended December 31, 2015. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of FairPoint Communications, Inc. and subsidiaries at December 31, 2015, and the consolidated results of their operations and their cash flows for each of the two years in the period ended December 31, 2015, in conformity with U.S. generally accepted accounting principles.

/s/ Ernst & Young LLP

Charlotte, North Carolina  
March 2, 2016

**FAIRPOINT COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**Consolidated Balance Sheets**  
**December 31, 2016 and 2015**  
(in thousands, except share data)

	December 31, 2016	December 31, 2015
<b>Assets:</b>		
Cash	\$ 34,924	\$ 26,560
Accounts receivable, net	62,395	60,136
Prepaid expenses	24,498	24,410
Other current assets	4,898	5,030
<b>Total current assets</b>	<b>126,715</b>	<b>116,136</b>
Property, plant and equipment, net	1,024,352	1,118,781
Intangible assets, net	75,913	83,879
Restricted cash	653	651
Other assets	3,202	3,079
<b>Total assets</b>	<b>\$ 1,230,835</b>	<b>\$ 1,322,526</b>
<b>Liabilities and Stockholders' Deficit:</b>		
Current portion of long-term debt	\$ 6,400	\$ 6,400
Current portion of capital lease obligations	1,227	918
Accounts payable	27,598	28,157
Accrued interest payable	10,120	9,983
Accrued payroll and related expenses	26,187	24,753
Other accrued liabilities	47,918	50,018
<b>Total current liabilities</b>	<b>119,450</b>	<b>120,229</b>
Capital lease obligations	1,311	1,223
Accrued pension obligations	133,917	150,562
Accrued post-employment benefit obligations	87,629	94,042
Deferred income taxes, net	28,016	35,075
Other long-term liabilities	16,219	22,739
Long-term debt, net of current portion	898,370	900,145
<b>Total long-term liabilities</b>	<b>1,165,462</b>	<b>1,203,786</b>
<b>Total liabilities</b>	<b>1,284,912</b>	<b>1,324,015</b>
<b>Commitments and contingencies (See Note 18)</b>		
Stockholders' deficit:		
Common stock, \$0.01 par value. 37,500,000 shares authorized, 27,074,398 and 26,921,066 shares issued and outstanding at December 31, 2016 and 2015, respectively	271	269
Additional paid-in capital	527,613	521,842
Accumulated deficit	(603,497)	(707,592)
Accumulated other comprehensive income	21,536	183,992
<b>Total stockholders' deficit</b>	<b>(54,077)</b>	<b>(1,489)</b>
<b>Total liabilities and stockholders' deficit</b>	<b>\$ 1,230,835</b>	<b>\$ 1,322,526</b>

See accompanying notes to consolidated financial statements.

**FAIRPOINT COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**Consolidated Statements of Operations**  
**Years Ended December 31, 2016, 2015 and 2014**  
(in thousands, except per share data)

	Years Ended December 31,		
	2016	2015	2014
<b>Revenues</b>	<b>\$ 824,443</b>	<b>\$ 859,465</b>	<b>\$ 901,396</b>
Operating expenses:			
Cost of services and sales, excluding depreciation and amortization	389,316	430,308	440,979
Other post-employment benefit and pension (benefit)/expense	(213,760)	(170,338)	75,282
Selling, general and administrative expense, excluding depreciation and amortization	197,239	206,046	257,627
Depreciation and amortization	222,303	223,819	220,678
Reorganization related expense	—	38	104
<b>Total operating expenses</b>	<b>595,098</b>	<b>689,873</b>	<b>994,670</b>
<b>Income/(loss) from operations</b>	<b>229,345</b>	<b>169,592</b>	<b>(93,274)</b>
Other income/(expense):			
Interest expense	(82,697)	(80,718)	(80,371)
Other, net	296	485	7,548
<b>Total other expense</b>	<b>(82,401)</b>	<b>(80,233)</b>	<b>(72,823)</b>
<b>Income/(loss) before income taxes</b>	<b>146,944</b>	<b>89,359</b>	<b>(166,097)</b>
Income tax (expense)/benefit	(42,849)	1,057	29,778
<b>Net income/(loss)</b>	<b>\$ 104,095</b>	<b>\$ 90,416</b>	<b>\$ (136,319)</b>
<b>Weighted average shares outstanding:</b>			
Basic	26,854	26,652	26,449
Diluted	27,119	26,973	26,449
Income/(loss) per share, basic	\$ 3.88	\$ 3.39	\$ (5.15)
Income/(loss) per share, diluted	\$ 3.84	\$ 3.35	\$ (5.15)

See accompanying notes to consolidated financial statements.

**FAIRPOINT COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**Consolidated Statements of Comprehensive Income/(Loss)**  
**Years Ended December 31, 2016, 2015 and 2014**  
(in thousands)

	Years Ended December 31,		
	2016	2015	2014
<b>Net income/(loss)</b>	\$ 104,095	\$ 90,416	\$ (136,319)
Other comprehensive income/(loss), net of taxes:			
Interest rate swaps (net of \$0.7 million tax expense and \$0.3 million and \$0.7 million tax benefit, respectively)	1,106	(521)	(1,037)
Qualified pension and post-employment benefit plans (net of \$49.8 million tax benefit, \$10.0 million tax expense and \$8.6 million tax benefit, respectively)	(163,562)	503,136	(157,807)
<b>Total other comprehensive income/(loss)</b>	<b>(162,456)</b>	<b>502,615</b>	<b>(158,844)</b>
<b>Comprehensive income/(loss)</b>	<b>\$ (58,361)</b>	<b>\$ 593,031</b>	<b>\$ (295,163)</b>

See accompanying notes to consolidated financial statements.

**FAIRPOINT COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**Consolidated Statements of Stockholders' Deficit**  
**Years Ended December 31, 2016, 2015, and 2014**  
(in thousands)

	Common stock		Additional paid-in capital	Accumulated deficit	Accumulated other comprehensive income/(loss)	Total stockholders' deficit
	Shares	Amount				
<b>Balance at December 31, 2013</b>	<b>26,481</b>	<b>\$ 264</b>	<b>\$ 512,008</b>	<b>\$ (661,689)</b>	<b>\$ (159,779)</b>	<b>\$ (309,196)</b>
Net loss	—	—	—	(136,319)	—	(136,319)
Stock-based compensation issued, net	230	3	(202)	—	—	(199)
Stock-based compensation expense	—	—	4,274	—	—	4,274
Interest rate swaps other comprehensive loss	—	—	—	—	(1,037)	(1,037)
Employee benefits other comprehensive loss before reclassifications	—	—	—	—	(166,673)	(166,673)
Employee benefits reclassified from accumulated other comprehensive loss	—	—	—	—	8,866	8,866
<b>Balance at December 31, 2014</b>	<b>26,711</b>	<b>\$ 267</b>	<b>\$ 516,080</b>	<b>\$ (798,008)</b>	<b>\$ (318,623)</b>	<b>\$ (600,284)</b>
Net income	—	—	—	90,416	—	90,416
Stock-based compensation issued, net	210	2	(595)	—	—	(593)
Stock-based compensation expense	—	—	6,357	—	—	6,357
Interest rate swaps other comprehensive loss	—	—	—	—	(521)	(521)
Employee benefits other comprehensive income before reclassifications	—	—	—	—	687,643	687,643
Employee benefits reclassified from accumulated other comprehensive income	—	—	—	—	(184,507)	(184,507)
<b>Balance at December 31, 2015</b>	<b>26,921</b>	<b>\$ 269</b>	<b>\$ 521,842</b>	<b>\$ (707,592)</b>	<b>\$ 183,992</b>	<b>\$ (1,489)</b>
Net income	—	—	—	104,095	—	104,095
Stock-based compensation issued, net	153	2	(520)	—	—	(518)
Stock-based compensation expense	—	—	6,291	—	—	6,291
Interest rate swaps other comprehensive loss before reclassifications	—	—	—	—	(361)	(361)
Interest rate swaps reclassified from accumulated other comprehensive loss	—	—	—	—	1,467	1,467
Employee benefits other comprehensive income before reclassifications	—	—	—	—	8,029	8,029
Employee benefits reclassified from accumulated other comprehensive income	—	—	—	—	(171,591)	(171,591)
<b>Balance at December 31, 2016</b>	<b>27,074</b>	<b>\$ 271</b>	<b>\$ 527,613</b>	<b>\$ (603,497)</b>	<b>\$ 21,536</b>	<b>\$ (54,077)</b>

See accompanying notes to consolidated financial statements.

65

**FAIRPOINT COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2016, 2015 and 2014**  
(in thousands)

	Years Ended December 31,		
	2016	2015	2014
<b>Cash flows from operating activities:</b>			
Net income/(loss)	\$ 104,095	\$ 90,416	\$ (136,319)
Adjustments to reconcile net income/(loss) to net cash provided by operating activities:			
Deferred income taxes	42,609	(1,260)	(29,864)
Provision for uncollectible revenue	577	5,793	9,218
Depreciation and amortization	222,303	223,819	220,678
Other post-employment benefits	(228,442)	(184,569)	51,337
Qualified pension	(6,508)	(5,534)	(10,129)
Stock-based compensation	6,291	6,357	4,274
Other non-cash items	5,265	4,211	2,137
Changes in assets and liabilities arising from operations:			
Accounts receivable	(2,478)	5,615	8,485
Prepaid and other assets	198	1,327	(338)
Restricted cash	—	—	463
Accounts payable and accrued liabilities	(4,094)	(36,642)	5,068
Accrued interest payable	137	5	1
Other assets and liabilities, net	(5,701)	2,463	(3,948)
<b>Total adjustments</b>	<b>30,157</b>	<b>21,585</b>	<b>257,382</b>
<b>Net cash provided by operating activities</b>	<b>134,252</b>	<b>112,001</b>	<b>121,063</b>
<b>Cash flows from investing activities:</b>			
Net capital additions	(117,050)	(116,159)	(119,489)
Acquisition of business, net of cash acquired	(2,729)	—	—
Distributions from investments and proceeds from the sale of property and equipment	1,319	288	1,126
<b>Net cash used in investing activities</b>	<b>(118,460)</b>	<b>(115,871)</b>	<b>(118,363)</b>
<b>Cash flows from financing activities:</b>			
Repayments of long-term debt	(6,400)	(6,400)	(6,400)
Restricted cash	(2)	—	—
Proceeds from exercise of stock options	12	13	32
Repayment of capital lease obligations	(1,038)	(770)	(1,445)
<b>Net cash used in financing activities</b>	<b>(7,428)</b>	<b>(7,157)</b>	<b>(7,813)</b>
<b>Net change</b>	<b>8,364</b>	<b>(11,027)</b>	<b>(5,113)</b>
Cash, beginning of period	26,560	37,587	42,700
<b>Cash, end of period</b>	<b>\$ 34,924</b>	<b>\$ 26,560</b>	<b>\$ 37,587</b>
<b>Supplemental disclosure of cash flow information:</b>			
Interest paid, net of capitalized interest	\$ 77,153	\$ 75,625	\$ 75,520
Income tax paid, net of refunds	1,346	1,021	2,363
Capital additions included in accounts payable	8,586	10,902	13,120
Acquisition of property and equipment by capital lease	1,436	1,320	1,142

See accompanying notes to consolidated financial statements.

**FAIRPOINT COMMUNICATIONS, INC. AND SUBSIDIARIES**  
**Notes to Consolidated Financial Statements**

*Except as otherwise required by the context, references in notes to the consolidated financial statements to:*

- *"FairPoint Communications" refers to FairPoint Communications, Inc., excluding its subsidiaries.*
- *"FairPoint" or the "Company" refer to the combined business of FairPoint Communications, Inc. and all of its subsidiaries after giving effect to the merger on March 31, 2008 with Northern New England Spinco Inc., a subsidiary of Verizon Communications Inc. ("Verizon"), which transaction is referred to herein as the "Spinco Merger".*
- *"Northern New England operations" refers to the local exchange business acquired from Verizon and certain of its subsidiaries after giving effect to the Spinco Merger.*
- *"Telecom Group" refers to FairPoint, exclusive of the acquired Northern New England operations.*

## **(1) Organization and Principles of Consolidation**

### *Organization*

FairPoint is a leading provider of advanced communications services to business, wholesale and residential customers within its service territories. FairPoint offers its customers a suite of advanced data services such as Ethernet, high capacity data transport and other IP-based services over an extensive fiber network with more than 22,000 miles of fiber optic cable, including approximately 18,000 miles of fiber optic cable in Maine, New Hampshire and Vermont, in addition to Internet access, high-speed data ("HSD") and local and long distance voice services. As of December 31, 2016, FairPoint's service territory spanned 17 states where it is the incumbent communications provider, primarily serving rural communities and small urban markets. Many of its local exchange carriers ("LECs") have served their respective communities for more than 80 years. As of December 31, 2016, the Company operated with approximately 306,600 broadband subscribers, approximately 15,700 Ethernet circuits and approximately 366,100 residential voice lines.

### *Principles of Consolidation*

The consolidated financial statements include all majority-owned subsidiaries of the Company. Partially owned equity affiliates are accounted for under the cost method or equity method when the Company demonstrates significant influence, but does not have a controlling financial interest. Intercompany accounts and transactions have been eliminated upon consolidation.

## **(2) Significant Accounting Policies**

### *(a) Presentation and Use of Estimates*

The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP"), which require management to make estimates and assumptions that affect reported amounts and disclosures. Actual results could differ from those estimates. The consolidated financial statements reflect all adjustments that, in the opinion of management, are necessary for a fair presentation of results of operations and financial condition for the interim periods shown, including normal recurring accruals and other items.

The Company reclassified "Claims payable and estimated claims accrual" to "Other accrued liabilities" in the December 31, 2015 consolidated balance sheet to be consistent with current period presentation.

Examples of significant estimates include the allowance for doubtful accounts, revenue reserves, the depreciation of property, plant and equipment, valuation of intangible assets, qualified pension and other post-employment benefit plan assumptions, stock-based compensation and income taxes.

### *(b) Revenue Recognition*

Revenues are recognized as services are rendered and are primarily derived from the usage of the Company's networks and facilities or under revenue-sharing arrangements with other communications carriers. Revenues are primarily derived from: voice services, access (including pooling), certain Connect America Fund ("CAF") receipts, Internet and broadband services and other miscellaneous services. Local access charges are billed to local end users under tariffs approved by each state's Public Utilities Commission ("PUC") or by rates, terms and conditions determined by the Company. Access revenues are derived for the intrastate jurisdiction by billing access charges to interexchange carriers and to other LECs. These charges are billed based on toll or access tariffs approved by the local state's PUC. Access charges for the interstate jurisdiction are billed in accordance with tariffs filed



by the National Exchange Carrier Association ("NECA") or by the individual company and approved by the Federal Communications Commission (the "FCC"). On July 14, 2016, the FCC adopted a Declaratory Order that classifies switched access services provided by Incumbent LECs as non-dominant services. This change in classification will not impact rates or revenues as the rates continue to be subject to rules established for all access providers pursuant to the Intercarrier Compensation transition rules adopted in 2011.

Revenues are determined on a bill-and-keep basis or a pooling basis. If on a bill-and-keep basis, the Company bills the charges to the customer and keeps the revenue. If the Company participates in a pooling environment (interstate or intrastate), the revenue from the covered services is contributed to a revenue pool. The revenue is then distributed to individual companies based on their company-specific revenue requirement or similar distribution methods. This distribution is based on individual state PUCs' (intrastate) or the FCC's (interstate) approved settlement mechanisms, separation rules and rates of return. Distribution from these pools can change relative to changes made to expenses, plant investment or rate-of-return. Some companies participate in federal and certain state universal service programs that are pooling in nature but are regulated by rules separate from those described above. These rules vary by state. Revenues earned through the various pooling arrangements are initially recorded based on the Company's estimates.

On November 18, 2011, the FCC released its comprehensive landmark order to modify the nationwide system of universal support and the CAF/intercarrier compensation ("ICC") system (the "CAF/ICC Order"). Rule changes associated with the FCC's CAF/ICC Order impact the NECA interstate pooling, in that a portion of the Company's interstate Universal Service Fund ("USF") revenues, which are administered through the NECA pools and which prior to January 1, 2012 were based on costs, are now based on rules from the FCC's CAF/ICC Order, including CAF Phase II support where FairPoint accepted CAF Phase II support, continued CAF Phase I frozen support where FairPoint did not accept CAF Phase II support and CAF/ICC rules in states where FairPoint is eligible for such support under the ICC Transition Rules for price cap and rate-of-return carriers. FairPoint accepted CAF Phase II support in all states except Kansas and Colorado. The CAF Phase II revenue is being recognized on a straight-line basis, ratably over the six-year period in which the funding will be received. The accepted transition funding is being recognized monthly as received over the three-year transition period ending in July 2018. The Company is required to meet certain interim milestones over the six-year period of CAF Phase II and the Company performs a quarterly assessment of its progress.

Revenue from long distance switched retail and wholesale services can be recurring due to coverage under an unlimited calling plan or can be usage sensitive. In either case, they are billed in arrears and recognized when earned. Internet and data services revenues are substantially all recurring revenues and are billed one month in advance and deferred until earned.

As of December 31, 2016 and 2015, unearned revenue of \$18.2 million and \$19.9 million, respectively, was included in other accrued liabilities and unearned revenue of \$4.8 million and \$7.6 million, respectively, was included in other long-term liabilities on the consolidated balance sheets.

The majority of the Company's other miscellaneous services revenue is generated from ancillary special projects at the request of third parties, video services, directory services and late payment charges to end users and wholesale carriers. The Company generally requires customers to pay for ancillary special projects in advance. As of December 31, 2016 and 2015, customer deposits of \$3.3 million and \$2.1 million, respectively, were included in other accrued liabilities on the consolidated balance sheets. Once the ancillary special project is completed or substantially complete and all project costs have been accumulated for proper accounting recognition, the advance payment is recognized as revenue with any overpayments refunded to the customer, as appropriate. The Company recognizes revenue upon the provision of video services in certain markets by reselling DirecTV and providing cable and IP television video-over-digital subscriber line services. The Company also publishes telephone directories in some of its Telecom Group markets and recognizes revenues associated with these publications evenly over the time period covered by the directory, which is typically twelve months. The Company bills late payment fees to customers who have not paid their bills in a timely manner. In general, late payment fee revenue is recognized based on collection of these charges.

Non-recurring customer activation fees, along with the related costs up to, but not exceeding, the activation fees, are deferred and amortized over the customer relationship period.

Under the Maine Public Utilities Commission ("MPUC") rules (Chapter 201), which went into effect August 1, 2014, the MPUC may open an investigation regarding the failure to meet any of the established SQI benchmarks and has the authority to impose penalties. The MPUC opened an investigation into the Company's failure to meet some third quarter 2014 SQI benchmarks and subsequently opened an investigation into the fourth quarter of 2014 and then with respect to each of the quarterly periods in 2015. On March 29, 2016, the MPUC consolidated the investigations of the six quarters into one investigation. On September 14, 2016, a hearing examiner for the MPUC issued a report recommending that the MPUC find that FairPoint had failed to meet SQI benchmarks for the period under review and impose a \$500,000 penalty as allowed by statute, and provided until October 7, 2016 for comments or exceptions to be filed by interested parties. This recommendation did not constitute MPUC action. The Company promptly filed a motion to implement adjudicatory procedures prior to entry of any final order. After the Company's motion to implement adjudicatory procedures was briefed by the parties, the Hearing Examiner issued an order on November 30, 2016 granting the Company's motion in part and permanently withdrawing the Examiner's September 14, 2016 report. A case schedule



was established by the Hearing Examiner, and a hearing is currently scheduled to begin May 11, 2017. Subsequent legislation in Maine has superseded the SQI benchmarks applied in the examiner's report. Effective with the new legislation, the reporting of service quality will be required only in the areas of the state where Provider of Last Resort ("POLR") is still required and will be filed and treated as confidential. The number of SQI reporting metrics has been reduced and the benchmarks are less stringent than under previous Commission rules.

The Company also adopted a separate performance assurance plan ("PAP") for certain services provided on a wholesale basis to competitive local exchange carriers ("CLECs") in each of the states of Maine, New Hampshire and Vermont. Pursuant to the PAPs, FairPoint was required to provide service credits in the event the Company was unable to meet the provisions of the respective PAP. Effective June 1, 2015, the PAP was retired and the Company began measuring and reporting certain wholesale local service performance results pursuant to the terms of a simplified measurement plan. The new plan, called the Wholesale Performance Plan ("WPP"), was developed collaboratively with CLECs over several years and was approved by the Maine, New Hampshire and Vermont regulatory commissions. Under the WPP, the Company is subject to significantly fewer performance criteria and its annual service credit exposure was reduced.

In evaluating the presentation of taxes and surcharges, such as USF charges, sales, use, value added and some excise taxes, the Company determines whether it is the primary obligor or principal taxpayer. In jurisdictions where the Company deems that it is the principal taxpayer, the Company records these taxes and surcharges on a gross basis and include them in its revenues and costs of services and sales. In jurisdictions where the Company determines that it is a pass through agent for the government authority, it records the taxes on a net basis through the consolidated balance sheets.

Customer arrangements that include both equipment and services are evaluated to determine whether the elements are separable. If the elements are deemed separable and separate earnings processes exist, the revenue associated with each element is allocated to each element based on the relative estimated selling price of the separate elements. The Company has estimated the selling prices of each element by reference to vendor-specific objective evidence of selling prices when the elements are sold separately. The revenue associated with each element is then recognized as earned.

Management makes estimated adjustments, as necessary, to revenue and accounts receivable for billing errors, including certain disputed amounts.

#### *(c) Cash and Cash Equivalents*

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

#### *(d) Accounts Receivable*

Accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is recorded as a contra-asset of accounts receivable and represents the Company's best estimate of probable credit losses in the Company's existing accounts receivable. The Company establishes an allowance for doubtful accounts based upon factors surrounding the credit risk of specific customers, historical trends, and other information. Accounts receivable balances are reviewed on an aged basis and account balances are written off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

The following is activity in the Company's allowance for doubtful accounts receivable for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	Years Ended December 31,					
	2016		2015		2014	
Balance, beginning of period	\$	8,333	\$	9,894	\$	13,142
Provision charged to expense		577		5,793		9,218
Provision charged to other accounts <sup>(a)</sup>		—		(18)		(43)
Amounts written off, net of recoveries		(5,273)		(7,336)		(12,423)
<b>Balance, end of period</b>	<b>\$</b>	<b>3,637</b>	<b>\$</b>	<b>8,333</b>	<b>\$</b>	<b>9,894</b>

(a) Provision charged to other accounts includes accruals charged to accounts payable for anticipated uncollectible charges on purchase of accounts receivable from others which were billed by the Company.



***(e) Credit Risk***

The financial instruments which potentially subject the Company to concentrations of credit risk consist principally of cash and gross accounts receivable existing at December 31, 2016. The Company places its cash with high-quality financial institutions. Concentrations of credit risk with respect to accounts receivable are principally related to trade receivables from other interexchange carriers and are otherwise limited to the Company's large number of customers in several states.

The Company sponsors qualified pension plans for certain employees. Plan assets associated with these qualified pension plans are held by third party trustees and investments are comprised principally of debt and equity securities. The fair value of these plan assets is dependent on the financial condition of those entities issuing the debt and equity securities. A significant decline in the fair value of plan assets could result in additional Company contributions to the qualified pension plans in order to meet funding requirements under the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). For additional information regarding the plan assets of the Company's qualified pension plans, including the December 31, 2016 balance at risk, see note (11) "Employee Benefit Plans" herein.

***(f) Property, Plant and Equipment***

Given that a majority of the Company's property, plant and equipment is plant used in the Company's wireline and fiber-based Ethernet networks, depreciation is principally based on the composite group remaining life method and straight-line composite rates. This methodology provides for the recognition of the cost of the remaining net investment in telephone plant, property and equipment less anticipated positive net salvage value, over the remaining asset lives. When depreciable telephone plant is replaced or retired, the carrying amount of such plant is deducted from the respective accounts and charged to accumulated depreciation. No gain or loss is generally recognized on disposition of assets. Use of this methodology requires the periodic revision of depreciation rates. In the evaluation of asset lives, multiple factors are considered, including, but not limited to, the ongoing network deployment, technology upgrades and enhancements, planned retirements and the adequacy of reserves. The Company utilizes straight-line depreciation for its non-telephone property, plant and equipment.

Periodically, the Company reviews the estimated remaining useful lives of its group asset categories to address continuing changes in technology, competition and the Company's overall reduction in capital spending and increased focus on more efficient utilization of its existing assets.

Network software purchased or developed in connection with related plant assets is capitalized. The Company also capitalizes interest associated with the acquisition or construction of network related assets. Capitalized interest is reported as part of the cost of the network related assets and as a reduction in interest expense. See "(i) Computer Software and Interest Costs" herein for additional information.

***(g) Long-Lived Assets***

Property, plant and equipment and intangible assets subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. An impairment charge is recognized for the amount, if any, by which the carrying value of the asset exceeds its fair value.

As of December 31, 2016, the Company performed its routine review of impairment triggering events and concluded that it does not believe a triggering event has occurred with respect to property, plant and equipment and intangible assets subject to amortization.

***(h) Asset Retirement Obligations***

The Company records the estimated fair value of an asset retirement obligation when incurred. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and depreciated over the asset's estimated useful life. The Company has asset retirement obligations related to battery, fuel tank and chemically-treated pole disposal as well as soil remediation at leased facilities. Considerable management judgment is required in estimating these obligations. Important assumptions include estimates of retirement costs, the timing of the future retirement activities and the likelihood or retirement provisions being enforced. Changes in these assumptions based on future information could result in adjustments to estimated liabilities.

***(i) Computer Software and Interest Costs***

The Company capitalizes certain costs incurred in connection with developing or obtaining internal use software which has a useful life in excess of one year. Capitalized costs include direct development costs associated with internal use software, including direct labor costs and external costs of materials and services.

Subsequent additions, modifications or upgrades to internal-use software are capitalized only to the extent that they allow the software to perform a task it previously did not perform. Software maintenance and training costs are expensed in the period in which they are incurred.

In addition, the Company capitalizes the interest cost associated with the period of time over which the Company's internal use software is developed or obtained.

During the years ended December 31, 2016, 2015 and 2014, the Company recorded the following with regards to software costs (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Capitalized software costs	\$ 10,282	\$ 22,768	\$ 17,984
Capitalized interest costs	\$ 148	\$ 99	\$ 70
Amortization expense on capitalized software	\$ 16,610	\$ 14,669	\$ 11,415

A summary of capitalized software is shown below (in thousands):

	December 31, 2016	December 31, 2015
Gross carrying amount	\$ 167,986	\$ 176,778
Less: accumulated amortization	(128,758)	(131,031)
<b>Net capitalized software</b>	<b>\$ 39,228</b>	<b>\$ 45,747</b>

Estimated future amortization on capitalized software for each of the five years subsequent to December 31, 2016 are as follows (in thousands):

Year ending December 31,		
2017	\$	14,856
2018	\$	11,670
2019	\$	7,731
2020	\$	4,528
2021	\$	443

#### (j) Impairment of Other Intangible Assets

**Indefinite-lived Intangible Asset.** Non-amortizable intangible assets are assessed for impairment at least annually. The Company performs its annual impairment test as of the first day of the fourth fiscal quarter of each year and assesses the fair value of the trade name based on the relief from royalty method. If the carrying amount of the trade name exceeds its estimated fair value, the asset is considered impaired.

For its non-amortizable intangible asset impairment assessments of the FairPoint trade name, the Company makes certain assumptions including an estimated royalty rate, a long-term growth rate, an effective tax rate and a discount rate, and applies these assumptions to projected future cash flows, exclusive of cash flows associated with wholesale revenues and other revenues not generated through brand recognition. As of October 1, 2016, the estimated fair value exceeded the carrying value in the Company's quantitative analysis; therefore, an impairment was not necessary. However, future changes in one or more of the assumptions discussed above may result in the recognition of an impairment loss.

**Amortizable Intangible Assets.** Amortizable intangible assets must be reviewed for impairment as part of long-lived assets whenever indicators of impairment exist. See "(g) Long-Lived Assets" herein for additional information.

#### (k) Accounting for Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or

settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management determines its estimates of future taxable income based upon the scheduled reversal of deferred tax liabilities and tax planning strategies. The Company establishes valuation allowances for deferred tax assets when it is estimated to be more likely than not that the tax assets will not be realized.

FairPoint Communications files a consolidated income tax return with its subsidiaries. All intercompany transactions and accounts have been eliminated in consolidation.

**(l) Stock-Based Compensation**

The Company accounts for employee awards which are expected to vest. Stock-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as expense on a straight-line basis over the requisite service period, which generally begins on the date the award is granted through the date the award vests.

**(m) Employee Benefit Plans**

The Company recognizes the overfunded or underfunded status of its qualified defined benefit plans and post-employment benefit plans as either an asset or liability, respectively, on the consolidated balance sheets. Actuarial gains and losses that arise during the year are recognized as a component of comprehensive income/(loss), net of applicable income taxes, and included in accumulated other comprehensive income. These gains and losses are amortized over future years as a component of the net periodic benefit cost.

**(n) Operating Segments**

Management views its business of providing data, video and voice communications services to residential, wholesale and business customers as one operating segment. The Company's services consist of retail and wholesale communications and data services, including voice and HSD in 17 states. The Company's chief operating decision maker assesses operating performance and allocates resources based on the consolidated results.

**(o) Other Liabilities**

**Accrued Bonuses.** As of December 31, 2016 and 2015, accrued bonuses of \$12.7 million and \$12.6 million, respectively, were included in accrued payroll and related liabilities on the consolidated balance sheets.

**(p) Advertising Costs**

Advertising costs are expensed as they are incurred. During the years ended December 31, 2016, 2015 and 2014, advertising costs were \$6.5 million, \$6.6 million and \$9.8 million, respectively.

**(q) Interest Rate Swap Agreements**

In the third quarter of 2013, the Company entered into interest rate swap agreements. For further information regarding these interest rate swap agreements, *see* note (9) "Interest Rate Swap Agreements." The interest rate swap agreements, at their inception, qualified for and were designated as cash flow hedging instruments. The Company records its interest rate swaps on the consolidated balance sheets at fair value. The effective portion of changes in fair value are recorded in accumulated other comprehensive income and are subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. Any ineffective portion is recognized in earnings. Both at inception and on a quarterly basis, the Company performs an effectiveness test.

**(3) Proposed Merger with Consolidated Communications Holdings, Inc.**

On December 3, 2016, FairPoint Communications entered into an Agreement and Plan of Merger (the "Merger Agreement") with Consolidated Communications Holdings, Inc. ("Consolidated"), a Delaware Corporation, and Falcon Merger Sub, Inc., a newly formed Delaware corporation and wholly-owned subsidiary of Consolidated ("Merger Sub"), which provides for, among other things, a business combination whereby Merger Sub will merge with and into FairPoint Communications, with FairPoint Communications as the surviving entity (the "Merger"). As a result of the Merger, the separate corporate existence of Merger Sub will cease, and FairPoint Communications will survive as a wholly owned subsidiary of Consolidated. Consolidated is a leading business and broadband communications provider throughout its 11-state service area.

If the Merger is completed, under the terms of the Merger Agreement, stockholders of FairPoint Communications will receive 0.7300 shares of common stock of Consolidated for each share of FairPoint Communications common stock that they own immediately before this transaction. If the Merger is not completed, FairPoint Communications may be required to pay a termination fee of \$18.9 million under certain circumstances set forth in the Merger Agreement. The Merger is expected to close around the middle of 2017 and is subject to standard closing conditions, including federal and state regulatory approvals and the approval of both Consolidated's and FairPoint Communications' stockholders.

For the year ended December 31, 2016, the Company recognized \$4.5 million of merger related expenses, primarily for legal and financial advisory costs included in selling, general and administrative expense, excluding depreciation and amortization, on the consolidated statement of operations.

The award agreements granted under the FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan (the "Long Term Incentive Plan") provide that upon the occurrence of a change in control, unvested benefits will be accelerated and vest in full.

#### (4) Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers, which is designed to clarify the principles used to recognize revenue for entities. The core principle of ASU 2014-09 is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In addition, ASU 2014-09 requires enhanced disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. While ASU 2014-09 is primarily associated with guidance for revenue from contracts with customers, it also includes new accounting principles related to deferral and amortization of contract acquisition and fulfillment costs. In 2016, the Company performed an assessment of its revenues, acquisition and fulfillment costs from contracts to understand any potential differences to its current accounting policies and business processes. The Company expects to have an impact concerning the deferral of acquisition costs as its current policy is to expense these costs as incurred. At this time, the Company continues to assess and determine data and system requirements necessary to quantify the impacts of this standard as well as to develop and provide the enhanced disclosures required by the new guidance.

In July 2015, the FASB approved a one-year deferral of the effective date of ASU 2014-09. Subsequently, the FASB has issued several additional ASUs to clarify the implementation guidance on principal versus agent considerations, identifying performance obligations, assessing collectability, presentation of sales taxes and other similar taxes collected from customers, non-cash considerations, contract modifications and completed contracts at transition. The new pronouncements will be effective for annual and interim periods beginning on or after December 15, 2017. The Company intends to adopt the new standard effective January 1, 2018.

The standard allows for two methods of adoption: (1) "full retrospective" adoption, meaning the standard is applied to all periods presented, or (2) "modified retrospective" adoption, meaning the cumulative effect of applying ASU 2014-09 is recognized as an adjustment to the fiscal year 2018 opening retained earnings balance. Currently, the Company is evaluating the available adoption methods and plans to select an adoption method in the second half of 2017.

In August 2014, the FASB issued ASU 2014-15, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern, which requires management to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures in certain circumstances. ASU 2014-15 is effective for annual periods beginning after December 15, 2016. The Company adopted this pronouncement for its year ended December 31, 2016 and it did not have a material impact on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases, whereby, lessees will be required to recognize for all leases at the commencement date a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. A modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements must be applied. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Companies may not apply a full retrospective transition approach. ASU 2016-02 is effective for annual and interim periods beginning after December 15, 2018. Early application is permitted. The Company is evaluating the potential impact of this pronouncement.

In March 2016, the FASB issued ASU 2016-09, Improvements to Employee Share-Based Payment Accounting, which simplifies several aspects of the accounting for share-based payment award transactions, including, but not limited to: (a) income



tax consequences; (b) classification of awards as either equity or liabilities; and (c) classification on the statement of cash flows. ASU 2016-09 is effective for annual and interim periods beginning after December 15, 2016. The Company does not believe the adoption of this pronouncement will have a material impact on its consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows: Restricted Cash*, which requires a statement of cash flows to explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU 2016-18 is effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years, and early adoption is permitted, including in an interim period. If early adopted in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. ASU 2016-18 is to be applied through a retrospective transition method to each period presented. The Company does not believe that the adoption of this pronouncement will have a significant impact on its consolidated statements of cash flows.

#### (5) Dividends

The Company currently does not pay a dividend on its common stock and has no plans to pay dividends.

#### (6) Other Intangible Assets

##### *Indefinite-lived Intangible Assets*

At December 31, 2016 and 2015, the Company's trade name is recorded at \$39.2 million. In addition, the Company completed an immaterial business acquisition during 2016 and recorded goodwill of \$2.5 million. On October 1, 2016 and October 1, 2015, the Company performed its annual non-amortizable intangible asset quantitative analysis and concluded that there was no impairment at that time. As of December 31, 2016, the Company performed its routine review of impairment indicators and concluded that it did not believe a triggering event had occurred.

##### *Other Amortizable Intangible Assets*

The Company's amortizable intangible assets are as follows (in thousands):

	December 31, 2016	December 31, 2015
Customer lists ( <i>weighted average 9.0 years</i> ):		
Gross carrying amount	\$ 99,410	\$ 99,000
Less: accumulated amortization	(65,312)	(54,290)
Net customer lists	\$ 34,098	\$ 44,710
Other net amortizable intangible assets	\$ 184	\$ —
<b>Total amortizable intangible assets</b>	<b>\$ 34,282</b>	<b>\$ 44,710</b>

Amortization expense of the Company's amortizable intangible assets was \$11.0 million, \$11.0 million and \$11.0 million for the years ended December 31, 2016, 2015 and 2014, respectively, and is expected to be approximately \$11.1 million in 2017, 2018, 2019, respectively, \$0.8 million in 2020 and \$0.1 million in 2021.

**(7) Property, Plant and Equipment**

A summary of property, plant and equipment is shown below (in thousands):

	Estimated Life (in years)	December 31, 2016	December 31, 2015
Land	—	\$ 35,217	\$ 35,632
Buildings	40	215,897	211,115
Central office equipment	7 – 10	662,042	635,208
Outside communications plant	15 – 35	1,191,142	1,161,042
Furniture, vehicles and other work equipment	5 – 15	257,337	258,749
Plant under construction	—	99,568	81,096
Other	—	16,029	17,144
<b>Total property, plant and equipment</b>		<b>2,477,232</b>	<b>2,399,986</b>
Less: Accumulated depreciation		(1,452,880)	(1,281,205)
<b>Net property, plant and equipment</b>		<b>\$ 1,024,352</b>	<b>\$ 1,118,781</b>

Depreciation expense, excluding amortization of intangible assets, for the years ended December 31, 2016, 2015 and 2014 was \$211.3 million, \$212.8 million and \$209.7 million, respectively. Depreciation expense includes amortization of assets recorded under capital leases.

The Company recorded \$0.6 million of asset retirement obligations during the year ended December 31, 2015. Net accretion expense, revisions in cash flow estimates and liability settlements were insignificant during the year. The Company's asset retirement obligations are included as a component of other accrued liabilities or other long-term liabilities in the consolidated balance sheets based on the expected timing of the obligation. As of December 31, 2016, the Company's asset retirement liability of \$4.8 million consisted of \$0.3 million in other accrued liabilities and \$4.5 million in other long-term liabilities. As of December 31, 2015, the Company's asset retirement liability of \$4.9 million consisted of \$0.8 million in other accrued liabilities and \$4.1 million in other long-term liabilities.

**(8) Long-term Debt**

Long-term debt for the Company at December 31, 2016 and 2015 is shown below (in thousands):

	December 31, 2016	December 31, 2015
Term Loan, due 2019 <i>(weighted average rate of 7.50%)</i>	\$ 616,000	\$ 622,400
Discount on Term Loan <sup>(a)</sup>	(7,834)	(11,138)
Debt issuance costs	(3,396)	(4,717)
Notes, 8.75%, due 2019	300,000	300,000
<b>Total long-term debt</b>	<b>904,770</b>	<b>906,545</b>
Less: current portion	(6,400)	(6,400)
<b>Total long-term debt, net of current portion</b>	<b>\$ 898,370</b>	<b>\$ 900,145</b>

(a) The \$7.8 million and \$11.1 million discount on the Term Loan (as defined below) as of December 31, 2016 and 2015, respectively, is being amortized using the effective interest method over the life of the Term Loan.

As of December 31, 2016, the Company had \$61.1 million, net of \$13.9 million outstanding letters of credit, available for additional borrowing under the Revolving Facility (as defined below).

The approximate aggregate maturities of long-term debt, excluding the debt discount on the Term Loan, for each of the three years subsequent to December 31, 2016 are as follows (in thousands):

Year ending December 31,	Balance Due
2017	\$ 6,400

2018		6,400
2019		903,200
<b>Total long-term debt, including current portion</b>	<b>\$</b>	<b>916,000</b>

**Refinancing.** On February 14, 2013 (the "Refinancing Closing Date"), FairPoint Communications refinanced its old credit agreement (the "Refinancing"). In connection with the Refinancing, FairPoint Communications (i) issued \$300.0 million aggregate principal amount of its 8.75% senior secured notes due 2019 (the "Notes") in a private offering exempt from registration under the Securities Act pursuant to an indenture (the "Indenture") that FairPoint Communications entered into on the Refinancing Closing Date with certain of its subsidiaries that guarantee the indebtedness under the Credit Agreement (as defined herein) (the "Subsidiary Guarantors") and U.S. Bank National Association, as trustee and collateral agent, and (ii) entered into a credit agreement (the "Credit Agreement"), dated as of the Refinancing Closing Date, with the lenders party thereto from time to time and Morgan Stanley Senior Funding, Inc., as administrative agent and letter of credit issuer. The Credit Agreement provides for a \$75.0 million revolving credit facility (the "Revolving Facility"), which has a sub-facility providing for the issuance of up to \$40.0 million in letters of credit, and a \$640.0 million term loan facility (the "Term Loan" and, together with the Revolving Facility, the "Credit Agreement Loans"). On the Refinancing Closing Date, FairPoint Communications used the proceeds of the Notes offering, together with \$640.0 million of borrowings under the Term Loan and cash on hand to (i) repay principal of \$946.5 million outstanding on the old term loan, plus approximately \$7.7 million of accrued interest and (ii) pay approximately \$32.6 million of fees, expenses and other costs related to the Refinancing.

**The Credit Agreement.** The principal amount of the Term Loan and commitments under the Revolving Facility may be increased by an aggregate amount of up to \$200.0 million, subject to certain terms and conditions specified in the Credit Agreement. The Term Loan will mature on February 14, 2019 and the Revolving Facility will mature on February 14, 2018, subject in each case to extensions pursuant to the terms of the Credit Agreement.

**Interest Rates and Fees.** Interest on borrowings under the Credit Agreement Loans accrue at an annual rate equal to either a British Bankers Association London Inter-Bank Offered Rate ("LIBOR") or the base rate, in each case plus an applicable margin. LIBOR is a per annum rate for dollar deposits with an interest period of one, two, three or six months (at FairPoint Communication's election), subject to a minimum LIBOR floor of 1.25% for the Term Loan. The base rate is the per annum rate equal to the greatest of (x) the federal funds effective rate plus 0.50%, (y) the rate of interest publicly quoted from time to time by The Wall Street Journal as the United States "Prime Rate" and (z) LIBOR with an interest period of one month plus 1.00%. The applicable margin for the Term Loan is (a) 6.25% per annum with respect to term loans bearing interest based on LIBOR or (b) 5.25% per annum with respect to term loans bearing interest based on the base rate. The applicable interest rate for the Revolving Facility is, initially, (a) 5.50% with respect to revolving loans bearing interest based on LIBOR or (b) 4.50% per annum with respect to revolving loans bearing interest based on the base rate, in each case subject to adjustment based on FairPoint Communication's consolidated total leverage ratio, as defined in the Credit Agreement. FairPoint Communications is required to pay a quarterly letter of credit fee on the average daily amount available to be drawn under letters of credit issued under the Revolving Facility equal to the applicable interest rate for revolving loans bearing interest based on LIBOR, plus a fronting fee of 0.125% per annum on the average daily amount available to be drawn under such letters of credit. In addition, FairPoint Communications is required to pay a quarterly commitment fee on the average daily unused portion of the New Revolving Facility, which is 0.50% initially, subject to reduction to 0.375% based on FairPoint Communication's consolidated total leverage ratio.

**Security/Guarantors.** All obligations under the Credit Agreement, together with certain designated hedging obligations and cash management obligations, are unconditionally guaranteed on a senior secured basis by certain subsidiaries of FairPoint Communications (the "Subsidiary Guarantors") and secured by a first-priority lien on substantially all personal property of FairPoint Communications and the Subsidiary Guarantors, subject to certain exclusions set forth in the related security documents, pari passu with the lien securing the obligations under the Notes.

**Mandatory Repayments.** FairPoint Communications is required to make quarterly repayments of the Term Loan in a principal amount of \$1.6 million during the term of the Credit Agreement. In addition, mandatory repayments are required under the Credit Agreement with (i) a percentage, initially equal to 50% and subject to reduction to 25% based on FairPoint Communication's consolidated total leverage ratio, of FairPoint Communication's excess cash flow, as defined in the Credit Agreement, (ii) the net cash proceeds of certain asset dispositions, insurance proceeds and condemnation awards and (iii) issuances of debt not permitted to be incurred under the Credit Agreement. No premium is required in connection with repayments.

**Covenants.** The Credit Agreement contains customary representations and warranties and affirmative and negative covenants for a transaction of this type, including two financial maintenance covenants: (i) a consolidated interest coverage ratio and (ii) a consolidated total leverage ratio. The Credit Agreement also contains a covenant limiting the amount of capital expenditures that FairPoint Communications and its subsidiaries may make in any fiscal year. As of December 31, 2016, FairPoint Communications was in compliance with all covenants under the Credit Agreement.

**Events of Default.** The Credit Agreement also contains customary events of default.

**The Notes.** On the Refinancing Closing Date, FairPoint Communications issued \$300.0 million of the Notes pursuant to the Indenture in a private offering exempt from registration under the Securities Act.



The terms of the Notes are governed by the Indenture. The Notes are senior secured obligations of FairPoint Communications and are guaranteed by the Subsidiary Guarantors. The Notes and the guarantees thereof are secured by a first-priority lien on substantially all personal property of FairPoint Communications and the Subsidiary Guarantors, subject to certain exclusions set forth in the related security documents, pari passu with the lien securing the obligations under the Credit Agreement. The Notes will mature on August 15, 2019 and accrue interest at a rate of 8.75% per annum, which is payable semi-annually in arrears on February 15 and August 15 of each year.

Notes redeemed after February 15, 2016 and prior to February 15, 2017 may be redeemed at 104.375% of the aggregate principal amount; Notes redeemed on or after February 15, 2017 and prior to February 15, 2018 may be redeemed at 102.188% of the aggregate principal amount; and Notes redeemed on or after February 15, 2018 may be redeemed at their par value.

The holders of the Notes have the ability to require FairPoint Communications to repurchase all or any part of the Notes if FairPoint Communications experiences certain kinds of changes in control or engages in certain asset sales, in each case at the repurchase prices and subject to the terms and conditions set forth in the Indenture.

The Indenture contains certain covenants which are customary with respect to non-investment grade debt securities, including limitations on FairPoint Communication's ability to incur additional indebtedness, pay dividends on or make other distributions or repurchase FairPoint Communication's capital stock, make certain investments, enter into certain types of transactions with affiliates, create liens and sell certain assets or merge with or into other companies. These covenants are subject to a number of important limitations and exceptions. As of December 31, 2016, FairPoint Communications was in compliance with all covenants under the Indenture.

The Indenture also provides for customary events of default, including cross defaults to other specified debt of FairPoint Communications and certain of its subsidiaries.

#### (9) Interest Rate Swap Agreements

The Company uses interest rate swap agreements to protect the Company against future adverse fluctuations in interest rates by reducing its exposure to variability in cash flows relating to interest payments on a portion of its outstanding debt. The Company's interest rate swaps, which are designated as cash flow hedges, involve the receipt of variable amounts from counterparties in exchange for the Company making fixed-rate payments over the effective term of the agreements without exchange of the underlying notional amount. The Company does not hold or issue any derivative financial instruments for speculative trading purposes.

In the third quarter of 2013, the Company entered into interest rate swap agreements with a combined notional amount of \$170.0 million with three counterparties that are effective for a two year period. Such swaps became effective on September 30, 2015 and mature on September 30, 2017. Each respective swap agreement requires the Company to pay a fixed rate of 2.665% and provides that the Company will receive a variable rate based on the three month LIBOR rate subject to a minimum LIBOR floor of 1.25%. Amounts payable by or due to the Company are net settled with the respective counterparties on the last business day of each fiscal quarter.

The effect of the Company's interest rate swap agreements on the consolidated balance sheets at December 31, 2016 and 2015 is shown below (in thousands):

	As of December 31, 2016	
	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments:		
Interest rate swaps, Current	Other accrued liabilities	\$ 1,762
	As of December 31, 2015	
	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments:		
Interest rate swaps, Current	Other accrued liabilities	\$ 2,375
Interest rate swaps, Long-term	Other long-term liabilities	\$ 1,232

The gross effect of the Company's interest rate swap agreements on the consolidated statements of comprehensive income/(loss) for the years ended December 31, 2016, 2015 and 2014 is shown below (in thousands):

	Amount Recognized in Interest Expense (Pre-Tax)			Amount of Loss/(Gain) Recognized in Other Comprehensive Income on Derivative (Effective Portion) (Pre-Tax)		
	Year Ended December 31, 2016	Year Ended December 31, 2015	Year Ended December 31, 2014	Year Ended December 31, 2016	Year Ended December 31, 2015	Year Ended December 31, 2014
Interest rate swaps	\$ 2,446	\$ —	\$ —	\$ (1,845)	\$ 865	\$ 1,737

Amounts reported in accumulated other comprehensive income related to interest rate swaps will be reclassified to interest expense as interest payments are made on the Term Loan. The Company estimates that approximately \$1.8 million will be reclassified as an increase to interest expense in the next 12 months.

Each interest rate swap agreement contains a provision whereby if the Company defaults on any of its indebtedness, the Company may also be declared in default under the interest rate swap agreements.

#### (10) Fair Value

In determining fair value, the Company uses a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

- Level 1 - Valuations based on quoted prices in active markets for identical assets or liabilities that the Company has the ability to access.
- Level 2 - Valuations based on quoted prices for similar instruments in active markets or quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.
- Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The Company's non-financial assets and liabilities, including its long-lived assets and indefinite-lived intangible assets, are measured and subsequently adjusted, if necessary, to fair value on a non-recurring basis. The Company periodically performs routine reviews of triggering events and/or an impairment test, as applicable. Based on these procedures, the Company did not require an adjustment to fair value to be recorded to these assets in 2016 or 2015.

The Company's financial instruments, other than interest rate swap agreements and long-term debt, consist primarily of cash, restricted cash, accounts receivable and accounts payable. The carrying amounts of these financial instruments are estimated to approximate fair value due to the relatively short period of time to maturity for these instruments. As of December 31, 2016, interest rate swap agreements are carried at their fair value and measured on a recurring basis as follows (in thousands):

	Fair Value Measurements Using		
	Level 1	Level 2	Level 3
Interest rate swaps, Current <sup>(a)</sup>	\$ —	\$ 1,762	\$ —

As of December 31, 2015, interest rate swap agreements are carried at their fair value and measured on a recurring basis as follows (in thousands):

	Fair Value Measurements Using		
	Level 1	Level 2	Level 3
Interest rate swaps, Current <sup>(a)</sup>	\$ —	\$ 2,375	\$ —
Interest rate swaps, Long-term <sup>(a)</sup>	\$ —	\$ 1,232	\$ —

- (a) The fair value is determined using valuation models which rely on the expected LIBOR based yield curve and estimates of counterparty and the Company's non-performance risk. Because each of these inputs are directly observable or can be corroborated by observable market data, the Company has categorized these interest rate swaps as Level 2 within the fair value hierarchy.

The estimated fair values of the Company's long-term debt as of December 31, 2016 and 2015 are as follows (in thousands):

	December 31, 2016		December 31, 2015	
	Carrying Amount	Fair Value <sup>(a)</sup>	Carrying Amount	Fair Value <sup>(a)</sup>
Term Loan, due 2019 <sup>(b)</sup>	\$ 608,166	\$ 620,620	\$ 611,262	\$ 616,954
Notes, 8.75%, due 2019	300,000	312,375	300,000	295,500
Total	\$ 908,166	\$ 932,995	\$ 911,262	\$ 912,454

- (a) The Company estimated fair value based on market prices of the Company's debt securities at the balance sheet dates, which falls within Level 2 of the fair value hierarchy.
- (b) The carrying amount of the Term Loan is net of the unamortized discount of \$7.8 million and \$11.1 million as of December 31, 2016 and 2015, respectively.

For a discussion of the fair value measurement of the Company's pension plan assets, *see* note (11) "Employee Benefit Plans—Plan Assets, Obligations and Funded Status—Qualified Pension Plan Assets".

### (11) Employee Benefit Plans

The Company sponsors noncontributory qualified defined benefit pension plans ("qualified pension plans") and post-employment benefit plans which provide certain cash payments and medical, dental and life insurance benefits to eligible retired employees and their beneficiaries and covered dependents. The qualified pension plans and certain post-employment benefit plans were created as part of the acquisition of the Northern New England operations from Verizon and mirrored the prior Verizon plans.

The qualified pension plan available to represented employees was closed to new participants and benefits under the prior formula were frozen as of October 14, 2014. For existing participants, future benefit accruals for service on and after February 22, 2015 are at 50% of prior rates and are capped at 30 years of total credited service. The qualified pension plan available to non-represented employees remains frozen.

The post-employment benefit plan provides medical, dental and life insurance benefits to eligible non-represented employees and former represented employees and, in some instances, to their spouses and families. Effective August 28, 2014, active represented employees are no longer eligible for this post-employment benefit plan. Upon ratification of the collective bargaining agreements on February 22, 2015 and for 30 months thereafter, active represented employees who retire and meet the eligibility requirements and their spouses are eligible to receive certain monthly reimbursements of medical insurance premiums until the retired employee reaches age 65 or dies, at which time the benefit will cease for the spouse as well.

The Company makes contributions to the qualified pension plans to meet minimum funding requirements under the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), and has the ability to elect to make additional discretionary contributions. The other post-employment benefit plans are unfunded and the Company funds the benefits that are paid. Annually, and as necessary, the Company remeasures the net liabilities of its qualified pension and other post-employment benefit plans.

*Plan Assets, Obligations and Funded Status*

A summary of plan assets, projected benefit obligation and funded status of the plans are as follows for the years ended December 31, 2016 and 2015 (in thousands):

	<b>Qualified Pension Plans</b>	
	<b>Year Ended December 31, 2016</b>	<b>Year Ended December 31, 2015</b>
Fair value of plan assets:		
Beginning fair value of plan assets	\$ 197,062	\$ 195,410
Actual return on plan assets	15,745	(3,677)
Plan settlements	(2,510)	(4,472)
Employer contributions	16,501	14,980
Benefits paid	(3,898)	(5,179)
<b>Ending fair value of plan assets</b>	<b>222,900</b>	<b>197,062</b>
Projected benefit obligation:		
Beginning projected benefit obligation	\$ 347,624	\$ 408,216
Service cost	6,880	8,391
Interest cost	15,079	14,879
Plan amendment <sup>(a)</sup>	—	(40,049)
Plan settlements	(2,510)	(4,472)
Plan curtailment	—	(2,426)
Benefits paid	(3,898)	(5,179)
Actuarial loss	(6,358)	(31,736)
<b>Ending projected benefit obligation</b>	<b>356,817</b>	<b>347,624</b>
<b>Funded status</b>	<b>\$ (133,917)</b>	<b>\$ (150,562)</b>
Accumulated benefit obligation	\$ 356,807	\$ 347,619
<b>Net amount recognized in long-term liabilities in the consolidated balance sheets</b>	<b>\$ (133,917)</b>	<b>\$ (150,562)</b>
Amounts recognized in accumulated other comprehensive income:		
Prior service credit	\$ 29,867	\$ 32,909
Net actuarial loss	(93,953)	(106,704)
<b>Net amount recognized in accumulated other comprehensive income</b>	<b>\$ (64,086)</b>	<b>\$ (73,795)</b>

- (a) In the first quarter of 2015, the Company recognized a prior service credit for a negative plan amendment at remeasurement of the represented employees pension plan related to the elimination of prospective future increase in pension bands that were reduced under the terms of the collective bargaining agreements.

	Post-employment Benefit Plans	
	Year Ended December 31, 2016	Year Ended December 31, 2015
Fair value of plan assets:		
Beginning fair value of plan assets	\$ —	\$ —
Employer contributions	5,715	5,597
Benefits paid	(5,715)	(5,597)
<b>Ending fair value of plan assets</b>	<b>—</b>	<b>—</b>
Projected benefit obligation:		
Beginning projected benefit obligation	\$ 100,154	\$ 741,372
Service cost	121	4,541
Interest cost	3,927	7,688
Plan amendments <sup>(a)</sup>	—	(609,619)
Plan curtailment	—	(5,409)
Benefits paid	(5,715)	(5,597)
Actuarial loss	(3,720)	(32,822)
<b>Ending projected benefit obligation</b>	<b>94,767</b>	<b>100,154</b>
<b>Funded status</b>	<b>\$ (94,767)</b>	<b>\$ (100,154)</b>
Amounts recognized in the consolidated balance sheets:		
Current liabilities	\$ (7,138)	\$ (6,112)
Long-term liabilities	(87,629)	(94,042)
<b>Net amount recognized in the consolidated balance sheets</b>	<b>\$ (94,767)</b>	<b>\$ (100,154)</b>
Amounts recognized in accumulated other comprehensive income:		
Net prior service credit	\$ 41,690	\$ 350,322
Net actuarial loss	\$ (16,508)	\$ (102,085)
<b>Net amount recognized in accumulated other comprehensive income</b>	<b>\$ 25,182</b>	<b>\$ 248,237</b>

- (a) In the first quarter of 2015, the Company recognized a net prior service credit for a negative plan amendment at remeasurement of the post-employment benefit plan for represented employees primarily related to the elimination of the post-employment benefits for active represented employees under the terms of the collective bargaining agreements.

**Qualified Pension Plan Assets.** The investment objective for the qualified pension plan assets is to achieve a rate of return sufficient to match or exceed the long-term growth rate of the plan liability, using investment vehicles that are consistent with the duration of each plan's liability. The investment objective also targets minimizing the risk of loss of principal. The Company's strategy emphasizes a long-term equity orientation, global diversification and financial and operating risk controls. Both active and passive management investment approaches are employed depending on perceived market efficiencies and various other factors. Diversification targets of 65% equity securities and 35% fixed income securities for the represented employees plan seeks to minimize the concentration of market risk. For the qualified pension plan for the non-represented employees, the diversification target is 45% equity securities and 55% fixed income securities and is invested using primarily a liability driven investment strategy. The asset allocation at December 31, 2016 for the Company's qualified pension plan assets was as follows:

	Non-Represented Employees Plan	Represented Employees Plan	Total Qualified Pension Plans
Cash and cash equivalents <sup>(a)</sup>	3.5%	5.4%	5.2%
Equity securities	42.0%	60.3%	58.3%

Fixed income securities	54.5%	34.3%	36.5%
<b>Plan asset portfolio allocation at December 31, 2016</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

- (a) Cash and cash equivalents at December 31, 2016 include amounts pending settlement from the purchase or sale of equity or fixed income securities.

The fair values for the qualified pension plan assets by asset category at December 31, 2016 are as follows (in thousands):

	Total	Level 1	Level 2	Level 3
Cash and cash equivalents	\$ 11,619	\$ 11,619	\$ —	\$ —
Equity securities	129,937	129,937	—	—
Fixed income securities	81,344	53,206	28,138	—
<b>Fair value of plan assets at December 31, 2016</b>	<b>\$ 222,900</b>	<b>\$ 194,762</b>	<b>\$ 28,138</b>	<b>\$ —</b>

The fair values for the qualified pension plan assets by asset category at December 31, 2015 were as follows (in thousands):

	Total	Level 1	Level 2	Level 3
Cash and cash equivalents	\$ 1,223	\$ 1,223	\$ —	\$ —
Equity securities	138,684	79,512	59,172	—
Fixed income securities	57,155	30,856	26,299	—
<b>Fair value of plan assets at December 31, 2015</b>	<b>\$ 197,062</b>	<b>\$ 111,591</b>	<b>\$ 85,471</b>	<b>\$ —</b>

Cash and cash equivalents include short-term investment funds, primarily in diversified portfolios of investment grade money market instruments and are valued using quoted market prices, and thus classified within Level 1 of the fair value hierarchy, as outlined in note (10) "Fair Value".

Equity securities include direct holdings of equity securities and units held in mutual funds that invest in equity securities of domestic and international corporations in a variety of industry sectors. The direct holdings and units held in publicly traded mutual funds are valued using quoted market prices and are classified within Level 1 of the fair value hierarchy. Fair values for units held in mutual funds that invest in equity securities that are not publicly traded are based on observable prices and are classified within Level 2 of the fair value hierarchy. The fair values of hedged equity funds are estimated using net asset value per share of the investments. The Company has the ability to redeem these investments at net asset value on a limited basis and thus has classified hedged equity funds within Level 3 of the fair value hierarchy. The Company liquidated its positions in all its hedged equity funds per the terms of its investment agreements with such hedge equity funds in 2015.

Fixed income securities are investments in corporate bonds, treasury securities, other debt instruments and mutual funds that invest in these instruments. These securities are expected to provide significant diversification benefits, in terms of asset volatility and pension funding volatility, in the portfolio and a stable source of income. Units held in corporate bonds, treasury securities and publicly traded mutual funds that invest in fixed income securities are valued using quoted market prices and are classified within Level 1 of the fair value hierarchy. Fair values of mutual funds that invest in fixed income securities that are not publicly traded are based on observable prices and are classified within Level 2 of the fair value hierarchy.

A reconciliation of the beginning and ending balance of plan assets that are measured at fair value using significant unobservable inputs (Level 3) for the year ended December 31, 2015 is as follows (in thousands):

	Hedged Equity Funds
Balance at December 31, 2014	\$ 351
Purchases, sales and settlements, net	(351)
<b>Balance at December 31, 2015</b>	<b>\$ —</b>

**Net Periodic Benefit Cost.** The Company capitalizes a portion of net periodic benefit cost in conjunction with its use of internal labor resources utilized on capital projects. During the years ended December 31, 2016, 2015 and 2014, the Company recognized settlement charges in the qualified pension plan that covers non-represented employees. The settlements were incurred when the cumulative amount of lump sums paid to participants in the respective years exceeded the expected service and interest cost for the respective years. Components of the net periodic benefit cost related to the Company's qualified pension plans and other post-employment benefit plans for the years ended December 31, 2016, 2015 and 2014 are as follows (in thousands):

	Qualified Pension Plans		
	Year Ended December 31, 2016	Year Ended December 31, 2015	Year Ended December 31, 2014
Service cost	\$ 6,880	\$ 8,391	\$ 14,760
Interest cost	15,079	14,879	15,367
Expected return on plan assets	(15,363)	(14,635)	(13,525)
Amortization of prior service credit	(3,042)	(2,933)	—
Amortization of actuarial loss	5,383	6,718	2,054
Plan curtailment <sup>(a)</sup>	—	(4,207)	—
Plan settlement	629	1,022	671
<b>Net periodic benefit cost</b>	<b>9,566</b>	<b>9,235</b>	<b>19,327</b>
Less capitalized portion	(599)	(600)	(1,184)
<b>Other post-employment benefit and pension (benefit)/expense</b>	<b>\$ 8,967</b>	<b>\$ 8,635</b>	<b>\$ 18,143</b>

(a) The Company recognized a curtailment gain as the result of a workforce reduction in July 2015.

	Post-employment Benefit Plans		
	Year Ended December 31, 2016	Year Ended December 31, 2015	Year Ended December 31, 2014
Service cost	\$ 121	\$ 4,541	\$ 24,969
Interest cost	3,927	7,688	29,908
Amortization of prior service credit	(308,632)	(304,626)	(948)
Amortization of actuarial loss	81,857	113,424	6,654
<b>Net periodic benefit cost</b>	<b>(222,727)</b>	<b>(178,973)</b>	<b>60,583</b>
Less capitalized portion	—	—	(3,444)
<b>Other post-employment benefit and pension (benefit)/expense</b>	<b>\$ (222,727)</b>	<b>\$ (178,973)</b>	<b>\$ 57,139</b>

**Other Comprehensive Income.** Other pre-tax changes in plan assets and benefit obligations recognized in other comprehensive income are as follows for the years ended December 31, 2016, 2015 and 2014, respectively, (in thousands):

	Qualified Pension Plans		
	Year Ended December 31, 2016	Year Ended December 31, 2015	Year Ended December 31, 2014
Amounts recognized in other comprehensive income:			
Prior service credit	\$ —	\$ (40,049)	\$ —
Net (gain)/loss arising during the period	(6,739)	(13,424)	72,670
Amortization of prior service credit	3,042	2,933	—
Amortization of net actuarial loss	(5,383)	(6,718)	(2,725)
Plan curtailment	—	1,781	—
Plan settlement	(629)	(1,022)	—
<b>Total amount recognized in other comprehensive income</b>	<b>\$ (9,709)</b>	<b>\$ (56,499)</b>	<b>\$ 69,945</b>

Estimated amounts that will be amortized from accumulated other comprehensive income in the next fiscal year:

Prior service credit	\$ 3,042
Net actuarial loss	(4,772)
<b>Total amount estimated to be amortized from accumulated other comprehensive income in the next fiscal year</b>	<b>\$ (1,730)</b>

	Post-employment Benefit Plans		
	Year Ended December 31, 2016	Year Ended December 31, 2015	Year Ended December 31, 2014
Amounts recognized in other comprehensive income:			
Prior service credit	\$ —	\$ (619,454)	\$ (46,277)
Prior service cost	—	9,835	—
Plan curtailment	—	(5,409)	—
Net (gain)/loss arising during the period	(3,720)	(32,822)	148,434
Amortization of prior service credit	308,632	304,626	948
Amortization of net actuarial loss	(81,857)	(113,424)	(6,654)
<b>Total amount recognized in other comprehensive income</b>	<b>\$ 223,055</b>	<b>\$ (456,648)</b>	<b>\$ 96,451</b>

Estimated amounts that will be amortized from accumulated other comprehensive income in the next fiscal year:

Net prior service credit	\$ 1,819
Net actuarial loss	(1,083)
<b>Total amount estimated to be amortized from accumulated other comprehensive income in the next fiscal year</b>	<b>\$ 736</b>

### Assumptions

The determination of the net liability and the net periodic benefit cost recognized for the qualified pension plans and post-employment benefit plans by the Company are, in part, based on assumptions made by management. These assumptions include, among others, the discount rate applied to estimated future cash flows of the plans, the expected return on assets held by the qualified pension plans, certain demographic characteristics of the participants, such as expected retirement and mortality rates, and future inflation in healthcare costs. The Company also has an assumption regarding increases in the amount of post-employment benefit plans expenditures to be paid by the Company, based upon the past practice of such increases being provided to participants. These assumptions are reviewed at least annually for changes with the Company's independent actuaries.



**Projected Benefit Obligation Assumptions.** The weighted average assumptions used in determining projected benefit obligations are as follows:

	December 31, 2016	December 31, 2015
Qualified Pension Plans:		
Discount rate	4.49%	4.44%
Rate of compensation increase <sup>(a)</sup>	3.00%	3.00%
Post-employment Benefit Plans:		
Discount rate	4.20%	4.15%
Rate of compensation increase <sup>(a)</sup>	N/A	N/A

- (a) The rate of future increases in compensation assumption only applies to the plans for represented employees as plans for non-represented employees are frozen.

**Net Periodic Benefit Cost Assumptions.** The weighted average assumptions used in determining net periodic cost are as follows:

	Years Ended December 31,		
	2016	2015	2014
Qualified Pension Plans:			
Discount rate	4.48%	4.39%	4.92%
Expected return on plan assets <sup>(a)</sup>	7.34%	7.31%	7.66%
Rate of compensation increase <sup>(b)</sup>	3.00%	3.00%	3.00%
Post-employment Benefit Plans:			
Discount rate	4.18%	3.54%	4.98%
Rate of compensation increase <sup>(b)</sup>	N/A	N/A	4.00%
Healthcare cost trend rate <sup>(c)</sup>	7.40%	7.70%	7.90%
Rate that the cost trend rates ultimately declines to	4.50%	4.50%	4.50%
Year that the rates reach the terminal rate	2037	2030	2030

- (a) The expected return on plan assets is the long-term rate-of-return the Company expects to earn on the plan assets. In developing the expected return on plan asset assumption, the Company evaluated historical investment performance, the plans' asset allocation strategies and return forecasts for each asset class and input from its advisors. Projected returns by such advisors were based on broad equity and fixed income indices. The expected return on plan assets is reviewed annually in conjunction with other plan assumptions and, if considered necessary, revised to reflect changes in the financial markets and the investment strategy. The investment strategy and target allocations of the qualified pension plans previously disclosed in "—Plan Assets, Obligations and Funded Status—Qualified Pension Plan Assets" herein were utilized.
- (b) The rate of future increases in compensation assumption only applies to the plans for represented employees as plans for non-represented employees are frozen.
- (c) The rate of healthcare cost trend assumption for 2016 and 2015 applies to the other post-employment benefit plan for management and existing represented retirees.

**Post-employment Benefit Plans Sensitivity.** A 1% change in the medical trend rate assumed for post-employment benefits at December 31, 2016 would have the following effects (in thousands):

	Increase (Decrease)
1% increase in the medical trend rate:	
Effect on total service cost and interest cost components	\$ 420
Effect on benefit obligation	\$ 10,122
1% decrease in the medical trend rate:	
Effect on total service cost and interest cost components	\$ (349)

Effect on benefit obligation

\$

(8,423)

---

### Estimated Future Contributions and Benefit Payments

Legislation enacted in 2014 changed the method in determining the discount rate used for calculating a qualified pension plan's unfunded liability. This act contained a pension funding stabilization provision which allows pension plan sponsors to use higher interest rate assumptions when determining funded status and funding obligations. As a result, the Company's 2016 and 2015 minimum required pension plan contributions are significantly lower than it would have been in the absence of this stabilization provision.

Estimated future employer contributions and benefit payments as of December 31, 2016 are as follows (in thousands):

	Qualified Pension Plans	Post-employment Benefit Plans
Expected employer contributions for fiscal year 2017	\$ 18,431	\$ 7,138
Expected benefit payments for fiscal years:		
2017	\$ 8,558	\$ 7,138
2018	9,919	6,686
2019	11,473	6,637
2020	11,846	6,455
2021	13,135	6,267
2022-2026	84,859	27,230

### 401(k) Savings Plans

As of December 31, 2016, the Company and its subsidiaries sponsor a voluntary 401(k) savings plans that cover all eligible Telecom Group employees and northern New England management employees, and a voluntary 401(k) savings plan that covers all eligible northern New England represented employees (collectively, "the 401(k) Plans"). Each 401(k) Plan year, the Company contributes an amount of matching contributions to the 401(k) Plans determined by the Company at its discretion for management employees and based on collective bargaining agreements for all other employees. For the 401(k) Plan years ended December 31, 2016, 2015 and 2014, the Company generally matched 100% of each employee's contribution up to 5% of compensation. Total Company contributions to all 401(k) Plans were \$8.9 million, \$8.8 million and \$9.5 million for the years ended December 31, 2016, 2015 and 2014, respectively.

### (12) Income Taxes

#### Income Tax (Expense)/Benefit

Income tax (expense)/benefit for the years ended December 31, 2016, 2015, 2014, respectively, consists of the following components (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Current:			
Federal	\$ —	\$ —	\$ —
State and local	(240)	(203)	(86)
<b>Total current income tax expense</b>	<b>(240)</b>	<b>(203)</b>	<b>(86)</b>
Deferred:			
Federal	(35,179)	(1,501)	25,081
State and local	(7,430)	2,761	4,783
<b>Total deferred income tax (expense)/benefit</b>	<b>(42,609)</b>	<b>1,260</b>	<b>29,864</b>
<b>Total income tax (expense)/benefit</b>	<b>\$ (42,849)</b>	<b>\$ 1,057</b>	<b>\$ 29,778</b>

For the year ended December 31, 2016, the tax expense on \$146.9 million of pre-tax net income equates to an effective tax rate of 29.2%. The rate differs from the 35% federal statutory rate primarily due to a tax benefit associated with a decrease in the valuation allowance offset by a tax expense related to state taxes.



For the year ended December 31, 2015, the tax benefit on \$89.4 million of pre-tax net income equates to an effective tax rate of (1.2)%. The rate differs from the 35% federal statutory rate primarily due to a tax benefit associated with a decrease in the valuation allowance as well as a tax benefit related to state taxes.

For the year ended December 31, 2014, the tax benefit on \$166.1 million of pre-tax loss equates to an effective tax rate of 17.9%. The rate differs from the 35% federal statutory rate primarily due to tax expense associated with an increase in the valuation allowance offset by a tax benefit related to state taxes.

A reconciliation of the Company's statutory tax rate to its effective tax rate is presented below (in percentages):

	Years Ended December 31,		
	2016	2015	2014
<b>Statutory federal income tax/(benefit) rate<sup>(1)</sup></b>	<b>35.0 %</b>	<b>35.0 %</b>	<b>(35.0)%</b>
State income tax benefit, net of federal income tax	3.3	(1.9)	(2.1)
Other, net	0.7	0.2	0.3
Valuation allowance (benefit)/expense	(9.8)	(34.5)	18.9
<b>Effective income tax rate</b>	<b>29.2 %</b>	<b>(1.2)%</b>	<b>(17.9)%</b>

(1) The statutory federal income tax is an expense in 2016 and 2015 due to pre-tax net income for those years and the statutory federal income tax is a benefit in 2014 due to pre-tax net losses for the year ended December 31, 2014.

The effective tax rate reflected in accumulated other comprehensive income for the year ended December 31, 2016 is 23.2%. This effective tax rate is due to a tax benefit on other net comprehensive loss partially offset by tax expense associated with an increase in the valuation allowance.

#### Deferred Income Taxes

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities as of December 31, 2016 and 2015 are presented below (in thousands):

	December 31, 2016	December 31, 2015
Deferred tax assets:		
Federal and state tax loss carryforwards	\$ 106,928	\$ 103,981
Employee benefits	107,152	115,531
Allowance for doubtful accounts	1,454	3,342
Alternative minimum tax and other state credits	4,299	5,094
Capitalized restructuring costs	2,326	2,739
Deferred revenue	3,636	4,414
Other, net	4,673	8,059
<b>Total gross deferred tax assets</b>	<b>230,468</b>	<b>243,160</b>
Deferred tax liabilities:		
Property, plant, and equipment	183,575	212,906
Goodwill and other intangible assets	26,184	29,588
Other, net	7,274	10,613
<b>Total gross deferred tax liabilities</b>	<b>217,033</b>	<b>253,107</b>
<b>Net deferred tax assets (liabilities) before valuation allowance</b>	<b>13,435</b>	<b>(9,947)</b>
Valuation allowance	(41,451)	(25,128)
<b>Net deferred tax liabilities</b>	<b>\$ (28,016)</b>	<b>\$ (35,075)</b>

At December 31, 2016, the Company had gross federal NOL carryforwards of \$285.0 million. The Company's remaining federal NOL carryforwards will expire from 2019 to 2036. At December 31, 2016, the Company had a net, after attribute reduction, state NOL deferred tax asset of \$11.6 million. The Company's remaining state NOL carryforwards will expire from 2017 to 2036. The amount that expired in 2016 was negligible. At December 31, 2016, the Company had a negligible alternative minimum tax credit carryover and had \$4.3 million in state credit carryovers. Telecom Group completed an initial public offering on February 8, 2005, which resulted

in an "ownership change" within the meaning of the United States of America federal income tax laws addressing NOL carryforwards, alternative minimum tax credits and other similar tax attributes. The Spinco Merger and the

Company's emergence from Chapter 11 protection also resulted in ownership changes. As a result of these ownership changes, there are specific limitations on the Company's ability to use its NOL carryforwards and other tax attributes. The Company believes it can use the NOLs even with these restrictions in place.

**Valuation Allowance.** At December 31, 2016 and 2015, the Company established a valuation allowance against its deferred tax assets of \$41.5 million and \$25.1 million, respectively, which consists of a \$29.2 million and \$14.7 million federal allowance, respectively, and a \$12.3 million and \$10.4 million state allowance, respectively. During 2016, an increase in the Company's valuation allowance of \$35.5 million was allocated to accumulated other comprehensive income in the consolidated balance sheet. During 2015, a decrease in the Company's valuation allowance of \$195.5 million was allocated to accumulated other comprehensive income in the consolidated balance sheet. During 2014, an increase in the Company's valuation allowance of \$58.3 million was allocated to accumulated other comprehensive income in the consolidated balance sheet.

The following is activity in the Company's valuation allowance for the years ended December 31, 2016, 2015 and 2014, respectively (in thousands):

	Years Ended December 31,		
	2016	2015	2014
<b>Balance, beginning of period</b>	\$ (25,128)	\$ (259,857)	\$ (166,773)
(Increase) decrease allocated to other comprehensive income	(35,511)	195,540	(58,254)
(Increase) decrease allocated to continuing operations	19,188	39,189	(34,830)
<b>Balance, end of period</b>	\$ (41,451)	\$ (25,128)	\$ (259,857)

**Unrecognized Tax Benefits.** As of December 31, 2016, the Company's total unrecognized tax benefits were \$4.0 million, which were recorded as a reduction of the Company's federal and state NOL carryforwards. The total unrecognized tax benefits that, if recognized, would affect the effective tax rate were \$3.8 million. The Company does not expect a significant increase or decrease in its unrecognized tax benefits during the next twelve months. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (in thousands):

<b>Balance as of December 31, 2014</b>	\$	4,035
Additions for tax positions of prior years		12
<b>Balance as of December 31, 2015</b>	\$	4,047
Additions for tax positions of prior years		—
<b>Balance as of December 31, 2016</b>	\$	4,047

The Company recognizes any interest and penalties accrued related to unrecognized tax benefits in income tax expense. During the year ended December 31, 2014, the Company made payments of interest and penalties in the amount of \$0.1 million. During the years ended December 31, 2016 and December 31, 2015, the Company did not make any payments of interest and penalties. There was nothing accrued in the consolidated balance sheets for the payment of interest and penalties at December 31, 2016 and 2015, respectively, as the remaining unrecognized tax benefits would only serve to reduce the Company's current federal and state NOL carryforwards, if ultimately recognized.

#### **Income Tax Returns**

The Company and its eligible subsidiaries file consolidated income tax returns in the United States of America federal jurisdiction and certain consolidated, combined and separate entity tax returns, as required, with various state and local governments. Based solely on statutes of limitations, the Company would not be subject to United States of America federal, state and local, or non-United States of America income tax examinations by tax authorities for years prior to 2012. However, tax years prior to 2012 may be subject to examination by federal or state taxing authorities if the Company's NOL carryovers from those years are utilized in the future. As of December 31, 2016 and 2015, the Company does not have any significant jurisdictional tax audits.

**(13) Accumulated Other Comprehensive Income**

Components of accumulated other comprehensive income, net of income tax, were as follows (in thousands):

	December 31, 2016	December 31, 2015
Accumulated other comprehensive income, net of taxes:		
Fair value of interest rate swaps	\$ (1,054)	\$ (2,160)
Qualified pension and other post-employment benefit plans	22,590	186,152
<b>Total accumulated other comprehensive income, net of taxes</b>	<b>\$ 21,536</b>	<b>\$ 183,992</b>

Other comprehensive income for the years ended December 31, 2016 and 2015, respectively, includes changes in the fair value of the Company's cash flow hedges, actuarial losses and prior service credits related to the qualified pension and other post-employment benefit plans arising during the respective periods and amortization of these actuarial losses and prior service credits. For further detail of amounts recognized in other comprehensive income related to the cash flow hedges, *see* note (9) "Interest Rate Swap Agreements" herein. For further detail of amounts recognized in other comprehensive income related to the qualified pension and other post-employment benefit plans, *see* note (11) "Employee Benefit Plans—Plan Assets, Obligations and Funded Status—Other Comprehensive Income" herein.

The following table provides a reconciliation of adjustments reclassified from accumulated other comprehensive income to the consolidated statement of operations (in thousands):

	Year Ended December 31, 2016
<b>Employee benefits:</b>	
Amortization of actuarial loss (.65 years to 11.47 years) <sup>(a)</sup>	\$ 87,240
Amortization of net prior service credit (.87 years to 23.91 years) <sup>(a)</sup>	(311,674)
Plan settlement <sup>(b)</sup>	629
Total employee benefits reclassified from accumulated other comprehensive income	(223,805)
Tax benefit <sup>(b)</sup>	52,214
Total employee benefits reclassified from accumulated other comprehensive income, net	\$ (171,591)
<b>Interest rate swaps:</b>	
Interest rate swaps reclassified from accumulated other comprehensive income <sup>(c)</sup>	\$ 2,446
Tax expense <sup>(b)</sup>	\$ (979)
Total interest rate swaps reclassified from accumulated other comprehensive income, net	\$ 1,467
<b>Total amounts reclassified from accumulated other comprehensive income, net</b>	<b>\$ (170,124)</b>

(a) These accumulated other comprehensive income components are included in the computation of net periodic benefit cost. *See* note (11) "Employee Benefit Plans" for details.

(b) *See* note (12) "Income Taxes" for details.

(c) These accumulated other comprehensive income components are included in interest expense. *See* note (9) "Interest Rate Swap Agreements" for details.

**(14) Earnings Per Share**

Basic earnings per share of the Company is computed by dividing net income/(loss) by the weighted average number of shares of common stock outstanding for the period. Except when the effect would be anti-dilutive, the diluted earnings per share calculation using the treasury stock method includes the impact of stock units, shares of non-vested restricted stock and shares that could be issued under outstanding stock options.

Weighted average number of common shares used for basic earnings per share excludes weighted average shares of non-vested restricted stock of 199,222, 232,274 and 235,462 for the years ended December 31, 2016, 2015 and 2014, respectively. Non-vested restricted stock is included in common shares issued and outstanding in the consolidated balance sheets.



Potentially dilutive shares exclude warrants and stock options in accordance with the treasury stock method primarily due to exercise prices exceeding the average market value. Since the Company incurred a loss for the year ended December 31, 2014, all potentially dilutive securities are anti-dilutive and, therefore, are excluded from the determination of diluted earnings per share.

The following table provides a reconciliation of the common shares used for basic earnings per share and diluted earnings per share:

	Years Ended December 31,		
	2016	2015	2014
Weighted average number of common shares used for basic earnings per share	26,854,396	26,652,240	26,449,408
Effect of potential dilutive shares	265,041	320,639	—
<b>Weighted average number of common shares and potential dilutive shares used for diluted earnings per share</b>	<b>27,119,437</b>	<b>26,972,879</b>	<b>26,449,408</b>
Weighted average number of anti-dilutive shares outstanding at period-end that are excluded from the above reconciliation	3,916,342	4,141,096	4,463,364

#### (15) Stockholders' Deficit

At December 31, 2016, 37,500,000 shares of common stock were authorized and 27,074,398 shares of common stock (including shares of non-vested restricted stock) and 3,582,402 warrants, each eligible to purchase one share of common stock, were outstanding.

The initial exercise price applicable to the warrants is \$48.81 per share of common stock. The exercise price applicable to the warrants is subject to adjustment upon the occurrence of certain events described in the warrant agreement. The warrants may be exercised at any time on or before January 24, 2018.

#### (16) Stock-Based Compensation

Stock-based compensation expense recognized in the financial statements is as follows (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Amounts charged against income, before income tax benefit	\$ 6,291	\$ 6,357	\$ 4,274
Amount of related income tax benefit recognized in income	(2,516)	(2,529)	(1,714)
<b>Total net income/loss impact</b>	<b>\$ 3,775</b>	<b>\$ 3,828</b>	<b>\$ 2,560</b>

At December 31, 2016, the Company had \$5.6 million of stock-based compensation cost related to non-vested awards that will be recognized over a weighted average period of 1.75 years, all of which is related to awards granted under the Long Term Incentive Plan.

#### *Long Term Incentive Plan*

The Long Term Incentive Plan provides for grants of up to 5,674,277 shares of common stock awards, of which stock options, restricted stock awards and performance share awards and other types of equity awards can be granted. As of December 31, 2016, there are 1,423,409 shares available for grant under the Long Term Incentive Plan. Each stock option granted reduces the availability under the Long Term Incentive Plan by one share. Prior to the approval of the amendment and restatement of the Long Term Incentive Plan by the Company's stockholders on May 12, 2014, each restricted stock award granted reduced the availability under the Long Term Incentive Plan by one share and on or after May 12, 2014 each restricted stock award granted reduces the availability by 1.35 shares. Upon the exercise of each stock option or vesting of each restricted share award, one new share of common stock will be issued.

For the years ended December 31, 2016, 2015 and 2014, the Company granted shares of restricted stock and stock options with one of the following vesting terms: (i) vest immediately; (ii) vest 100% on the first anniversary; (iii) vest over three equal annual installments, with one-third vesting on the first anniversary of the grant date and one-third on the second and third anniversaries thereafter or (iv) vest 25% immediately and 25% on the first, second and third anniversaries thereafter. In addition,

for the year ended December 31, 2016, the Company granted performance share awards that vest at the end of a three-year performance period based upon achievement of certain market (total shareholder return) and non-market (growth revenue) performance measures.

**Stock Options.** Stock options have a term of 10 years from the date of grant; however, vested stock options will generally expire 90 days after an employee's termination with the Company, unless the Company is in a blackout period. Stock option activity under the Long Term Incentive Plan is summarized as follows:

	Options Outstanding	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life (in years)
<b>Outstanding at December 31, 2013</b>	<b>1,399,123</b>	<b>\$ 16.74</b>	
Granted <sup>(a)</sup>	462,374	13.31	
Exercised	(51,050)	6.28	
Forfeited	(2,005)	4.31	
Expired	(33,597)	23.65	
<b>Outstanding at December 31, 2014</b>	<b>1,774,845</b>	<b>\$ 16.03</b>	
Granted <sup>(a)</sup>	620,843	14.74	
Exercised <sup>(b)</sup>	(210,638)	10.07	
Forfeited	(83,495)	13.41	
Expired	(70,943)	24.07	
<b>Outstanding at December 31, 2015</b>	<b>2,030,612</b>	<b>\$ 16.08</b>	
Granted <sup>(a)</sup>	531,975	14.57	
Exercised <sup>(b)</sup>	(178,650)	10.27	
Forfeited	(96,592)	14.35	
Expired	(115,875)	23.58	
<b>Outstanding at December 31, 2016</b>	<b>2,171,470</b>	<b>\$ 15.87</b>	<b>6.5</b>
<b>Exercisable at December 31, 2016 <sup>(c)</sup></b>	<b>1,492,405</b>	<b>\$ 16.49</b>	<b>5.6</b>
<b>Vested and Expected to Vest at December 31, 2016 <sup>(d)</sup></b>	<b>2,148,754</b>	<b>\$ 15.88</b>	<b>6.5</b>

(a) During the years ended December 31, 2016, 2015 and 2014, the weighted average grant date fair value of stock options granted was \$4.3 million, \$5.4 million and \$3.2 million, respectively. For purposes of determining compensation expense, the grant date fair value per share of the stock options was estimated using the Black-Scholes option pricing model which requires the use of various assumptions including the expected life of the option, expected dividend rate, expected volatility and risk-free interest rate. Key assumptions used for determining the fair value of stock options granted were as follows:

	Years Ended December 31,		
	2016	2015	2014
Expected life <sup>(1)</sup>	5.5 - 6.5 years	5.5 - 6.5 years	5.5 - 6.5 years
Expected dividend <sup>(2)</sup>	—	—	—
Expected volatility <sup>(3)</sup>	55.1%	59.6%	51.0%
Risk-free interest rate <sup>(4)</sup>	1.40% - 1.76%	1.35% - 2.02%	1.63% - 2.19%

(1) The 5.5-year and 6.5-year expected lives (estimated period of time outstanding) of stock options granted were estimated using the 'Simplified Method' which utilizes the midpoint between the vesting date and the end of the contractual term. This method was utilized for the stock options due to the lack of historical exercise behavior of the Company's employees.

(2) For all stock options granted during 2016, 2015 and 2014, no dividends are planned to be paid over the contractual term of the stock options resulting in the use of a zero expected dividend rate.

(3) The expected volatility rate is based on the observed historical volatilities of the Company's common stock and

observed historical and implied volatilities of comparable companies, which were adjusted to account for the various differences between the comparable companies and the Company.

- (4) The risk-free interest rate is specific to the date of grant and is based on the United States Treasury constant maturity market yield in effect at the time of the grant.
- (b) During the years ended December 31, 2016 and 2015, the total intrinsic value of stock options that were exercised was \$0.9 million and \$1.7 million, respectively.
- (c) Based upon a fair market value of the common stock as of December 30, 2016 of \$18.70 per share, the stock options that are exercisable have an aggregate intrinsic value (equal to the value of in-the-money stock options above their respective exercise price) of \$6.5 million.
- (d) Based upon a fair market value of the common stock as of December 30, 2016 of \$18.70 per share, the stock options that have vested and are expected to vest have an aggregate intrinsic value (equal to the value of in-the-money stock options above their respective exercise price) of \$9.2 million.

Based upon the respective grant fair value, the aggregate fair value of stock options that vested during the years ended December 31, 2016, 2015, and 2014 was \$3.2 million, \$2.7 million, and \$2.9 million, respectively.

*Time-Based Restricted Stock Awards.* Restricted stock award activity under the Long Term Incentive Plan is summarized as follows:

	Awards Outstanding	Weighted Average Grant Date Fair Value Per Share
<b>Non-vested at December 31, 2013</b>	<b>264,655</b>	<b>\$ 12.64</b>
Granted <sup>(a)</sup>	216,586	13.21
Vested <sup>(b)</sup>	(249,205)	13.58
<b>Non-vested at December 31, 2014</b>	<b>232,036</b>	<b>\$ 12.15</b>
Granted <sup>(a)</sup>	161,011	15.06
Vested <sup>(b)</sup>	(156,445)	12.52
Forfeited	(10,550)	\$ 12.21
<b>Non-vested at December 31, 2015</b>	<b>226,052</b>	<b>\$ 13.97</b>
Granted <sup>(a)</sup>	175,735	14.68
Vested <sup>(b)</sup>	(158,469)	13.89
Forfeited	(47,350)	14.42
<b>Non-vested at December 31, 2016</b>	<b>195,968</b>	<b>\$ 14.56</b>

- (a) The grant date fair value per share of the restricted stock awards under the Long Term Incentive Plan was calculated as the fair market value per share of the common stock on the date of grant. During the years ended December 31, 2016, 2015 and 2014, the weighted average grant date fair value of restricted stock awards granted was \$2.6 million, \$2.4 million, and \$2.9 million, respectively.
- (b) Based upon the respective grant date fair value, the aggregate fair value of restricted stock which vested during the years ended December 31, 2016, 2015 and 2014 was \$2.2 million, \$2.0 million and \$3.4 million, respectively.

*Performance Share Awards.* Performance share awards activity under the Long Term Incentive Plan is summarized as follows:

	Awards Outstanding	Weighted Average Grant Date Fair Value Per Share
<b>Non-vested at December 31, 2014</b>	<b>—</b>	<b>\$ —</b>
Granted <sup>(a)</sup>	149,500	12.87
Forfeited	(18,443)	12.82
<b>Non-vested at December 31, 2015</b>	<b>131,057</b>	<b>\$ 12.87</b>
Granted <sup>(a)</sup>	126,000	11.88
Forfeited	(38,278)	12.38
<b>Non-vested at December 31, 2016</b>	<b>218,779</b>	<b>\$ 12.39</b>

- (a) During the years ended December 31, 2016 and 2015, the weighted average grant date fair value of performance share

awards granted was \$1.5 million and \$1.9 million, respectively. The grant date fair value of the non-market portion of the performance share awards was calculated as the fair market value of the common stock on the date of grant. For

purposes of determining compensation expense for the market portion of the performance share awards, the grant date fair value was estimated using the Monte Carlo valuation model.

## (17) Business Concentrations

### *Geographic*

As of December 31, 2016, 83% of the Company's residential voice lines were located in Maine, New Hampshire and Vermont. As a result of this geographic concentration, the Company's financial results will depend significantly upon economic conditions in these markets. A deterioration or recession in any of these markets could result in a decrease in demand for the Company's services and a resulting loss of access line equivalents which could have a material adverse effect on the Company's business, financial condition, results of operations, liquidity and/or the market price of the Company's outstanding securities.

In addition, if state regulators in Maine, New Hampshire or Vermont were to take an action that is adverse to the Company's operations in those states, the Company could suffer greater harm from that action by state regulators than it would from action in other states because of the concentration of operations in those states.

### *Labor*

As of December 31, 2016, the Company employed approximately 2,500 employees, approximately 1,500, or 60%, of whom were covered by 13 collective bargaining agreements.

## (18) Commitments and Contingencies

### *(a) Leases*

The Company currently leases real estate and network equipment under capital and operating leases expiring through the year ending 2039. The Company accounts for leases using the straight-line method, which amortizes contracted total payments evenly over the lease term.

Future minimum lease payments under capital leases and non-cancelable operating leases as of December 31, 2016 are as follows (in thousands):

	<u>Capital Leases</u>	<u>Operating Leases</u>
Year ending December 31:		
2017	\$ 1,279	\$ 6,644
2018	921	4,607
2019	554	2,912
2020	224	1,895
2021	56	962
Thereafter	—	739
<b>Total minimum lease payments</b>	<b>\$ 3,034</b>	<b>\$ 17,759</b>
Less: interest and executory cost	(496)	
<b>Present value of minimum lease payments</b>	<b>2,538</b>	
Less: current installments	(1,227)	
<b>Long-term obligations at December 31, 2016</b>	<b>\$ 1,311</b>	

Total rent expense primarily for real estate, vehicles and office equipment was \$9.4 million, \$9.4 million and \$9.8 million for the years ended December 31, 2016, 2015 and 2014, respectively.

The Company does not have any leases with contingent rental payments or any leases with contingency renewal, purchase options, or escalation clauses.

### *(b) Legal Proceedings*

From time to time, the Company is party to various other legal and regulatory proceedings in the ordinary course of business. The Company is a defendant in approximately 16 lawsuits filed by two long distance communications companies, who as plaintiffs

have collectively filed over 60 lawsuits arising from switched access charges for calls originating and terminating within the same wireless major trading area. These cases have all been consolidated and transferred to federal district court (the "Court") in Dallas.

Texas. The defendants filed joint motions to dismiss these actions. On November 17, 2015, the Court granted the defendants' motions dismissing the plaintiffs' federal law based claims with prejudice. The state law based claims were allowed to be amended and refiled. The Court denied the plaintiffs' request for an immediate appeal of the dismissal of the federal law based claims. Counterclaims against the plaintiffs for the failure to pay these access charges have been filed by the Company. The Company and some of the co-defendants have filed lawsuits against a third long distance communications company for the failure to pay this same type of access charge. These additional lawsuits have also been consolidated and transferred to the Court. Additional motions have been filed by the plaintiffs and defendants, which are still pending. At this time, an estimate of the impact, if any, of these claims cannot be made.

See also "Class Action Complaint" under note (20) "Subsequent Events" herein.

While management presently believes that the ultimate outcome of these proceedings, individually and in the aggregate, will not materially harm the Company's financial position, cash flows, or overall trends in results of operations, legal proceedings are inherently uncertain, and unfavorable rulings could, individually or in aggregate, have a material adverse effect on the Company's business, financial condition, or operating results.

**(c) Restricted Cash**

As of December 31, 2016 and 2015, the Company had \$0.7 million and \$0.7 million, respectively, of restricted cash, which is restricted for regulatory purposes and is included in long-term restricted cash on the consolidated balance sheets.

**(19) Quarterly Financial Information (Unaudited)**

The quarterly information presented below represents selected quarterly financial results for the quarters ended March 31, June 30, September 30, and December 31, 2016 and 2015 (in thousands, except per share data).

2016	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenue	\$ 206,816	\$ 206,557	\$ 207,141	\$ 203,929
Other post-employment benefit and pension (benefit)/expense (1)	(53,228)	(53,486)	(67,428)	(39,618)
Net income (2)	18,568	29,315	40,207	16,005
Income/(loss) per share:				
Basic	\$ 0.69	\$ 1.09	\$ 1.50	\$ 0.60
Diluted	\$ 0.68	\$ 1.08	\$ 1.48	\$ 0.59

2015	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenue	\$ 213,974	\$ 214,098	\$ 221,569	\$ 209,824
Other post-employment benefit and pension (benefit)/expense (1)	(6,898)	(52,460)	(57,568)	(53,412)
Net income/(loss) (2)	(45,213)	40,265	53,054	42,310
Loss per share:				
Basic	\$ (1.70)	\$ 1.51	\$ 1.99	\$ 1.59
Diluted	\$ (1.70)	\$ 1.49	\$ 1.96	\$ 1.56

(1) Presented for comparative purposes.

(2) The Company generated net income beginning in the second quarter of 2015 largely due to the remeasurement of the employee benefit plans in the first quarter of 2015 as described further in note (11) "Employee Benefit Plans."

**(20) Subsequent Events*****Class Action Complaint***

On February 7, 2017, an alleged class action complaint was filed by a purported stockholder of FairPoint Communications in the United States District Court for the Western District of North Carolina (Case No. 3:17-cv-51) against FairPoint Communications, its directors, Consolidated and Merger Sub. Among other things, the complaint alleges that the disclosures in the Form S-4 Registration Statement filed by Consolidated with the Securities and Exchange Commission on January 26, 2017 in connection with the Merger are materially incomplete and misleading in violation of Sections 14(a) and 20(a) of the Exchange Act. The plaintiff seeks to enjoin the defendants from consummating the Merger on the agreed-upon terms or alternatively, to rescind the Merger in the event the defendants consummate the Merger, in addition to damages and attorney fees and costs. FairPoint Communications and the other defendants have not yet filed an answer or other responsive pleading to the complaint.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

**ITEM 9A. CONTROLS AND PROCEDURES*****(a) Evaluation of Disclosure Controls and Procedures***

As of the end of the period covered by this Annual Report, we carried out an evaluation under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, of the effectiveness of our "disclosure controls and procedures" (as defined in Rule 13a-15(e) of the Exchange Act). Disclosure controls and procedures are controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC.

Based upon this evaluation, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were effective as of December 31, 2016.

***(b) Changes in Internal Control Over Financial Reporting***

There have been no changes in our internal control over financial reporting during the quarter ended December 31, 2016 that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

See "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report for the Report of Management on Internal Control over Financial Reporting and the Report of Independent Registered Public Accounting Firm on Internal Control over Financial Reporting, each of which is incorporated herein by reference.

**ITEM 9B. OTHER INFORMATION**

Not applicable.

## PART III

## ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

*Directors*

The following table sets forth the names and ages of our directors, with the exception of Mr. Sunu, as of December 31, 2016.

<u>Name</u>	<u>Age</u>
Peter D. Aquino	55
Dennis J. Austin	72
Peter C. Gingold	43
Edward D. Horowitz	69
Michael J. Mahoney	66
Michael K. Robinson	59
David L. Treadwell	62
Wayne Wilson	67

*Peter D. Aquino*—Mr. Aquino has served as President and CEO of Internap Corporation ("Internap") (NASDAQ: INAP) since September 2016. Mr. Aquino held leadership positions in both public and private companies, specializing in turnarounds, start-ups and emerging markets. He is the founder of Broad Valley Capital, LLC, focused on companies needing both telecommunications expertise and capital. Mr. Aquino previously served as the Executive Chairman of Primus Telecom Group, Inc. ("PTGI") (NYSE: PTGI) until April 30, 2013, transitioning from chairman and CEO after nearly a three-year assignment with the international telecommunications company. Prior to PTGI, Mr. Aquino was the President and CEO of RCN Corporation (formerly NASDAQ: RCNI) from December 2004 until its go-private sale in August 2010. Mr. Aquino formerly served as chairman of the United Way Worldwide - U.S. Board of Trustees through 2015 and as a board member of TiVo, Inc. (NASDAQ: TIVO) through 2016. Mr. Aquino currently serves as a board member of Internap and Lumos Networks Corp. (NASDAQ: LMOS). Mr. Aquino is a graduate of Montclair State College in New Jersey and has a Masters of Business Administration from George Washington University in Washington, DC.

We believe Mr. Aquino's qualifications to serve on our board include his leadership background in the communications industry, including his experience from both an operational and financial perspective and his service as a member of the board of directors of two other publicly-traded companies.

*Dennis J. Austin*—Mr. Austin has served as an independent telecommunications consultant since 2002. Mr. Austin previously served as a consultant at BearingPoint, formerly KPMG Consulting and formerly KPMG LLP, from 1995 to 2002 and as vice president at San Francisco Consulting Group ("SFCG") from 1985 to 1995. Prior to joining SFCG, Mr. Austin was vice president of engineering with Dataspeed Inc. from 1983 to 1985 and director of switch engineering, network planning and design at GTE Sprint from 1977 to 1983. Prior to joining GTE Sprint, Mr. Austin served as a member of the technical staff with Bell Telephone Laboratories from 1966 to 1977. Mr. Austin holds a Ph.D. in electrical engineering from Stanford University.

We believe Mr. Austin's qualifications to serve on our board include his significant consulting and leadership experience in the telecommunications industry, as well as his strong technical and product background.

*Peter C. Gingold*—Mr. Gingold joined Angelo, Gordon & Co. ("Angelo Gordon") in May of 2007 as a vice president and became a director of Angelo Gordon in February 2011, in each case focusing in distressed and leverage credit. Mr. Gingold became a managing director of Angelo Gordon in February 2014. Mr. Gingold's background includes significant management experience across several operational roles, positions as an investment banker and functions related to corporate development and strategy. Mr. Gingold currently serves as a board member of C&D Technologies, Inc. He holds a Bachelor of Science degree from Cornell University and a Master of Business Administration degree from the Columbia Business School.

We believe Mr. Gingold's qualifications to serve on our board include his extensive understanding of equity and debt capital markets, as well as his current and past positions on the boards or as a board observer of other companies.

*Edward D. Horowitz*—Mr. Horowitz currently serves as our chair of the board of directors. Mr. Horowitz is chairman of EdsLink LLC, a New York City based venture capital firm, which he founded in 2000 and is also a director of Globecom Systems Inc. and the First Responder Network Authority. He served as co-CEO of Encompass Digital Media, a global operator of satellite teleports and

digital content management from January 2013 through March 2014 and on its board from 2010 through 2014. Mr. Horowitz served as president and CEO of SES-Americom, a communications satellite operator and as a member of the executive

committee of its parent company, SES (SESG, Lux.) from 2005 to 2008. Before founding EdsLink LLC, Mr. Horowitz was executive vice president of Advanced Development at Citigroup from 1997 through 2000 and was the founder and chairman of e-Citi. Prior to joining Citigroup, from 1989 to 1997, Mr. Horowitz was a senior vice president of Viacom Inc. and a member of its operating committee. Mr. Horowitz is a trustee of the New York Hall of Science and the American Management Association. He received a Bachelor of Science degree in physics from the City College of New York and a Master of Business Administration degree from the Columbia Business School.

We believe Mr. Horowitz's qualifications to serve on our board include his breadth of leadership experience in the communications industry, as well as his current and past service on the boards of other companies.

*Michael J. Mahoney*—Mr. Mahoney previously served as president and CEO of Commonwealth Telephone Enterprises, Inc. ("Commonwealth Telephone") from 2000 to 2007. Prior to joining Commonwealth Telephone, Mr. Mahoney served as president and chief operating officer of RCN Corporation from 1997 to 2000 and as president and chief operating officer of C-TEC Corporation from 1993 to 1997. Mr. Mahoney currently serves as a director of Level 3 Communications, Inc. (NYSE: LVL3). He received a Bachelor of Science degree in accounting from Villanova University.

We believe Mr. Mahoney's qualifications to serve on our board include his extensive management, operational and financial experience in telecommunications and specifically in businesses similar to ours, his significant regulatory experience and expertise and his service as a director of another publicly-traded company.

*Michael K. Robinson*—Mr. Robinson has served as president and CEO since 2005, and as a director since 2009, of Broadview Networks, Inc. ("Broadview"). Broadview executed a pre-packaged Chapter 11 restructuring in the third quarter of 2012 and exited bankruptcy in November 2012. Mr. Robinson previously served as executive vice president and chief financial officer ("CFO") of US LEC (which is now part of Windstream Corporation) from 1998 to 2005. Prior to 1998, Mr. Robinson spent 10 years as an executive at Alcatel (now Alcatel-Lucent). Mr. Robinson also serves as a director of Lumos Networks Corp. (NASDAQ: LMOS). Mr. Robinson received a bachelor's degree in Business and Economics from Emory & Henry College and a Master of Business Administration degree from Wake Forest University.

We believe Mr. Robinson's prior experience in telecommunications, from an operational, strategic and financial perspective, adds significant perspective to the changing market for communication services.

*David L. Treadwell*—Mr. Treadwell has been a director of FairPoint since 2011 and serves on a number of other boards in various industries. Mr. Treadwell currently serves on the board of directors of two other publicly traded companies: Flagstar Bancorp, Inc. (NYSE: FBC) and Visteon Corporation (NYSE: VC). He also serves as chairman of the following privately held firms: Revere Industries, LLC, AGY, LLC, WinCorp LLC, U.S. Well Services LLC and Grow Michigan, LLC. Mr. Treadwell also serves on the board of directors of C&D Technologies, Inc. He previously served as president and CEO of EP Management Corporation, formerly known as EaglePicher Corporation, from 2006 through 2011. Mr. Treadwell was EaglePicher Corporation's chief operating officer from 2005 to 2006. Prior to that, he served as CEO of Oxford Automotive, Inc. in 2004 to 2005 through its restructuring. Mr. Treadwell received a Bachelor of Business Administration degree from the University of Michigan, Ann Arbor.

We believe Mr. Treadwell's qualifications to serve on our board include his strong operational and leadership skills and his previous experience outside of the telecommunications industry, as well as his previous experience as a turn-around agent for businesses seeking strategic alternatives.

*Wayne Wilson*—Mr. Wilson, a New Hampshire resident, has been an independent business advisor since 2002. From 1995 to 2002, Mr. Wilson served in various roles as president, chief operating officer and CFO of PC Connection, Inc., a Fortune 1000 direct marketer of information technology products and services. From 1986 to 1995, Mr. Wilson was a partner in the assurance and advisory services practice of Deloitte & Touche LLP. He previously served as a director of ARIAD Pharmaceuticals, Inc. (NASDAQ: ARIA), Edgewater Technology, Inc. (NASDAQ: EDGW), Hologic, Inc. (NASDAQ: HOLX) and Cytoc Corporation. Mr. Wilson received a Bachelor of Arts degree in political science from Duke University and a Master of Business Administration degree from the University of North Carolina at Chapel Hill. He is a certified public accountant in New Hampshire and North Carolina.

We believe Mr. Wilson's qualifications to serve on our board include his strong accounting and finance understanding gained from years as a certified public accountant in industry and with a major public accounting firm. This allows him to provide leadership to our audit committee. Mr. Wilson's qualifications also include his experience as a director on the boards of multiple publicly-traded companies. Mr. Wilson also fulfills the regulatory requirement that at least one member of our board reside in northern New England, as Mr. Wilson is a resident of New Hampshire.

## Executive Officers

The following table sets forth the names and positions of our current executive officers and their ages as of December 31, 2016.

Name	Age	Position
Paul H. Sunu	60	Director and Chief Executive Officer
Karen D. Turner	48	Executive Vice President and Chief Financial Officer
Bruce F. Metge	60	Executive Vice President and Chief Legal Officer
Peter G. Nixon	64	Executive Vice President, Revenue and External Affairs
John J. Lunny	53	Executive Vice President and Chief Technology Officer
Steven G. Rush	59	Executive Vice President, Northern New England Operations
John T. Hogshire	55	Senior Vice President and Controller

The following sets forth selected biographical information for our executive officers.

*Paul H. Sunu*—Mr. Sunu has served as our CEO since August 2010, prior to which he was CFO of Hargray Communications Group, Inc., a position he had held since 2008. Mr. Sunu was CFO of Hawaiian Telecom Communications, Inc. from 2007 to 2008 and a managing director and CFO of Madison River Communications Corp. from 1996 to 2007. He currently serves as the vice-chairman of the board of directors of Electric Lightwave Communications, Inc. and is a former board member of Madison River Communications Corp., Hawaiian Telecom Communications, Inc. and Centennial Communications Corp. He received a Bachelor of Arts degree in public administration from the University of Illinois and a J.D. from the University of Illinois College of Law.

We believe Mr. Sunu's role as our CEO makes him uniquely qualified to serve on our board, as he brings the day to day knowledge of our business to the board and shares his strategic vision with the board as it provides oversight and policy direction for the Company.

*Karen D. Turner*. In August 2016, Ms. Turner was appointed as our Executive Vice President and Chief Financial Officer. In this role, Ms. Turner oversees our financial, human resources and risk management functions. Ms. Turner was recently Executive Vice President, Operational Support from January 2016 until August 2016 and prior to that, was Senior Vice President, Strategy and Business Support from December 2014 until January 2016. Ms. Turner joined us in May 2014 as Vice President, Strategy and Business Support and served in that role until December 2014. Prior to joining FairPoint, Ms. Turner previously served as Vice President of Global Business Finance from 2011 to 2014 and Corporate Controller from 2008 to 2011 at INC Research, LLC. Ms. Turner has more than 20 years of experience in finance, accounting, operational support and administration.

*Bruce F. Metge*. In September 2016, Mr. Metge was appointed as our Executive Vice President and Chief Legal Officer. Mr. Metge brings to FairPoint more than 35 years of legal experience having served as General Counsel for several public and private companies and in private practice. He most recently served as General Counsel for Hillcrest Laboratories, Inc., a firm specializing in complex motion sensing software used throughout the world in television monitors, virtual reality and telecommunication devices. Prior to Hillcrest, Metge worked as General Counsel and Chief Compliance Officer for Catalyst Health Solutions, Inc., a publicly traded administrator of the prescription drug component of overall health benefit programs, and previous to that, he was a Partner at Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C. He has a bachelor's degree in Public Policy from Duke University and a J.D. from Northwestern University School of Law. He has bar memberships in the District of Columbia, Illinois and Massachusetts.

*Peter G. Nixon*. In January 2016, Mr. Nixon was appointed as our Executive Vice President, Revenue and External Affairs. Mr. Nixon is responsible for revenue, regulatory and governmental affairs activities. Previously, since July 2011, Mr. Nixon served as Executive Vice President, External Affairs and Operational Support. From July 2007 to July 2011 Mr. Nixon served as our President. Prior to July 2007, Mr. Nixon had served as our Chief Operating Officer since November 2002. Previously, Mr. Nixon was our Senior Vice President of Corporate Development from February 2002 to November 2002 and President of our Telecom Group from April 2001 to February 2002. Prior to this, Mr. Nixon served as President of our Eastern Region, Telecom Group from June 1999 to April 2001 and President of Chautauqua and Erie Telephone Corporation, which we refer to as C&E, from July 1997, when we acquired C&E, to June 1999. From April 1989 to June 1997, Mr. Nixon served as Executive Vice President of C&E. From April 1978 to March 1989, Mr. Nixon served as Vice President of Operations for C&E. Mr. Nixon served as the past chairman of the New York State Telecommunications Association from June 1996 to June 1998.

*John J. Lunny*. In August 2015, Mr. Lunny was appointed as our Executive Vice President and Chief Technology Officer. Mr. Lunny is responsible for voice and data network architecture, data center operations, IT, engineering and provisioning, as well as project management and product development. Mr. Lunny has 27 years of network operations, engineering and service delivery experience in the communications industry. He joined us in 2008 as director of sales engineering and was promoted to vice president



of network planning in 2009, Senior Vice President of Planning and Engineering in 2010 and Senior Vice President and Chief Technology Officer before moving into his current position in 2015. Prior to joining us, Mr. Lunny was senior director of service delivery at Comcast Business Services and before that he spent 13 years at Level 3 Communications, Inc. in operations, where he took on roles of increasing responsibility and became vice president of operations for the northeast region. Mr. Lunny also worked in sales engineering and operations at Reliance CommTec / Lorain Power. He began his career in Network Operations for AT&T.

*Steven G. Rush.* In August 2015, Mr. Rush was appointed as our Executive Vice President, Northern New England Operations. Mr. Rush is responsible for operational leadership of our northern New England properties. Mr. Rush was most recently Senior Vice President, Northern New England Operations and prior to December 2014 he was Senior Vice President, Customer Care and Network Assurance for us. Prior to joining us in 2007, Mr. Rush was Vice President of the Technical Network for INFONXX. Mr. Rush spent 26 years with AT&T in roles of increasing responsibility and tackled many challenges including mobilizing and coordinating restoral of the telecommunications network serving the New York Stock Exchange following the events of September 11, 2001. In his last role with AT&T, he was Vice President of Network Operations. He began his career as a Fire Control Technician in the U.S. Navy specializing in the Advanced Electronics and Electricity division.

*John T. Hogshire.* In April 2014, Mr. Hogshire was appointed as our Senior Vice President and Controller. Previously, Mr. Hogshire served as our Vice President and Controller from September 2010 to April 2014. Mr. Hogshire previously served as the Director of Accounting for Aviat Networks from July 2008 to September 2010, as a Consultant with Aviat Networks from January 2008 to July 2008 and as Vice President—Controller of Madison River Communications Corp. from December 1998 to July 2007.

#### **Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Securities Exchange Act of 1934 requires our officers and directors, and persons who own, or are part of a group that owns, more than 10% of a registered class of our equity securities, to file reports of ownership and changes in ownership with the SEC and NASDAQ. Officers, directors and beneficial owners of more than 10% of our common stock are required by regulation of the SEC to furnish us with copies of all Section 16(a) forms they file.

Based solely on our review of Forms 3, 4 and 5 and amendments thereto available to us and other information obtained from our directors, officers and beneficial owners of more than 10% of our common stock or otherwise available to us, we believe that no director, officer or beneficial owner of more than 10% of our common stock failed to file on a timely basis reports required pursuant to Section 16(a) of the Exchange Act for fiscal year 2016.

#### **Codes of Ethics**

##### *Code of Business Conduct and Ethics*

We have adopted a code of business conduct and ethics that applies to all of our employees, including our principal executive officer, principal financial officer and principal accounting officer. This code of business conduct and ethics is designed to comply with the SEC regulations and the NASDAQ listing standards related to codes of conduct and ethics and is posted on our corporate website at [www.fairpoint.com](http://www.fairpoint.com) on the "Investor Relations" page, under the "Corporate Governance" caption. A copy of our code of business conduct and ethics, which was updated in November 2015, is available free of charge upon request directed to our secretary at: Secretary, FairPoint Communications, Inc., 521 East Morehead Street, Suite 500, Charlotte, North Carolina 28202.

##### *Code of Ethics for Financial Professionals*

We have also adopted a code of ethics for financial professionals as required by the SEC under Section 406 of the Sarbanes—Oxley Act of 2002. This code sets forth written standards that are designed to deter wrongdoing and to promote honest and ethical conduct by our senior financial officers, including our CEO, and is a supplement to our code of business conduct and ethics. In addition to applying to our CEO, CFO, Chief Accounting Officer and Treasurer, this code applies to all of the other persons employed by us who have significant responsibility for preparing or overseeing the preparation of our financial statements and the other financial data included in our periodic reports filed with the SEC and in other public communications made by us that are designated from time to time by our CFO as senior financial professionals. Our code of ethics for financial professionals is posted on our corporate website at [www.fairpoint.com](http://www.fairpoint.com) on the "Investor Relations" page, under the "Corporate Governance" caption. A copy of our code of ethics for financial professionals is available free of charge upon request directed to our secretary at: Secretary, FairPoint Communications, Inc., 521 East Morehead Street, Suite 500, Charlotte, North Carolina 28202.

## Corporate Governance

### *Nomination of Directors*

There have been no material changes to the procedures by which shareholders may recommend nominees to our board of directors.

### *Audit Committee*

Our board of directors has a separately designated standing audit committee. Our audit committee members are: Wayne Wilson (chair), Peter D. Aquino, Dennis J. Austin and Michael K. Robinson. Messrs. Wilson and Robinson are qualified as audit committee financial experts within the meaning of item 407(d)(5)(ii) of Regulation S-K under the Securities Exchange Act of 1934 (the "Exchange Act") and our board of directors has determined that they have the requisite accounting and related financial management expertise within the meaning of the listing standards of the NASDAQ. Messrs. Wilson and Robinson satisfy the independence criteria and each have the qualifications set forth in the listing standards of the NASDAQ and the applicable provisions of the Exchange Act. The SEC has determined that the audit committee financial expert designation does not impose on any person with that designation any duties, obligations or liability that are greater than the duties, obligations or liability imposed on such person as a member of the audit committee of the board of directors in the absence of such designation.

## ITEM 11. EXECUTIVE COMPENSATION

Our executive compensation is presented in the following sections:

- Compensation Discussion and Analysis
- 2016 Summary Compensation Table
- Grants of Plan-Based Awards for 2016
- Outstanding Equity Awards at December 31, 2016
- Option Exercises and Stock Vested for 2016
- Potential Payments Upon Termination or Change in Control
- Director Compensation
- Compensation Committee Interlocks and Insider Participation
- Compensation Committee Report

### Compensation Discussion and Analysis

#### General Principles and Procedures

##### *Executive Summary*

Our executive compensation program is designed to attract, motivate and retain top executives and managerial talent and to reward our executives and managers for delivering results that will build sustainable growth and value for our shareholders over the long-term. We believe our compensation program aligns the interests of our executives with those of our shareholders by tying short- and long-term incentive compensation directly to the Company's achievement of short- and long-term performance goals. In determining certain aspects of executive compensation for fiscal year 2016, the compensation committee considered the sustained, overwhelming shareholder support our "say-on-pay" advisory votes have received since 2012 and the continued alignment of executive compensation with shareholder interests.

The Company's named executive officers ("NEOs") included in the tables that follow this Compensation Discussion and Analysis for 2016 are:

- Paul H. Sunu, Director and Chief Executive Officer
- Karen D. Turner, Executive Vice President and Chief Financial Officer (Ms. Turner was appointed to this position effective August 3, 2016)
- Ajay Sabherwal, former Executive Vice President and Chief Financial Officer (Mr. Sabherwal resigned effective August 3, 2016)
- Peter G. Nixon, Executive Vice President, Revenue and External Affairs

- John J. Lunny, Executive Vice President and Chief Technology Officer

- Steven G. Rush, Executive Vice President, Northern New England Operations
- Anthony A. Tomae, former Executive Vice President and Chief Revenue Officer (Mr. Tomae's employment was terminated without cause effective January 29, 2016)

### *2016 Executive Compensation Highlights*

The key compensation decisions and factors affecting the compensation of our NEOs for 2016 were as follows:

- Base salary increases, which are further described on page 106.
- Performance-based annual bonuses earned during 2016 and will be paid in 2017 based on achievement of corporate and individual performance goals as described on pages 107-108.
- Equity awards with grant date values between 88% and 179% of base salary as described on pages 108-109.

### *2016 Performance Highlights*

The direct alignment of our compensation program with Company performance helped produce the following 2016 business highlights:

- (1) *Enhanced Operational Performance.* We continue to focus on delivering exceptional customer service while at the same time, cultivating, improving and enhancing our people and processes. Our trouble loads have continued to decline and mean time to repair has improved as we continue to implement improvements in our operations.
- (2) *Delivered Solid Financial Performance.* For 2016, we achieved our financial guidance and ended the year with what we believe is a strong cash position through diligent and effective cost management.
- (3) *Enhanced Network.* We have strategically invested in our network to extend service availability and improve offered broadband speeds. We are on track to meet the requirements under the CAF Phase II Program. Additionally, we continue to expand our network through "edge out" strategies including purchase and construction of unique fiber extensions during 2016.
- (4) *Continued Transformation of Revenue Mix.* We lowered our revenue losses during 2016 and increased growth revenues to 31% of total revenue. We continued our focus on advanced services, while developing new products and capabilities to serve more effectively small and medium sized businesses which are an important element of many of our markets. We accelerated our product development pipeline through the acquisition of a Maine based value added reseller of unified communications, data networking and cabling infrastructure solutions. Additionally, with more than 22,000 miles of fiber, we experienced an 8% increase in Ethernet circuits in 2016 compared to 2015.
- (5) *Exploration of Strategic Alternatives.* On December 3, 2016, FairPoint Communications entered into the Merger Agreement with Consolidated. The combined company will have enhanced scale, including presence in 24 states and ownership of over 35,000 miles of fiber. The Merger is expected to close around the middle of 2017. Additional details, including reasons for the Merger and conditions to close, as well as compensation that may be payable to our executive officers in connection with the Merger, are disclosed in our definitive proxy statement filed with the SEC on February 27, 2017.

### *Compensation Philosophy and Objectives*

Our overriding objective is to achieve and sustain significant increases in shareholder value. Our executive compensation program has been designed to support this objective with a clear link between pay and corporate and individual performance while discouraging executives from taking excessive risks. We structure our compensation plans to provide target compensation levels and opportunities that are competitive with the median target opportunities for comparable positions among the companies in our peer group. This approach is also aimed at ensuring our ability to attract, retain and motivate the executives, managers and professionals who are critical to our short- and long-term success. A significant portion of our executives' compensation is "performance-based" in the form of both short- and long-term incentives that are intended to motivate balanced decision making by our executives while also aligning their interests with those of our shareholders.

### *Shareholder Engagement*

Our board encourages shareholder feedback and believes that fostering relationships with shareholders is an important objective. Our engagement team, which is comprised of senior leaders and members of the board, interacts with shareholders on a regular basis through face-to-face meetings, participation in industry conferences, phone calls and email.



Since our last annual meeting, our engagement team has conducted face-to-face meetings with shareholders that, combined, represented in excess of 50% of our outstanding common stock. These forums allow for an open dialogue on our financial performance, community involvement, governance practices, compensation programs and industry trends. Feedback received from shareholders is routinely shared with the chair of the board.

At our 2016 annual meeting, we received strong support of our executive compensation programs, with the "say-on-pay" proposal receiving votes in favor of approximately 99% of those cast. We will continue to engage with shareholders on executive compensation and other pertinent matters.

#### *Governance and Oversight of our Executive Compensation Program*

Our executive compensation program is governed and administered by the compensation committee of the board of directors. The compensation committee is comprised of independent, non-employee members of the board.

The compensation committee's overall responsibilities include approving our compensation philosophy, policies and plans; reviewing and approving corporate goals and objectives relevant to the compensation for our CEO and other executive officers; evaluating the CEO's performance in light of these goals; setting the compensation of our CEO; and after considering the recommendation of our CEO, approving the compensation of our other executives, including the other NEOs. Our CEO does not participate in discussions or decision-making regarding his own compensation but does make recommendations to the compensation committee regarding the compensation of the other NEOs as well as other senior executives. However, the ultimate decisions are made by the compensation committee. The compensation committee also has oversight responsibility for our management development and succession planning efforts.

The compensation committee retains an independent executive compensation consulting firm, Lyons, Benenson & Company Inc. ("LB&Co."), to assist and advise the compensation committee on all aspects of our executive compensation program. LB&Co. provides no other services to us. The services of LB&Co. include:

- Advising on the compensation philosophy and the compensation committee charter;
- Assessing risk in connection with compensation programs;
- Developing and analyzing the appropriateness of our peer group;
- Providing and analyzing competitive market compensation data;
- Analyzing the effectiveness of our executive compensation plans and making recommendations, as appropriate;
- Assisting in the design of employment and severance agreements, as applicable;
- Evaluating how well our compensation program adheres to our stated objectives and philosophy; and
- Providing data, advice and counsel on director compensation.

Harvey Benenson, the Managing Director of LB&Co., generally attends all meetings of the compensation committee. Certain of our directors, including Mr. Sunu, serve or have served on the boards of other companies, including their compensation committees, for which LB&Co. has provided or provides compensation consulting services. The compensation committee assessed the independence of LB&Co. pursuant to SEC rules and concluded that no conflict of interest exists that prevents LB&Co. from providing independent consulting services to the compensation committee.

#### *Peer Group*

The compensation committee uses executive compensation data from a peer group of companies to assist the compensation committee with analyzing the effectiveness and competitiveness of our executive compensation program. The peer group is designed to reflect the current competitive environment for our products, services and executive talent, as well as the competitive environment we expect to face in the future. In structuring the peer group, we focused on companies of comparable scope with notable performance accomplishments. Using data from the public filings of a large number of companies, we narrowed the peer group to 12 companies by applying the following selection criteria:

- Relevant industry classification (based on our global industry classification standard), business description and services provided;
- With some exceptions based on industry relevance, comparable size, with revenues between \$400 million and \$5.77 billion; and
- Levels of achievement in certain performance metrics, such as three-year revenue growth, three-year earnings before interest, taxes, depreciation and amortization ("EBITDA") growth and three-year free cash flow growth.



The companies included in the peer group in 2015 were: Akamai Technologies, Inc.; AOL Inc.; Cablevision Systems Corporation; Charter Communications, Inc.; Cincinnati Bell Inc.; Consolidated Communications Holdings, Inc.; EarthLink Holdings Corp.; Frontier Communications Corporation; Hawaiian Telcom Holdco, Inc.; j2 Global, Inc.; Level 3 Communications, Inc.; Premiere Global Services, Inc.; SBA Communications Corporation; Vonage Holdings Corp. and Windstream Corporation.

The following companies were removed from our peer group in 2016:

Company Name	Reason for Removal
AOL Inc.	No longer publicly traded
Cablevision Systems Corporation	Above revenue range
Charter Communications, Inc.	Above revenue range
Level 3 Communications, Inc.	Above revenue range
Premiere Global Services, Inc.	No longer publicly traded

General Communication, Inc. and Cogent Communications Holdings, Inc. were added to our peer group in 2016 using the selection criteria described above.

As a result of these changes, the companies included in the peer group in 2016 were: Akamai Technologies, Inc.; Cincinnati Bell Inc.; Cogent Communications Holdings, Inc.; Consolidated Communications Holdings, Inc.; EarthLink Holdings Corp.; Frontier Communications Corporation; General Communication, Inc.; Hawaiian Telcom Holdco, Inc.; j2 Global, Inc.; SBA Communications Corporation; Vonage Holdings Corp. and Windstream Corporation.

The compensation committee believes this peer group is both reflective of where we are positioned currently as well as where we aspire to be in the future. The compensation committee recognizes that certain of the companies included in the peer group are considerably larger than us. These companies have been included because of their relevance to the industry and their offerings and because we draw from the same talent pool for employees. The compensation committee is mindful of differences in size and scope when using peer group data.

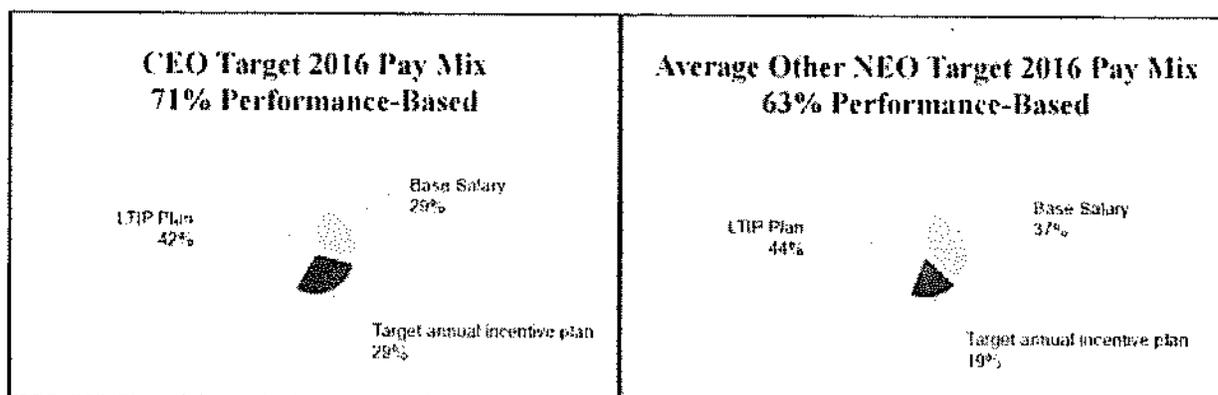
#### Specific Principles for Determining Executive Compensation

##### *Assessing the Competitiveness of Our Compensation Program*

The compensation committee benchmarks executive compensation levels annually. We strive to ensure that the target total compensation opportunity for each of our executives is competitive relative to comparable positions with the peer group companies. Specifically, base salaries, annual incentives and equity based incentives are all targeted at the peer group median. Both our annual and long-term incentives are structured, however, to deliver actual total compensation that may exceed the market median when the underlying performance upon which those incentives are based exceeds median performance.

##### *Total Compensation Mix*

As reflected in the following charts, a significant portion, 71% and 63%, respectively, of our CEO's and the average of other NEOs' target total compensation opportunity was performance-based using 2016 annual base salary, 2016 target annual incentive plan and 2016 LTIP Plan (as defined hereinafter) grants as illustrated below.



### Paying for Performance

We are committed to the principle of paying for performance. Our compensation program is designed such that a significant portion of the total compensation opportunity of our executives is based on achievement of financial measures as illustrated below. For the 2016 annual incentive payout, actual achievement of \$265.1 million for Pre-Bonus Adjusted EBITDA (as defined hereinafter), or 116.9% of target, resulted in payout at 38.0% for that measure compared to a target payout of 32.5%. The actual achievement of \$42.1 million for Pre-Bonus Free Cash Flow (as defined hereinafter), or 125.0% of target, resulted in payout at 40.6% for that measure compared to a target payout of 32.5%.

2016 Pre-Bonus Adjusted EBITDA (in millions)				2016 Pre-Bonus Free Cash Flow (in millions)			
		\$265.1				\$42.1	
\$246.3	\$260.4		\$274.5	\$22.5	\$35.1		\$49.1
Threshold	Target	Actual	Maximum	Threshold	Target	Actual	Maximum

The table below identifies and explains the reason for each component and the method for determining amounts earned under our executive compensation program.

Element	Reason and Method for Element
Base Salary	Base salary represents "fair" pay for the performance of duties and responsibilities. The compensation committee determines the level of base salary based on compensation benchmarking, the different levels of responsibility that exist within the Company, each executive's level of experience within the communications industry and individual performance at the Company.
Annual Incentives	Under the annual incentive plan, executives may earn annual cash incentives based on short-term corporate and individual performance. The incentive opportunity motivates executives to achieve the performance objectives and goals that are consistent with our plans and budgets and that strengthen our ability to compete effectively.
Long Term Incentives/Equity Awards	The FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan (the "LTIP Plan") effective May 12, 2014 allows executives to receive stock-based awards that link the executives' interests with those of our shareholders. The value of the awards is based on the Company's performance over multi-year periods to retain and motivate key executives and encourage them to operate the Company's business with a view towards creating long-term shareholder value.
Retirement and Welfare Benefits	We maintain a 401(k) retirement savings plan. In 2016, this plan included an employer matching contribution up to an amount equal to 5% of each participant's compensation. Additionally, we provide, on equal terms for all employees, group term life insurance, group health insurance and short- and long-term disability insurance.
Post-employment, Severance and Change-in-Control Benefits	We provide severance benefits to certain NEOs at levels that we consider conservative yet competitive when compared to those offered by our peers. We believe that such benefits are necessary and appropriate in order to attract and retain qualified NEOs.  The severance benefits for these executives are generally paid if the executives are terminated without cause or they resign with good reason. In addition to cash severance payments that would be due upon a qualifying termination, each terminated executive is entitled to continued welfare benefits for a limited period after termination.

### Share Ownership Guidelines

Our executive officers are subject to share ownership guidelines to better align their interests with those of our shareholders by requiring the executives to acquire and maintain meaningful equity positions in the Company. Under the guidelines, each executive officer is required to own shares of our common stock with a value equal to a multiple of the executive officer's base salary as indicated in the table below. Executive officers are required to meet these guidelines within the later of five years of the date of adoption of these guidelines (by June 4, 2018) or of such individual becoming subject to them.

Position	Base Salary Multiple
Chief Executive Officer	4.00X
Executive Vice Presidents	2.25X

For executive officers, the failure to timely meet or, in certain circumstances, to show sustained progress toward timely meeting the goals set forth in the share ownership guidelines could result in a reduction of future equity grants and/or payment of future annual and/or cash incentive payouts in the form of equity, at the discretion of the compensation committee.

### No Hedging/No Pledging Provisions

Our insider trading policy prohibits the executive officers from using any strategies or products (such as derivative securities or short-selling techniques) to hedge against potential changes in the value of our common stock, prohibits the holding of our securities in a margin account and prohibits any executive officer from pledging our securities as collateral for a loan.

### Incentive Recoupment Policy

The compensation committee has adopted a clawback policy that requires an executive officer to repay us a compensation payment or award previously made to the officer if the following conditions are met:

- (1) the payment was predicated upon achieving certain financial results that were required to be reported under the securities laws that were subsequently the subject of a restatement of our financial statements filed with the SEC due to our material noncompliance with any financial reporting requirement under the securities laws;
- (2) the compensation committee determines the officer engaged in fraud and/or intentional misconduct that caused or substantially caused the need for the restatement; and
- (3) a lower payment would have been made to the officer based upon the restated financial results.

### Executive Compensation Decisions for 2016

#### Base Salary

The table below shows the annual base salary rate increases from 2015 to 2016 for each NEO:

Executive <sup>(1)</sup>	Annual Base Salary Rate <sup>(2)</sup>		% of Base Salary Increase
	2016	2015	
Mr. Sunu	\$830,000	\$830,000	—%
Ms. Turner	\$375,000	\$263,000	43%
Mr. Nixon	\$353,000	\$342,000	3%
Mr. Lunny	\$300,000	\$288,300	4%
Mr. Rush	\$285,000	\$273,000	4%

- (1) Mr. Tomae's employment was terminated without cause effective January 29, 2016 and Mr. Sabherwal resigned his employment effective August 3, 2016.
- (2) The annual base salary rate for 2016 was effective on July 1, 2016 with the exception of Ms. Turner, which was effective August 3, 2016 upon her appointment to Chief Financial Officer. Base salary reflected in the *Realized Compensation* table and the *Summary Compensation* table is based on the respective NEO's compensation reported on IRS Form W-2.



### Annual Incentive Compensation Awards

NEOs earn annual incentive compensation based on the achievement of financial and non-financial goals established by the compensation committee each year. For 2016, the financial goals were measured by the Company's Pre-Bonus Consolidated EBITDA and Pre-Bonus Free Cash Flow and the non-financial goals included seven service quality measures. In setting the 2016 financial goals, the compensation committee considered the industry-wide trends that are negatively impacting revenue (primarily for voice-related products). The target goals for 2016 were set based on the expected business plan with stretch goals added to achieve maximum payout.

The compensation committee believes achievement of these goals is critically important to the Company's business and strategy and will increase the value of the Company.

The compensation committee adopted the following challenging financial targets for the 2016 annual incentive compensation awards (\$ in millions):

	Weight	Performance Measures	Threshold (25% payout)	Target (100% payout)	Maximum (150% payout)	2016 Actual Results	2016 Results Relative to Target
Financial Measures	32.5%	Pre-Bonus Consolidated EBITDA <sup>(1)</sup>	\$ 246.3	\$ 260.4	\$ 274.5	\$ 265.1	116.9% of target
	32.5%	Pre-Bonus Free Cash Flow <sup>(1)</sup>	\$ 22.5	\$ 35.1	\$ 49.1	\$ 42.1	125.0% of target

- (1) Pre-Bonus Consolidated EBITDA and Pre-Bonus Free Cash Flow are non-GAAP financial measures used by management to measure operational and financial performance. For purposes of calculating Pre-Bonus Consolidated EBITDA, the Company adjusts net income/(loss) for interest, income taxes, depreciation and amortization, in addition to: a) the add-back of aggregate pension and other post-employment benefits ("OPEB") expense, b) the add-back (or subtraction) of the adjustment to the compensated absences accrual to eliminate the impact of changes in the accrual, c) the add-back of costs related to the reorganization, including professional fees for advisors and consultants, d) other adjustments, such as the add-back of costs and expenses, including those imposed by regulatory authorities, with respect to casualty events, acts of God or force majeure to the extent they are not reimbursed from proceeds of insurance; other non-cash items, except to the extent they will require a cash payment in a future period, including impairment charges; and other items, including facility and office closures, expenses related to permitted transactions, labor negotiation related expenses (including losses related to disruption of operations), non-cash gains/losses, non-operating dividend and interest income and other extraordinary gains/losses and e) the add-back of any bonus expense to the extent any bonuses were earned. Pre-Bonus Free Cash Flow adjusts Pre-Bonus Consolidated EBITDA for pension contributions, OPEB payments and capital expenditures.

In addition, 5% and 30% of each officer's 2016 annual incentive award was based on the officer's achieving specified service quality targets and individual or departmental goals or milestones related to the officer's areas of responsibility, respectively. The specified service quality targets included: call center abandonment rate, installation appointments not met for Company reasons, mean time to repair service affecting abnormal events, whole performance credits and productivity and quality metrics. The goals or milestones include certain financial and human resources milestones, revenue and sales force development milestones, technology milestones and operational improvement milestones. In order for any bonuses to be paid for 2016, the Company had to achieve threshold performance under both of the financial objectives (Pre-Bonus Consolidated EBITDA and Pre-Bonus Free Cash Flow) set by the compensation committee.

The table below shows the 2016 target bonus opportunity percentages, performance goals and weightings for our NEOs:

Executive	Bonus Target (% of 2016 Annual Base Salary)	Performance Criteria
Mr. Sunu	100%	(i) 32.5%—Pre-Bonus Consolidated EBITDA; (ii) 32.5%—Pre-Bonus Free Cash Flow; (iii) 5%—the Company achieving specified service quality measures and (iv) 30%—the Company meeting certain objectives set by the board of directors.
Messrs. Nixon, Lunny and Rush and Ms. Turner	50%	(i) 32.5%—Pre-Bonus Consolidated EBITDA; (ii) 32.5%—Pre-Bonus Free Cash Flow; (iii) 5%—the Company achieving specified service quality measures and (iv) 30%—the executive officer achieving certain individual or departmental goals or milestones.
Messrs. Sabherwal and Tomae*	N/A	N/A

\*Mr. Tomae's employment was terminated without cause effective January 29, 2016 and Mr. Sabherwal resigned his employment effective August 3, 2016.

The following table shows the 2016 annual incentive earned by the NEOs based on the financial and service quality results achieved, the relative weighting of each corporate performance objective (as shown above) and each NEO's individual performance rating:

Executive	Performance Achievement			Annual Incentive Payout	
	Financial Measures	Service Quality Measures	Individual Goals	\$	As a % of Target
Mr. Sunu	78.62%	4.95%	30.00%	960,800	113.57%
Ms. Turner	78.62%	4.95%	30.00%	179,100	113.57%
Mr. Nixon	78.62%	4.95%	30.00%	201,100	113.57%
Mr. Lunny	78.62%	4.95%	30.00%	167,100	113.57%
Mr. Rush	78.62%	4.95%	30.00%	161,400	113.57%
Messrs. Sabherwal and Tomae*	N/A	N/A	N/A	N/A	N/A

\*Mr. Tomae's employment was terminated without cause effective January 29, 2016 and Mr. Sabherwal resigned his employment effective August 3, 2016.

#### 2016 Equity Compensation Awards

The compensation committee awards long-term, equity based awards to executives to reward the NEOs for their performance and to retain and motivate them and encourage them to create long-term shareholder value. The compensation committee approved the following equity compensation awards to our NEOs:

Executive <sup>(1)</sup>	Number of Shares of Restricted Stock	Number of Stock Options	Number of Performance Shares	Grant Date Value (\$)	Grant Date Value (% of Base Salary)
Mr. Sunu	31,000	54,000	27,000	\$1,216,221	147%
Ms. Turner	22,000	37,000	6,000	\$671,251	179%
Mr. Sabherwal	11,000	19,000	9,000	\$423,356	101%
Mr. Nixon	9,000	16,000	8,000	\$357,625	101%
Mr. Lunny	6,000	13,000	6,000	\$265,229	88%
Mr. Rush	6,000	13,000	6,000	\$265,229	93%
Mr. Tomae	N/A	N/A	N/A	N/A	N/A

(1) The grant date for these awards was January 22, 2016, except the following grants awarded on August 15, 2016 to Ms. Turner upon her appointment to Chief Financial Officer: 15,000 shares of restricted stock and 25,000 stock options. Mr. Tomae's employment was terminated without cause effective January 29, 2016.

The amount of equity awards for 2016 were determined by the compensation committee in its discretion, taking into account the CEO's recommendations other than with respect to the amounts awarded to the CEO. The equity grant included a mix of stock options, restricted stock and performance shares. The options and restricted stock granted on January 22, 2016 are time-vested,

with 25% vesting on the grant date and the remainder vesting in three equal annual installments, commencing on the first anniversary date of the grant. The options and restricted stock granted on August 15, 2016 to Ms. Turner are time-vested, vesting in three equal annual installments, commencing on the first anniversary date of the grant. The performance shares will be earned, at the end of a three-year performance period, based upon (i) the Company's achievement of a growth revenue performance goal and (ii) the total shareholder return to our shareholders compared to the total shareholder return achieved by the companies in a telecommunications industry group. One share of our common stock will be distributed to the participant for each whole performance share earned by the participant.

#### Employment Agreements

##### *Paul H. Sunu*

On April 9, 2013, the Company entered into an amended and restated employment agreement with Mr. Sunu, as amended on August 14, 2015 (the "Sunu Employment Agreement"). Mr. Sunu's term of employment is through August 31, 2017, unless terminated sooner or renewed as provided in the Sunu Employment Agreement. In addition, under the Sunu Employment Agreement, Mr. Sunu is nominated annually to the board of directors of the Company (and has served and will so serve, if elected).

Mr. Sunu is eligible to participate in the benefits programs generally available to the Company's other senior executives, including the LTIP Plan, as determined at the discretion of the compensation committee of the board of directors and subject to the terms of such plan. In any year that the compensation committee determines to make a grant or grants under the LTIP Plan, the grant date value of any award to Mr. Sunu is anticipated to be no less than 1.5 times the annual base salary payable to him in effect at such time. Under the Sunu Employment Agreement, Mr. Sunu is eligible to participate in the Company's annual incentive plan and earn a performance-based bonus thereunder for annual performance periods. Mr. Sunu's target level bonus under the annual incentive plan is 100% of the base salary payable to him during the applicable performance period and Mr. Sunu is eligible for a maximum bonus under such plan of up to 150% of his base salary.

Under the Sunu Employment Agreement, either party may terminate Mr. Sunu's employment at any time. Information about his potential severance pay and benefits appears under "*Potential Payments Upon Termination or Change in Control*."

##### *Karen D. Turner, Ajay Sabherwal, Peter G. Nixon, John J. Lunny and Steven G. Rush*

The Company entered into employment agreements with Ms. Turner (on November 20, 2014, as amended on August 14, 2015 and November 21, 2016); Mr. Sabherwal (on January 22, 2013, as amended on August 14, 2015 and May 16, 2016); Mr. Nixon (on January 22, 2013, as amended on August 14, 2015 and May 16, 2016); Mr. Lunny (on July 1, 2014, as amended on August 14, 2015 and November 21, 2016) and Mr. Rush (on August 10, 2015, as amended on June 1, 2016).

Pursuant to the respective employment agreements, each current executive will serve in their respective positions (with such title subject to change from time to time as determined by the board of directors) with the Company through December 31, 2019, subject to earlier termination or extension as set forth in the employment agreements with the exception of Mr. Rush, whose employment with the Company is through August 10, 2018. Following such period of employment (or the applicable extension term, if any), the current executive will continue on an at will basis until such time as the Company provides a written notice of termination in accordance with the terms of his or her employment agreement.

The current executives are eligible to participate in the annual incentive plan and are eligible to earn a performance-based bonus thereunder. The current executives are also eligible to participate in the benefits programs and other plans made available generally to the Company's other senior executives, including but not limited to the LTIP Plan.

Information about the potential severance pay and benefits associated with these employment agreements appears under "*Potential Payments Upon Termination or Change in Control*" herein with the exception of Mr. Sabherwal. Mr. Sabherwal resigned his employment effective August 3, 2016.

##### *Anthony A. Tomae*

The Company entered into an employment agreement with Mr. Tomae on November 15, 2012. Mr. Tomae's employment agreement set forth the terms and conditions of his employment as Executive Vice President and Chief Revenue Officer of the Company for a three-year term ending on November 15, 2015, subject to extension as set forth in his employment agreement. On August 14, 2015, the Company amended Mr. Tomae's employment agreement, which extended the term of the agreement through December 31, 2016. Following the term of employment (or the applicable extension term, if any), Mr. Tomae was to have remained employed on an at-will basis until such time as the Company provided a written notice of termination in accordance with the terms of his employment agreement.

Mr. Tomae's employment with the Company terminated without cause effective January 29, 2016. Further information about his severance pay and benefits appear "*Potential Payments Upon Termination or Change in Control*" herein.

### *Tax Considerations*

Section 162(m) of the Code generally disallows a tax deduction to public corporations for taxable compensation, other than performance-based compensation, over \$1.0 million paid for any fiscal year to any of the Company's NEOs (excluding the Chief Financial Officer) as of the end of any fiscal year. The Company's policy is to qualify its executive program and plans for deductibility under Section 162(m) to the extent the compensation committee determines such action to be appropriate.

While the compensation committee's general policy is to preserve the deductibility of compensation paid to the NEOs, the compensation committee nevertheless authorizes payments that might not be deductible if it believes that they are in the best interests of the Company and its shareholders.

### Realized Compensation

The SEC's calculation of total compensation, as shown in the *Summary Compensation* table, includes several items that are driven by accounting assumptions. In some cases, the actual compensation realized by the NEOs may be very different than what is reported in the *Summary Compensation* table and compensation reported may not be realized for many years, if at all. Furthermore, realized compensation for a NEO for any given year may be greater or less than the compensation reported in the *Summary Compensation* table for that year depending on fluctuations in stock prices on the grant and vesting dates, differences in equity grant values from year to year and SEC reporting requirements, as described below.

The primary difference between the table below (the "*Realized Compensation* table") and the *Summary Compensation* table is the method used to value restricted stock awards, stock options and performance shares. SEC rules require that the entire grant date fair value of all restricted stock awards (calculated as the fair market value of the common stock on the date of grant), stock options (estimated using the Black-Scholes option pricing model, as outlined in footnote (1) of the *Summary Compensation* table) and performance shares (calculated as the fair market value of the common stock on the date of grant based upon the probable outcome of performance conditions) be reported in the *Summary Compensation* table during the year in which they were granted. As a result, a significant portion of the total compensation amounts reported in the *Summary Compensation* table relates to restricted stock awards and performance shares that have not vested and stock options that have not been exercised during the year. In contrast, the *Realized Compensation* table below includes only the value of restricted stock awards that vested (calculated as the fair market value of the common stock on the date of vesting) and stock options that were exercised (calculated as the difference between the exercise price and the market value of the common stock on the date of exercise) during the applicable fiscal year. In addition, the *Realized Compensation* table below does not include any items from the "All Other Compensation" column of the *Summary Compensation* table, which include (1) matching contributions made by the Company to its 401(k) retirement savings plan, (2) contributions made by the Company to the term life insurance plan it sponsors and (3) relocation expense reimbursement, since in each case for subsections (1), (2) and (3) there is no cash compensation received by the NEO for these benefits, as well as (4) severance expenses, because this is not compensation received during the course of employment with the Company.

The *Realized Compensation* table below supplements the *Summary Compensation* table and shows compensation actually realized by each NEO in 2016, 2015 and 2014, as described above.

Executive	Year	Salary <sup>(1)</sup> \$	Bonus <sup>(1)</sup> \$	Non-Equity Incentive Plan Compensation <sup>(2)</sup> \$	Stock Awards <sup>(3)</sup> \$	Option Awards <sup>(4)</sup> \$	Total \$
Mr. Sunu	2016	845,962	—	960,800	609,675	—	2,416,437
	2015	830,000	500,000	893,100	504,510	—	2,727,610
	2014	815,000	—	407,500	706,320	—	1,928,820
Ms. Turner <sup>(5)</sup>	2016	315,442	—	179,100	74,394	—	568,936
	2015	263,000	—	141,500	54,732	—	459,232
	2014	146,154	—	36,600	—	—	182,754
Mr. Sabherwal <sup>(6)</sup>	2016	267,312	—	—	208,768	392,014	868,094
	2015	408,000	—	219,500	171,308	—	798,808
	2014	401,600	—	100,400	215,940	—	717,940
Mr. Nixon	2016	354,119	—	201,100	181,425	—	736,644
	2015	342,000	—	184,000	150,977	—	676,977
	2014	336,400	—	84,100	178,692	—	599,192
Mr. Lunny	2016	294,202	—	167,100	103,460	—	564,762
	2015	283,060	—	146,600	82,830	170,938	683,428
	2014	261,580	—	65,400	55,835	—	382,815
Mr. Rush	2016	284,296	—	161,400	51,730	—	497,426
	2015	266,846	—	143,600	30,120	—	440,566
	2014	243,797	8,000	61,000	12,350	—	325,147
Mr. Tomae <sup>(7)</sup>	2016	46,579	—	—	150,387	464,640	661,606
	2015	343,000	—	184,500	334,856	—	862,356
	2014	337,200	—	84,300	222,455	—	643,955

(1) Base salary and bonus as reported on the respective NEO's W-2 and as presented in the *Summary Compensation* table.

(2) For 2016, represents the performance-based compensation under the annual incentive plan earned during 2016 and will be paid in 2017, as presented in the *Summary Compensation* table.

(3) The value of restricted stock that vested during the year, as reported on the respective NEO's W-2 and as presented in the table "*Option Exercises and Stock Vested for 2016*" herein (the "*Option Exercises and Stock Vested for 2016*" table").

(4) The value of stock options exercised during the year, as reported on the respective NEO's W-2 and as presented in the *Option Exercises and Stock Vested for 2016* table.

(5) Ms. Turner began employment with the Company on April 7, 2014 and she was appointed as Chief Financial Officer effective August 3, 2016.

(6) Mr. Sabherwal resigned his employment effective August 3, 2016.

(7) Mr. Tomae's employment was terminated without cause effective January 29, 2016.

## 2016 Summary Compensation Table

The table below summarizes the total compensation paid or earned by each of the NEOs for the fiscal years ended December 31, 2016, 2015 and 2014.

Name and Principal Position	Year	Salary \$	Bonus \$	Stock Awards <sup>(1)</sup> \$	Option Awards <sup>(1)</sup> \$	Non-Equity Incentive Plan Compensation <sup>(2)</sup> \$	All Other Compensation <sup>(3)</sup> \$	Total \$
Paul H. Sunu <sup>(4)</sup> Director and Chief Executive Officer	2016	845,962	—	779,048	437,173	960,800	15,722	3,038,705
	2015	830,000	500,000	905,704	569,160	893,100	15,722	3,713,686
	2014	815,000	—	738,080	583,075	407,500	15,664	2,559,319
Karen D. Turner <sup>(5)</sup> Executive Vice President and Chief Financial Officer	2016	315,442	—	385,364	285,887	179,100	14,227	1,180,020
	2015	263,000	—	197,424	128,718	141,500	13,868	744,510
	2014	146,154	—	55,320	42,810	36,600	6,256	287,140
Ajay Sabherwal <sup>(6)</sup> Former Executive Vice President and Chief Financial Officer	2016	267,312	—	269,536	153,820	—	14,181	704,849
	2015	408,000	—	318,726	199,644	219,500	14,763	1,160,633
	2014	401,600	—	263,600	198,931	100,400	14,578	979,109
Peter G. Nixon Executive Vice President, Revenue and External Affairs	2016	354,119	—	228,092	129,533	201,100	14,518	927,362
	2015	342,000	—	290,842	166,370	184,000	14,518	997,730
	2014	336,400	—	218,788	167,239	84,100	14,323	820,850
John J. Lunny Executive Vice President and Chief Technology Officer	2016	294,202	—	159,984	105,245	167,100	13,050	739,581
	2015	283,060	—	218,896	135,723	146,600	14,215	798,494
	2014	261,580	—	171,340	131,706	65,400	11,935	641,961
Steven G. Rush <sup>(7)</sup> Executive Vice President, Northern New England Operations	2016	284,296	—	159,984	105,245	161,400	34,122	745,047
	2015	266,846	—	197,424	128,718	143,600	60,175	796,763
	2014	243,797	8,000	—	150,913	61,000	46,384	510,094
Anthony A. Tonnae <sup>(8)</sup> Former Executive Vice President and Chief Revenue Officer	2016	46,579	—	—	—	—	1,005,394	1,051,973
	2015	343,000	—	272,382	166,370	184,500	14,522	980,774
	2014	337,200	—	263,600	198,931	84,300	14,323	898,354

- (1) The amounts shown are the grant date fair value of the stock and option awards, adjusted to eliminate the effect of any forfeiture assumption in calculating stock compensation, computed in accordance with the Compensation—Stock Compensation Topic of the Accounting Standards Codification ("ASC"). In the case of performance shares, the grant date fair value is based upon the probable outcome of the performance conditions.

The grant date fair value per share of the restricted stock awards was calculated as the fair market value per share of the common stock on the date of grant.

The performance shares are based upon (i) the Company's achievement of a growth revenue performance goal (non-market portion) and (ii) the total shareholder return to our shareholders compared to the total shareholder return achieved by the companies in a telecommunications industry group (market portion). The grant date fair value of the non-market portion of the performance shares was calculated as the fair market value per share of the common stock on the date of grant. For purposes of determining compensation expense for the market portion of the performance shares, the grant date fair value was estimated using the Monte Carlo valuation model.

The grant date fair value per share of the stock options was estimated using the Black-Scholes option pricing model which requires the use of various assumptions including the expected life of the option, expected dividend rate, expected volatility and risk-free interest rate. Key assumptions used for determining the fair value of the stock options granted during 2016, 2015 and 2014 were as follows:

	Year Ended December 31, 2016	Year Ended December 31, 2015	Year Ended December 31, 2014
Expected life <sup>(a)</sup>	5.5 - 6.5 years	5.5 - 6.5 years	5.5 - 6.5 years
Expected dividend <sup>(b)</sup>	—	—	—

Expected volatility <sup>(c)</sup>	55.1%	59.6%	51%
Risk-free interest rate <sup>(d)</sup>	1.40% - 1.76%	1.35% - 1.66%	1.63% - 2.29%

---

- (a) The expected lives (estimated period of time outstanding) of stock options granted were estimated using the 'Simplified Method' which utilizes the midpoint between the vesting date and the end of the contractual term. This method was utilized for the stock options due to the lack of historical exercise behavior of the Company's employees.
- (b) For all stock options granted during 2016, 2015 and 2014, no dividends are planned to be paid over the contractual term of the stock options resulting in the use of a zero expected dividend rate.
- (c) The expected volatility rate is based on the observed historical volatilities of our common stock and observed historical and implied volatilities of comparable companies, which were adjusted to account for the various differences between the comparable companies and us.
- (d) The risk-free interest rate is specific to the date of grant and is based on the United States Treasury constant maturity market yields in effect at the time of the grant.

(2) These awards were granted pursuant to the annual incentive plan. The 2016 amounts will be paid in March 2017. See "*Annual Incentive Compensation Awards*" for additional information.

(3) The amount shown for 2016 reflects the following for each NEO:

Name	401(k) <sup>(a)</sup>	Term life <sup>(b)</sup>	Relocation Expense Reimbursement <sup>(c)</sup>	Severance <sup>(d)</sup>	Total All Other Compensation
Mr. Sunu	\$ 13,250	\$ 2,472	\$ —	\$ —	\$ 15,722
Ms. Turner	13,250	977	—	—	14,227
Mr. Sabherwal	13,250	931	—	—	14,181
Mr. Nixon	13,250	1,268	—	—	14,518
Mr. Lunny	11,981	1,069	—	—	13,050
Mr. Rush	12,640	1,012	20,470	—	34,122
Mr. Tomae	11,554	147	—	993,693	1,005,394

(a) Reflects matching contributions made by the Company to its 401(k) retirement savings plan for each NEO.

(b) Contributions made by the Company to the term life insurance plans it sponsors for all eligible employees (including our NEOs).

(c) Relocation expenses reimbursed by the Company.

(d) As described further in "*Employment Agreements*", Mr. Tomae received a separation payment in 2016.

- (4) Mr. Sunu received a \$500,000 signing bonus during 2015 in connection with the extension of his employment agreement. Mr. Sunu does not receive any compensation for serving on our board of directors.
- (5) Ms. Turner began employment with the Company on April 7, 2014 and she was appointed as Chief Financial Officer effective August 3, 2016.
- (6) Mr. Sabherwal resigned his employment effective August 3, 2016.
- (7) Mr. Rush received an \$8,000 bonus during 2014.
- (8) Mr. Tomae's employment was terminated without cause effective January 29, 2016.

## Grants of Plan-Based Awards for 2016

Executive <sup>(1)</sup>	Grant Date	Estimated Future Payouts Under Non-Equity Incentive Plan Awards			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Stock Awards: Number of Shares of Stock or Units (#)	All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards <sup>(6)</sup> (\$/Sh)	Closing Market Price on Date of Option Award Grant <sup>(6)</sup> (\$/Sh)	Grant Date Fair Value of Stock and Option Awards <sup>(7)</sup> (\$)
		Threshold (\$)	Target (\$)	Maximum (\$)	Threshold (#)	Target (#)	Maximum (#)					
Mr. Sunu	2/9/2016 <sup>(2)</sup>	211,491	845,962	1,268,943	—	—	—	—	—	—	—	—
	1/22/2016 <sup>(3)</sup>	—	—	—	—	27,000	27,000	—	—	—	N/A	320,868
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	—	54,000	14.61	14.78	437,173
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	31,000	—	—	N/A	458,180
Ms. Turner	2/9/2016 <sup>(2)</sup>	39,430	157,721	236,582	—	—	—	—	—	—	—	—
	1/22/2016 <sup>(3)</sup>	—	—	—	—	6,000	6,000	—	—	—	N/A	71,304
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	—	12,000	14.61	14.78	97,150
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	7,000	—	—	N/A	103,460
	8/15/2016 <sup>(5)</sup>	—	—	—	—	—	—	—	25,000	14.14	14.04	188,737
8/15/2016 <sup>(5)</sup>	—	—	—	—	—	—	15,000	—	—	N/A	210,600	
Mr. Sabherwal	2/9/2016 <sup>(2)</sup>	52,500	210,000	315,000	—	—	—	—	—	—	—	—
	1/22/2016 <sup>(3)</sup>	—	—	—	—	9,000	9,000	—	—	—	N/A	106,956
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	—	19,000	14.61	14.78	153,820
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	11,000	—	—	N/A	162,580
Mr. Nixon	2/9/2016 <sup>(2)</sup>	44,265	177,060	265,590	—	—	—	—	—	—	—	—
	1/22/2016 <sup>(3)</sup>	—	—	—	—	8,000	8,000	—	—	—	N/A	157,148
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	—	16,000	14.61	14.78	129,533
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	9,000	—	—	N/A	70,944
Mr. Lunny	2/9/2016 <sup>(2)</sup>	36,775	147,101	220,652	—	—	—	—	—	—	—	—
	1/22/2016 <sup>(3)</sup>	—	—	—	—	6,000	6,000	—	—	—	N/A	71,304
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	—	13,000	14.61	14.78	105,245
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	6,000	—	—	N/A	88,680
Mr. Rush	2/9/2016 <sup>(2)</sup>	35,537	142,148	213,222	—	—	—	—	—	—	—	—
	1/22/2016 <sup>(3)</sup>	—	—	—	—	6,000	6,000	—	—	—	N/A	71,304
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	—	15,000	14.61	14.78	105,245
	1/22/2016 <sup>(4)</sup>	—	—	—	—	—	—	6,000	—	—	N/A	88,680

- (1) Mr. Tomae's employment was terminated without cause effective January 29, 2016.
- (2) See "—Annual Incentive Compensation Awards" and the *Summary Compensation* table for additional information. Amounts represent potential payouts under the annual incentive plan based on a percentage of 2016 annual base salary assuming achievement of the financial and service quality targets as follows: 25% for threshold, 100% for target and 150% for maximum. The actual amounts earned under the annual incentive plan for 2016 for Messrs. Sunu, Nixon, Lunny and Rush and Ms. Turner will be paid in March 2017 and are indicated in the *Summary Compensation* table. Mr. Sabherwal resigned his employment effective August 3, 2016.
- (3) These performance shares were granted under the LTIP Plan and will be earned, at the end of a three-year performance period, based upon (i) the Company's achievement of a growth revenue performance goal and (ii) the total shareholder return to our shareholders compared to the total shareholder return achieved by the companies in a telecommunications industry group.
- (4) These restricted stock awards and stock options were granted under the LTIP Plan and are time-vested. 25% vested on the grant date with the remainder vesting in equal installments on January 23, 2017, January 22, 2018 and January 22, 2019.

- (5) These restricted stock awards and stock options were granted under the LTIP Plan and are time-vested in equal installments on August 15, 2017, August 15, 2018 and August 15, 2019.
- (6) Exercise price of stock options is calculated as the average of the low and high market value of our common stock on the date of grant.
- (7) Reflects the grant date fair value of stock and option awards based on the number of awards included in the grant and the fair value of the awards at the date of grant, as determined in accordance with the Compensation—Stock Compensation Topic of the ASC. In the case of restricted stock this amount is equal to the number of restricted shares issued multiplied by the market value of our common stock on the date of grant. In the case of performance shares, the grant date fair value is based upon the probable outcome of the performance conditions. See note (1) to the *Summary Compensation* table for more information on the assumptions used.

### Outstanding Equity Awards at December 31, 2016

Executive(s)	Grant Date	Option Awards				Stock Awards			
		Number of Securities Underlying Unexercised Options (2) (#)	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (2) (#)	Option Exercise Price (3) (\$)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (4) (#)	Market Value of Shares or Units of Stock That Have Not Vested (5) (\$)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (6) (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (7) (\$)
Mr. Sunu	1/22/2016	—	—	—	—	23,250	434,775	—	—
	1/22/2016	—	—	—	—	—	—	27,000	504,900
	1/22/2016	13,500	40,500	14.61	1/22/2026	—	—	—	—
	1/22/2015	—	—	—	—	19,000	355,300	—	—
	1/22/2015	32,500	32,500	14.73	1/22/2025	—	—	—	—
	1/22/2015	—	—	—	—	—	—	26,000	486,200
	1/22/2014	—	—	—	—	14,000	261,800	—	—
	1/22/2014	63,750	21,250	13.29	1/22/2024	—	—	—	—
	1/22/2013	94,000	—	9.36	1/22/2023	—	—	—	—
	1/24/2012	48,000	—	4.56	1/24/2022	—	—	—	—
1/24/2011	125,000	—	24.29	1/24/2021	—	—	—	—	
Ms. Turner	8/15/2016	—	—	—	—	15,000	280,500	—	—
	8/15/2016	—	25,000	14.14	8/15/2026	—	—	—	—
	1/22/2016	—	—	—	—	5,250	98,175	—	—
	1/22/2016	—	—	—	—	—	—	6,000	112,200
	1/22/2016	3,000	9,000	14.61	1/22/2026	—	—	—	—
	1/22/2015	—	—	—	—	4,000	74,800	—	—
	1/22/2015	7,350	7,350	14.73	1/22/2025	—	—	—	—
	1/22/2015	—	—	—	—	—	—	6,000	112,200
	5/12/2014	—	—	—	—	1,333	24,927	—	—
5/12/2014	4,000	2,000	13.60	5/12/2024	—	—	—	—	

Executive(s)	Grant Date	Option Awards				Stock Awards			
		Number of Securities Underlying Unexercised Options (2) (#) Exercisable	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (2) (#)	Option Exercise Price (3) (\$)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (4) (#)	Market Value of Shares or Units of Stock That Have Not Vested (5) (\$)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (6) (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (7) (\$)
Mr. Nixon	1/22/2016	—	—	—	—	6,750	126,225	—	—
	1/22/2016	—	—	—	—	—	—	8,000	149,600
	1/22/2016	4,000	12,000	14.61	1/22/2026	—	—	—	—
	1/22/2015	—	—	—	—	6,250	116,875	—	—
	1/22/2015	9,500	9,500	14.73	1/22/2025	—	—	—	—
	1/22/2015	—	—	—	—	—	—	8,000	149,600
	1/22/2014	—	—	—	—	4,150	77,605	—	—
	1/22/2014	18,285	6,095	13.29	1/22/2024	—	—	—	—
	1/22/2013	27,500	—	9.36	1/22/2023	—	—	—	—
	1/24/2012	13,000	—	4.56	1/24/2022	—	—	—	—
1/24/2011	33,000	—	24.29	1/24/2021	—	—	—	—	
Mr. Lunny	1/22/2016	—	—	—	—	4,500	84,150	—	—
	1/22/2016	—	—	—	—	—	—	6,000	112,200
	1/22/2016	3,250	9,750	14.61	1/22/2026	—	—	—	—
	1/22/2015	—	—	—	—	4,500	84,150	—	—
	1/22/2015	3,875	7,750	14.73	1/22/2025	—	—	—	—
	1/22/2015	—	—	—	—	—	—	6,500	121,550
	1/22/2014	—	—	—	—	3,250	60,775	—	—
	1/22/2014	4,800	4,800	13.29	1/22/2024	—	—	—	—
	1/22/2013	1,000	—	9.36	1/22/2023	—	—	—	—
1/24/2011	18,500	—	24.29	1/24/2021	—	—	—	—	
Mr. Rush	1/22/2016	—	—	—	—	4,500	84,150	—	—
	1/22/2016	—	—	—	—	—	—	6,000	112,200
	1/22/2016	3,250	9,750	14.61	1/22/2026	—	—	—	—
	1/22/2015	—	—	—	—	4,000	74,800	—	—
	1/22/2015	7,350	7,350	14.73	1/22/2025	—	—	—	—
	1/22/2015	—	—	—	—	—	—	6,000	112,200
	1/22/2014	16,500	5,500	13.29	1/22/2024	—	—	—	—
	1/22/2013	2,000	—	9.36	1/22/2023	—	—	—	—
	1/24/2012	6,050	—	4.56	1/24/2022	—	—	—	—
1/24/2011	15,500	—	24.29	1/24/2021	—	—	—	—	
Mr. Tomasi <sup>(a)</sup>	1/22/2015	—	—	—	—	—	2,500	46,750	

(1) No unvested stock options or stock awards were outstanding at December 31, 2016 for Mr. Sabherwal.

(2) These stock options were granted under the LTIP Plan. See "—Grants of Plan-Based Awards for 2016" for vesting details of the January 22, 2016 and August 15, 2016 grants. The stock options shown for the January 22, 2015, January 22, 2014, January 22, 2013, January 24, 2012 and January 24, 2011 grants are time-vested. 25% vested on the grant date with the remainder vesting in three annual installments of 25%, commencing on or about the first anniversary date of the grant, except 3,000 stock options for Mr. Nixon granted on January 22, 2013 that vested 100% on the grant date. The stock options shown for the May 12, 2014 grant are time-vested, vesting in three equal annual installments, commencing on the first anniversary date of the grant.

- (3) The exercise price is calculated as the average of the low and high market value of our common stock on the date of grant.
- (4) These stock awards were granted under the LTIP Plan. See "*Grants of Plan-Based Awards for 2016*" for vesting details of the January 22, 2016 and August 15, 2016 grants. The stock awards shown for the January 22, 2015 and January 22,

2014 grants are time-vested. 25% vested on the grant date with the remainder vesting in three annual installments of 25%, commencing on or about the first anniversary date of the grant. The stock awards shown for the May 12, 2014 grant are time-vested, vesting in three equal annual installments, commencing on the first anniversary date of the grant.

- (5) Computed by multiplying the number of unvested shares by \$18.70, the market closing price of our common stock on December 30, 2016.
- (6) These performance share awards were granted under the LTIP Plan. See "*Grants of Plan-Based Awards for 2016*" for vesting details of the January 22, 2016 grant. The performance share awards shown for the January 22, 2015 grant will be earned, at the end of a three-year performance period, based upon (i) the Company's achievement of a growth revenue performance goal and (ii) the total shareholder return to our shareholders compared to the total shareholder return achieved by the companies in a telecommunications industry group.
- (7) Computed by multiplying the number of unvested shares by \$18.70, the market closing price of our common stock on December 30, 2016.
- (8) In accordance with the performance share awards pursuant to the LTIP Plan, Mr. Tomae's outstanding performance awards on his termination date were prorated to reflect the number of performance shares earned during the performance period while the remaining performance shares were forfeited on his termination date.

### Option Exercises and Stock Vested for 2016

Executive	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise <sup>(1)</sup> (\$)	Number of Shares Acquired on Vesting (#)	Value Realized on Vesting <sup>(2)</sup> (\$)
Mr. Sunu	—	—	41,250	609,675
Ms. Turner	—	—	5,083	74,394
Mr. Sabherwal	86,900	392,014	14,125	208,768
Mr. Nixon	—	—	12,275	181,425
Mr. Lunny	—	—	7,000	103,460
Mr. Rush	—	—	3,500	51,730
Mr. Tomae	79,250	464,640	10,175	150,387

- (1) Value realized by Mr. Sabherwal is computed by multiplying the number of shares acquired upon exercise by the difference between the market price of the underlying securities on the exercise date (\$14.99) and the strike price of the stock options (15,500 at \$4.56; 33,500 at \$9.36; 21,750 at \$13.29; 11,400 at \$14.73 and 4,750 at \$14.61). Value realized by Mr. Tomae is computed by multiplying the number of shares acquired upon exercise by the difference between the market price of the underlying securities on the exercise date (\$15.61) and the strike price of the stock options (26,000 at \$5.29; 22,000 at \$9.36; 21,750 at \$13.29 and 9,500 at \$14.73).
- (2) Value realized is computed by multiplying the number of shares acquired upon vesting by the market price of the underlying securities on the vesting date of January 22, 2016 at \$14.78 for all shares except 1,333 shares for Ms. Turner which vested on May 12, 2016 at \$14.23.

### Potential Payments Upon Termination or Change in Control

As of December 31, 2016, we had employment agreements with Messrs. Sunu, Nixon, Lunny and Rush and Ms. Turner. The employment agreements provide benefits to our NEOs in the event their employment is terminated under certain circumstances as summarized below. In addition, as described below, we had an employment agreement with Mr. Tomae, whose employment terminated without cause effective January 29, 2016, pursuant to which Mr. Tomae received certain benefits upon such termination.

On December 3, 2016, FairPoint Communications entered into the Merger Agreement with Consolidated. Additional details, including reasons for the Merger and conditions to close as well as compensation that may be payable to our executive officers in connection with the Merger, are disclosed in our definitive proxy statement filed with the SEC on February 27, 2017.

## *Employment Agreements*

### *Paul H. Sunu*

Under the Sunu Employment Agreement, in the event (a) the Company terminates Mr. Sunu's employment without cause (as defined in the Sunu Employment Agreement), (b) the term of employment under the Employment Agreement expires following the Company's delivery of a non-extension notice or (c) Mr. Sunu resigns his employment for good reason (as defined in the Sunu Employment Agreement), Mr. Sunu is entitled to receive (i) any accrued but unpaid base salary through the date of the termination, any unpaid annual incentive plan bonus (in respect of any completed fiscal year that has ended prior to the date of the termination of Mr. Sunu's employment), any unpaid or unreimbursed expenses and any benefits to be provided under the Company's employee benefits plans upon a termination of employment; and (ii) an amount equal to the sum of (A) two times the amount of Mr. Sunu's then-current base salary, (B) two times the amount of his average annual incentive plan bonus; and (C) the cost of continued health and disability insurance coverage for Mr. Sunu and his covered dependents for a period of 24 months. Mr. Sunu will also be entitled to any (x) amounts payable under the LTIP Plan (in accordance with its terms) and (y) a pro rata portion of the annual incentive plan bonus for the year in which the termination occurred. The amount of Mr. Sunu's average annual incentive plan bonus will be determined based on Mr. Sunu's actual annual incentive plan bonus in the two years immediately preceding the year in which termination occurs.

In addition, upon termination of his employment under the circumstances described in (a), (b) and (c) of the preceding paragraph, Mr. Sunu is entitled to immediate accelerated vesting of (i) the next tranche of any time-based equity award that would have otherwise vested except for the termination or receipt of a non-extension notice and (ii) any performance-based equity award, if, in the discretion of the compensation committee, the performance vesting criteria have been met as of the date of termination, prorated for the time employed during the performance period prior to the date of termination or receipt of a non-extension notice. The benefits and payments described in this and the preceding paragraph are subject to adjustment in the event that Mr. Sunu's employment is terminated by the Company without cause (other than due to his death or disability) within 12 months before or 12 months after a change in control (as defined in the Sunu Employment Agreement). The amount of Mr. Sunu's bonus upon termination related to a change in control will be the greater of (B) of the preceding paragraph or two times his target annual incentive plan bonus for the year in which the termination occurred. Also upon the occurrence of a change in control, Mr. Sunu's unvested benefits under the LTIP Plan are accelerated and vest in full.

Pursuant to the Sunu Employment Agreement, in the event that Mr. Sunu's employment is terminated (a) by the Company with cause, (b) by Mr. Sunu without good reason or (c) upon the expiration of the term of employment following delivery by Mr. Sunu to the Company of a non-extension notice, Mr. Sunu is entitled to (x) any accrued but unpaid base salary through the date of the termination of Mr. Sunu's employment, (y) any unpaid or unreimbursed expenses and (z) any benefits to be provided under the Company's employee benefits plans (in accordance with the terms of such plans). Mr. Sunu will also be entitled to amounts payable under the LTIP Plan (in accordance with its terms). However, Mr. Sunu will be entitled to receive the payments and benefits as provided by the Sunu Employment Agreement for termination by Mr. Sunu for good reason, subject to the same conditions as those under such circumstances, in the event that Mr. Sunu provides the Company with notice of his termination of employment without good reason during the 13th month following the consummation of a change in control.

In the event that Mr. Sunu's employment is terminated due to death or disability, Mr. Sunu or his estate or his beneficiaries, as the case may be, are entitled to (i) any accrued but unpaid base salary through the date of the termination of Mr. Sunu's employment, (ii) any unpaid annual incentive plan bonus (in respect of any completed fiscal year that has ended prior to the date of the termination of Mr. Sunu's employment), (iii) any unpaid or unreimbursed expenses, (iv) any benefits to be provided under the Company's employee benefits plans (in accordance with such plans), (v) amounts payable under the LTIP Plan (in accordance with its terms) and (vi) an amount equal to the sum of (x) Mr. Sunu's then-current base salary, (y) Mr. Sunu's annual incentive plan bonus for the immediately preceding fiscal year and (z) the cost of continued health and disability insurance coverage for Mr. Sunu and his covered dependents during the 12-month period following the date of such termination.

The payment of any amount or provision of any benefit, subject to certain exceptions set forth in the Sunu Employment Agreement, is conditioned upon Mr. Sunu's execution and delivery to the Company of a release of all claims against, among other parties, the Company and its subsidiaries, in connection with those termination circumstances under the Sunu Employment Agreement requiring a release. In addition, Mr. Sunu's entitlement to payments and benefits upon termination under the Sunu Employment Agreement is subject to his compliance with a non-interference agreement with the Company, pursuant to which Mr. Sunu agrees to, among other things, certain non-competition and non-solicitation provisions for 24 months following the termination of his employment with the Company.

### *Karen D. Turner, Peter G. Nixon, John J. Lunny and Steven G. Rush*

Under the respective employment agreements with each of the above named executives, either party may terminate the executive's employment at any time. In the event (i) the Company terminates the executive's employment without cause (as defined in the employment agreements) prior to the expiration of the term of employment, (ii) the Company delivers a termination notice



to the executive in accordance with the provisions of his or her employment agreement or (iii) the executive resigns his or her employment for good reason (as defined in the employment agreements), the executive will receive: (x) any accrued but unpaid base salary through the date of the termination, any unpaid annual incentive plan bonus (in respect of any completed fiscal year that has ended prior to the date of the termination of the executive's employment), any unpaid or unreimbursed expenses, any benefits to be provided under the Company's employee benefits plans upon a termination of employment and any amounts payable under the LTIP Plan; and (y) an amount equal to the sum of (A) two times the amount of the executive's then-current base salary, (B) two times the amount of his or her average annual incentive plan bonus for the immediately preceding two fiscal years where such average is determined by reference to the actual annual bonus paid to the executive for the immediately two preceding fiscal years; and (C) the cost of continued health and disability insurance coverage for the executive and his or her covered dependents for a period of 24 months following such termination or resignation, as applicable. In the case of (iii) above, the executive is also entitled to accelerated vesting of the next tranche of awards payable under the LTIP Plan. The employment agreements do not require the Company to provide any tax gross-up on the benefits paid under the employment agreements.

In the event the Company terminates the executive's employment without cause (as defined in the employment agreements) or the Company delivers a termination notice to the executive, in either case after the expiration of the term of employment, the executive will receive: (i) any accrued but unpaid base salary through the date of the termination, (ii) any unpaid or unreimbursed expenses, (iii) any benefits to be provided under the Company's employee benefits plans and (iv) any amounts payable under the LTIP Plan. However, if such termination occurs within six months of a change in control, the executive is also entitled to any unpaid annual incentive plan bonus (in respect of any completed fiscal year that has ended prior to the date of the termination of the executive's employment) and each of the payments and benefits described in (A) and (C) in the immediately preceding paragraph. The amount of the executive's bonus upon termination related to a change in control will be the greater of (B) in the preceding paragraph or two times his or her target annual incentive plan bonus for the year in which the termination occurred.

In the event that the executive's employment is terminated due to death or disability, the executive or his or her estate or his or her beneficiaries, as the case may be, is entitled to (i) any accrued but unpaid base salary through the date of the termination of the executive's employment, (ii) any unpaid annual incentive plan bonus (in respect of any completed fiscal year that has ended prior to the date of the termination of the executive's employment), (iii) any unpaid or unreimbursed expenses, (iv) any benefits to be provided under the Company's employee benefits plans (in accordance with such plans) and (v) any amounts payable under the LTIP Plan.

In the event that the executive's employment is terminated (i) by the Company with cause, (ii) by the executive without good reason or (iii) upon the delivery by the executive to the Company of a termination notice pursuant to the terms of his or her employment agreement, the executive is entitled to any accrued but unpaid base salary through the date of the termination of the executive's employment, any unpaid or unreimbursed expenses, any benefits to be provided under the Company's employee benefits plans upon a termination of employment (in accordance with the terms of such plans) and any amounts payable under the LTIP Plan.

Upon the occurrence of a change in control, all of the executives' unvested benefits under the LTIP Plan are accelerated and vest in full.

The executive's entitlement to payments and benefits under his or her employment agreement is subject to his or her compliance with a non-interference agreement with the Company, pursuant to which the executive agrees to, among other things, certain non-competition and non-solicitation provisions for 12 months following his or her employment with the Company.

In addition, in the event that (i) the executive's employment is terminated due to death or disability, (ii) the Company terminates the executive's employment without cause, (iii) the Company delivers a termination notice prior to the expiration of the executive's term of employment pursuant to the provisions of the employment agreement, or (iv) the executive terminates his or her employment with good reason in accordance with his or her employment agreement, the payment of any amount or provision of any benefit in connection therewith is conditioned upon the executive's execution and delivery to the Company of a release of all claims, subject to certain exceptions set forth in the employment agreements.

#### *Anthony A. Tomae*

Mr. Tomae's employment with the Company terminated without cause effective January 29, 2016. The benefits and payments provided to him in connection with such termination were provided pursuant to his employment agreement with the Company dated as of November 15, 2012, as amended on August 14, 2015.

In accordance with his employment agreement, Mr. Tomae received a separation payment which consisted of: (x) his accrued, but unpaid, base salary through the date of termination, unpaid or unreimbursed expenses and accrued and unpaid vacation pay as provided under the Company's employee benefits plans upon a termination of employment; and (y) an amount equal to the sum of (A) two times the amount of Mr. Tomae's then-current base salary, (B) two times the amount of his average annual incentive plan bonus for 2014 and 2015 where the average was determined by reference to the actual annual bonus paid to Mr. Tomae and (C) the cost of continued health and disability insurance coverage for Mr. Tomae for a period of 24 months following his termination.



In accordance with his employment agreement, the Company did not provide any tax gross-up on the benefits paid under the agreement.

Upon the occurrence of a change in control, Mr. Tomae's unvested benefits under the LTIP Plan are accelerated and vest in full.

Mr. Tomae's entitlement to payments and benefits under his employment agreement were subject to his compliance with a non-interference agreement with the Company, pursuant to which Mr. Tomae agreed to, among other things, certain non-competition and non-solicitation provisions for twelve months following his employment with the Company and a general release of claims.

*Potential Post-Employment Payments Table*

The following table shows cash compensation and other benefits that would have been provided under the employment agreements with the CEO if his employment had terminated on December 31, 2016 under conditions that would trigger payments.

<u>Reason for Payment</u>	<u>Base Salary<sup>(1)</sup> (S)</u>	<u>Non-Equity Incentive Plan<sup>(2)</sup> (S)</u>	<u>Acceleration and Continuation of Equity Awards<sup>(3)</sup> (S)</u>	<u>Continuation of Medical/Welfare Benefits<sup>(4)</sup> (S)</u>	<u>Total Termination Benefits (S)</u>
<b>Mr. Sunu</b>					
Involuntary termination with cause or voluntary termination without good reason	—	—	—	—	—
Death or disability	830,000	893,100	1,778,998	17,585	3,519,683
Expiration following non-extension notice	1,660,000	1,300,600	492,433	35,171	3,488,204
Termination without cause or voluntary termination with good reason	1,660,000	1,300,600	1,311,498	35,171	4,307,269
Termination after change in control	1,660,000	1,660,000	2,452,608	35,171	5,807,779

- (1) Other than for Mr. Sunu's death or disability, the base salary paid upon termination under the applicable scenario is calculated as two times the 2016 base salary. In the event of Mr. Sunu's death or disability, the base salary paid upon termination is equal to his 2016 base salary.
- (2) Other than for Mr. Sunu's death or disability, the incentive paid upon termination under the applicable scenario is calculated as two times the average of the annual incentive paid for the immediately two preceding fiscal years (fiscal years 2015 and 2014), except in the case of termination due to a change in control, which is the greater of the average annual incentive paid for the immediately two preceding fiscal years or two times the annual incentive target. In the event of Mr. Sunu's death or disability, the incentive is equal to his annual incentive paid for the immediately preceding fiscal year (fiscal year 2015).
- (3) The amounts are calculated based on the closing price of \$18.70 on December 30, 2016 under the applicable scenario. In the event of Mr. Sunu's death or disability, the amount is calculated for full vesting of stock awards, the next tranche for option awards and a prorated amount for performance share awards pursuant to the LTIP Plan. In the event of Mr. Sunu's receipt of a non-extension notice, the amount is calculated for a prorated amount for performance awards. In the event of Mr. Sunu's termination without cause or voluntary termination with good reason, the amount is calculated for the next tranche of stock and option awards and a prorated amount for performance awards. In the case of termination related to a change in control, the amount is calculated for full vesting of all unvested awards.
- (4) Other than for Mr. Sunu's death or disability, the cost of continued health and disability insurance coverage paid upon termination under the applicable scenario is calculated at the present value of 24 months of benefits. In the event of Mr. Sunu's death or disability, the amount is calculated at the present value of 12 months of benefits.

The following table shows cash compensation and other benefits that would have been provided under the employment agreements with the other NEOs, other than Mr. Tomae, if their employment had terminated on December 31, 2016 under conditions that would trigger payments. The information set forth in the table below with respect to Mr. Tomae shows the cash compensation and other benefits provided to him in connection with the termination of his employment with the Company without cause effective January 29, 2016.



Reason for Payment	Base Salary <sup>(1)</sup> (\$)	Non-Equity Incentive Plan <sup>(2)</sup> (\$)	Acceleration and Continuation of Equity Awards <sup>(3)</sup> (\$)	Continuation of Medical/Welfare Benefits <sup>(4)</sup> (\$)	Total Termination Benefits (\$)
<b>Ms. Turner</b>					
Involuntary termination with cause or voluntary termination without good reason	—	—	—	—	—
Death or disability	—	—	665,668	—	665,668
Termination without cause	750,000	178,100	420,195	30,659	1,378,954
Voluntary termination with good reason	750,000	178,100	263,618	30,659	1,222,377
Termination after change in control	750,000	375,000	892,998	30,659	2,048,657
<b>Mr. Nixon</b>					
Involuntary termination with cause or voluntary termination without good reason	—	—	—	—	—
Death or disability	—	—	538,496	—	538,496
Termination without cause	706,000	268,100	208,035	35,171	1,217,306
Voluntary termination with good reason	706,000	268,100	246,309	35,171	1,255,580
Termination after change in control	706,000	353,000	739,674	35,171	1,833,845
<b>Mr. Lunny</b>					
Involuntary termination with cause or voluntary termination without good reason	—	—	—	—	—
Death or disability	—	—	402,153	—	402,153
Termination without cause	600,000	212,000	159,776	45,250	1,017,026
Voluntary termination with good reason	600,000	212,000	185,544	45,250	1,042,794
Termination after change in control	600,000	300,000	559,438	45,250	1,504,688
<b>Mr. Rush</b>					
Involuntary termination with cause or voluntary termination without good reason	—	—	—	—	—
Death or disability	—	—	328,787	—	328,787
Termination without cause	570,000	204,600	153,543	50,058	978,201
Voluntary termination with good reason	570,000	204,600	123,087	50,058	947,745
Termination after change in control	570,000	285,000	482,162	50,058	1,387,220
<b>Mr. Tomae<sup>(5)</sup></b>					
Termination without cause	686,000	268,800	46,750	38,893	1,040,443

- (1) The base salary paid upon termination under the applicable scenario is calculated as two times the 2016 base salary.
- (2) The incentive paid upon termination under the applicable scenario is calculated as two times the average of the annual incentive paid for the immediately two preceding fiscal years (fiscal years 2015 and 2014), except in the case of termination due to a change in control, which is the greater of the average annual incentive paid for the immediately two preceding fiscal years or two times the annual incentive target.
- (3) The amounts are calculated based on the closing price of \$18.70 on December 30, 2016 under the applicable scenario. In the event of death or disability, the amount is calculated for full vesting of stock awards, the next tranche for option awards and a prorated amount for performance share awards pursuant to the LTIP Plan. In the event of voluntary termination with good reason, the amount is calculated for the next tranche of stock and option awards. The amount is calculated for the next tranche for January 22, 2016 stock and option awards and the next two tranches for August 15, 2016 stock and option awards in order to obtain at least 50% vesting as well as a prorated amount for performance share awards in the event of termination without cause pursuant to the LTIP Plan. In the case of termination related to a change in control, the amount is calculated for full vesting of all unvested awards.



- (4) The cost of continued health and disability insurance coverage paid upon termination under the applicable scenario is calculated at the present value of 24 months of benefits.
- (5) Mr. Tomae's employment with the Company terminated without cause effective January 29, 2016. The base salary, non-equity incentive plan and the continuation of health and disability insurance coverage reflects the actual payment and benefits received by Mr. Tomae upon his termination. The acceleration and continuation of equity awards amount is calculated based on the closing price of \$18.70 on December 30, 2016. In accordance with the performance share awards pursuant to the LTIP Plan, Mr. Tomae's outstanding performance awards on his termination date were prorated to reflect the number of performance shares earned during the performance period while the remaining performance shares were forfeited on his termination date.

### Director Compensation

We use a combination of cash and stock-based incentive compensation to attract and retain qualified candidates to serve on our board of directors. In setting director compensation, we consider the significant amount of time that directors spend in fulfilling their duties to us as well as the skill level required by the members of our board of directors. Our employee director, Mr. Sunu, does not receive any compensation for serving on our board of directors.

#### *2016 Compensation*

*Cash Compensation.* With the exception of Mr. Gingold, who elected to forgo all compensation, our non-employee directors were paid the following cash fees in 2016: (i) an annual fee of \$75,000 for serving as a non-employee director; (ii) a \$40,000 annual cash retainer for serving as the chair of the board of directors; (iii) a \$30,000 annual cash retainer for serving as the chair of the audit committee; (iv) a \$20,000 annual cash retainer for serving as the chair of the compensation committee (prorated for a partial year's service in the case of Messrs. Horowitz and Treadwell), the corporate governance and nominating committee (prorated for a partial year's service in the case of Messrs. Treadwell and Horowitz) and the regulatory committee; and (v) annual committee member fees of \$15,000 for serving on the audit committee (prorated for a partial year's service in the case of Mr. Mahoney) and \$7,500 for serving on the compensation committee (prorated for a partial year's service in the case of Messrs. Horowitz, Mahoney and Treadwell). All annual fees were paid in quarterly installments.

*Equity Compensation.* Again, with the exception of Mr. Gingold, who elected to forgo all compensation, on January 22, 2016, each of our non-employee directors received an award of approximately \$150,000 in the form of restricted stock and stock options under the LTIP Plan. These awards vested 100% on the first anniversary of the grant date, January 23, 2017.

#### *Share Ownership Guidelines*

Our directors are subject to share ownership guidelines to better align their interests with those of our shareholders by requiring directors to acquire and maintain meaningful equity positions in the Company. Under the guidelines, each director is required to own shares of our common stock with a value equal to at least three times their annual base cash retainer. Directors are required to meet these guidelines within the later of five years of the date of adoption of these guidelines (by June 3, 2018) or of such individual becoming subject to them. If a director does not meet the required ownership guidelines within the specified period, he may receive all of his future board compensation in equity until the goal is met.

#### *No Hedging/No Pledging Provisions*

Our insider trading policy prohibits the directors from using any strategies or products (such as derivative securities or short-selling techniques) to hedge against the potential changes in the value of our common stock, prohibits the holding of our securities in a margin account and prohibits any director from pledging our securities as collateral for a loan.

## 2016 Director Summary Compensation Table

Name	Fees Earned or Paid in Cash <sup>(1)</sup> (S)	Stock Awards <sup>(2)</sup> (S)	Option Awards <sup>(3)</sup> (S)	Total (S)
Peter D. Aquino	90,000	105,012	44,992	240,004
Dennis J. Austin	90,000	105,012	44,992	240,004
Peter C. Gingold <sup>(4)</sup>	—	—	—	—
Edward D. Horowitz	138,750	105,012	44,992	288,754
Michael J. Mahoney	106,250	105,012	44,992	256,254
Michael K. Robinson	90,000	105,012	44,992	240,004
David L. Treadwell	98,750	105,012	44,992	248,754
Wayne Wilson	105,000	105,012	44,992	255,004

- (1) See the discussion preceding this table for the general method used to determine each non-employee director's cash compensation. For fiscal 2016, the particular components paid as cash compensation in excess of each non-employee director's \$75,000 annual retainer were as follows: Mr. Aquino (\$15,000 as member of the audit committee); Mr. Austin (\$15,000 as member of the audit committee); Mr. Horowitz (\$40,000 as chair of the board of directors, \$10,000 as chair of the corporate governance and nominating committee effective June 1, 2016, \$10,000 as chair of the compensation committee through May 31, 2016 and \$3,750 as member of the compensation committee effective June 1, 2016); Mr. Mahoney (\$20,000 as chair of the regulatory committee, \$7,500 as member of the audit committee through May 31, 2016 and \$3,750 as member of the compensation committee effective June 1, 2016); Mr. Robinson (\$15,000 as member of the audit committee); Mr. Treadwell (\$10,000 as chair of the compensation committee effective June 1, 2016, \$10,000 as chair of the corporate governance and nominating committee through May 31, 2016, and \$3,750 as member of the compensation committee through May 31, 2016) and Mr. Wilson (\$30,000 as chair of the audit committee).
- (2) Reflects the grant date fair value based on the number of awards included in the grant and the fair value of the awards at the date of grant, as determined in accordance with the Compensation—Stock Compensation Topic of the ASC. This amount is equal to the number of shares of restricted stock issued multiplied by the market value of our common stock on the date of grant. On January 22, 2016, each director, with the exception of Mr. Gingold, was granted 7,105 shares of restricted stock with a market value of \$14.78 per share that vested on January 23, 2017.
- (3) Reflects the grant date fair value based on the number of awards included in the grant and the fair value of the awards at the date of grant, as determined in accordance with the Compensation—Stock Compensation Topic of the ASC. See note (1) to the *Summary Compensation* table for more information on the assumptions used. On January 22, 2016, each director, with the exception of Mr. Gingold, was granted 6,025 options with a grant date fair value of \$7.47 per share that vested on January 23, 2017.
- (4) Mr. Gingold waived the receipt of all compensation.

**Compensation Committee Interlocks and Insider Participation**

The compensation committee of the board of directors for 2016 was comprised of Mr. Treadwell, Mr. Gingold, Mr. Horowitz and Mr. Mahoney (effective June 1, 2016). None of the members of the board of directors who sat on the compensation committee in 2016 was employed by us as an officer or employee during or prior to 2016 or had any interlocking relationships requiring disclosure under applicable rules and regulations. No executive officer of the Company served as a member of the compensation committee of another entity, one of whose executive officers served on our board of directors in 2016.

**Compensation Committee Report\***

The compensation committee of the board of directors oversees the executive compensation program for the Company's CEO and other executive officers, including those named in "*Compensation Discussion and Analysis—2016 Summary Compensation Table*" in this Annual Report. The executive officers named in that table are referred to collectively as the named executive officers (the "NEOs").

The compensation committee is generally responsible for strategic decisions relating to the overall compensation structure and program applicable to the Company's executives and senior management. The program currently includes: base salaries, cash-based annual incentive compensation and equity-based long-term incentives. The compensation committee, jointly with the corporate governance and nominating committee, is responsible for the compensation program of our non-employee directors, which program is currently comprised of cash fees and equity.



On behalf of the shareholders, the compensation committee has carefully monitored the Company's executive compensation program. We believe that the Compensation Discussion and Analysis contained in this Annual Report and the related tables that follow will show an executive compensation program that is designed to maximize long-term shareholder value and provide the NEOs with incentives for superior corporate and individual performance and encourage them to remain with the Company.

The compensation committee has reviewed and discussed the Compensation Discussion and Analysis with management, and, based on such review and discussions, recommended to the board of directors that it be included in this Annual Report.

Shareholders are invited to express their views to the board of directors regarding executive compensation as well as other matters as described in this Annual Report. See "Board of Directors and Committees of the Board of Directors—Policies Relating to our Board of Directors—Communications with Board of Directors" in this Annual Report.

*Submitted by the compensation committee of the board of directors:*

*David L. Treadwell (Chair)*

*Edward D. Horowitz*

*Peter C. Gingold*

*Michael J. Mahoney*

\* The material in this report shall not be deemed to be "soliciting material", or to be "filed" with the SEC or subject to the liabilities of Section 18 of the Exchange Act, and is not incorporated by reference in any filing of the Company under the Securities Act of 1933 or the Exchange Act, whether made before or after the date hereof and regardless of any general incorporation language in any such filing.

## **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The information required by Item 201(d) of Regulation S-K is incorporated herein by reference to "Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities—Securities Authorized for Issuance under Equity Compensation Plans" included elsewhere in this Annual Report.

### **Security Ownership of Certain Beneficial Owners and Management**

The following table sets forth information regarding beneficial ownership of our common stock as of February 27, 2017. The information (other than with respect to our current directors and executives) is based on a review of statements filed prior to February 27, 2017 with the SEC pursuant to Sections 13(d), 13(f), 13(g) and 16 of the Exchange Act with respect to our common stock. The following table includes beneficial ownership for:

- each NEO;
- all other executive officers as a group;
- each director;
- all executive officers and directors as a group; and
- each person known to us to be the beneficial owner of 5% or more of the outstanding shares of our common stock based on such person's most recently filed Schedule 13D or Schedule 13G.

The address of each director and executive officer listed is c/o FairPoint Communications, Inc., 521 East Morehead Street, Suite 500, Charlotte, NC 28202.

The amounts and percentages of common stock beneficially owned are reported on the basis of regulations of the SEC governing the determination of beneficial ownership of securities. Under the rules of the SEC, a person is deemed to be a "beneficial owner" of a security if that person has or shares "voting power", which includes the power to vote or to direct the voting of such security, or "investment power", which includes the power to dispose of or direct the disposition of such security. A person is also deemed to be a beneficial owner of any securities of which that person has a right to acquire beneficial ownership within 60 days. All persons listed have sole voting and investment power with respect to their shares unless otherwise indicated.

Name	Common Stock Beneficially Owned <sup>(1)</sup>	
	Number	Percent of Class
<b>Executive Officers and Directors:</b>		
Paul H. Sunu <sup>(2)</sup>	743,236	2.7%
Karen D. Turner <sup>(3)</sup>	61,730	0.2%
Peter G. Nixon <sup>(4)</sup>	199,642	0.7%
John J. Lunny <sup>(5)</sup>	81,605	0.3%
Steven G. Rush <sup>(6)</sup>	82,919	0.3%
Ajay Sabherwal <sup>(7)</sup>	69,355	0.3%
Anthony A. Tomac <sup>(8)</sup>	49,608	0.2%
Other executive officers as a group (2 persons) <sup>(9)</sup>	60,259	0.2%
Peter D. Aquino <sup>(10)</sup>	42,952	0.2%
Dennis J. Austin <sup>(11)</sup>	106,798	0.4%
Peter C. Gingold <sup>(12)</sup>	—	—
Edward D. Horowitz <sup>(13)</sup>	117,298	0.4%
Michael J. Mahoney <sup>(14)</sup>	104,798	0.4%
Michael K. Robinson <sup>(15)</sup>	104,798	0.4%
David L. Treadwell <sup>(16)</sup>	123,798	0.5%
Wayne Wilson <sup>(17)</sup>	104,798	0.4%
All current executive officers and directors as a group (15 persons) <sup>(18)</sup>	1,934,631	7.1%
<b>5% Shareholders:</b>		
Angelo, Gordon & Co., L.P. <sup>(19)</sup>	5,128,325	18.8%
The Vanguard Group <sup>(20)</sup>	2,312,969	8.5%
Maglan Capital LP <sup>(21)</sup>	2,062,812	7.6%
BlackRock, Inc. <sup>(22)</sup>	1,594,606	5.8%
Renaissance Technologies LLC <sup>(23)</sup>	1,477,800	5.4%
Vanguard World Funds <sup>(24)</sup>	1,426,565	5.2%

- (1) Unless otherwise indicated below, the persons and entities named in the table have sole voting and sole investment power with respect to all shares beneficially owned by them, subject to community property laws where applicable. The percentage of beneficial ownership is based on 27,266,570 shares of our common stock outstanding as of February 27, 2017.
- (2) With respect to shares Mr. Sunu beneficially owned: (i) includes 427,750 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 43,000 shares of restricted stock awarded under the LTIP Plan and (iii) includes 272,486 shares of common stock.
- (3) With respect to shares Ms. Turner beneficially owned: (i) includes 21,025 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 28,583 shares of restricted stock awarded under the LTIP Plan and (iii) includes 12,122 shares of common stock.
- (4) With respect to shares Mr. Nixon beneficially owned: (i) includes 120,130 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 13,625 shares of restricted stock awarded under the LTIP Plan and (iii) includes 65,887 shares of common stock.
- (5) With respect to shares Mr. Lunny beneficially owned: (i) includes 43,350 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 11,250 shares of restricted stock awarded under the LTIP Plan and (iii) includes 27,005 shares of common stock.
- (6) With respect to shares Mr. Rush beneficially owned: (i) includes 63,075 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 11,000 shares of restricted stock awarded under the LTIP Plan and (iii) includes 8,844 shares of common stock.

- (7) Mr. Sabherwal resigned his employment with the Company effective August 3, 2016. With respect to shares beneficially owned, includes 69,355 shares of common stock as of his termination date, the latest date for which information is available to the Company.

- (8) Mr. Tomae's employment with the Company terminated without cause effective January 29, 2016. With respect to shares beneficially owned, includes 49,608 shares of common stock as of his termination date, the latest date for which information is available to the Company.
- (9) With respect to shares beneficially owned: (i) includes 37,850 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 21,000 shares of restricted stock awarded under the LTIP Plan and (iii) includes 1,409 shares of common stock.
- (10) With respect to shares Mr. Aquino beneficially owned: (i) includes 15,842 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 7,500 shares of restricted stock awarded under the LTIP Plan and (iii) includes 19,610 shares of common stock.
- (11) With respect to shares Mr. Austin beneficially owned: (i) includes 47,643 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 7,500 shares of restricted stock awarded under the LTIP Plan and (iii) includes 51,655 shares of common stock.
- (12) Mr. Gingold has elected to waive all compensation and otherwise owns no shares of common stock.
- (13) With respect to shares Mr. Horowitz beneficially owned: (i) includes 47,643 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 7,500 shares of restricted stock awarded under the LTIP Plan and (iii) includes 62,155 shares of common stock.
- (14) With respect to shares Mr. Mahoney beneficially owned: (i) includes 47,643 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 7,500 shares of restricted stock awarded under the LTIP Plan and (iii) includes 49,655 shares of common stock.
- (15) With respect to shares Mr. Robinson beneficially owned: (i) includes 47,643 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 7,500 shares of restricted stock awarded under the LTIP Plan and (iii) includes 49,655 shares of common stock.
- (16) With respect to shares Mr. Treadwell beneficially owned: (i) includes 47,643 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 7,500 shares of restricted stock awarded under the LTIP Plan and (iii) includes 68,655 shares of common stock.
- (17) With respect to shares Mr. Wilson beneficially owned: (i) includes 47,643 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 7,500 shares of restricted stock awarded under the LTIP Plan and (iii) includes 49,655 shares of common stock.
- (18) With respect to shares beneficially owned: (i) includes 1,014,880 shares of our common stock issuable upon exercise of stock options that are either currently exercisable or become exercisable during the next 60 days, (ii) includes 180,958 shares of restricted stock awarded under the LTIP Plan and (iii) includes 738,793 shares of common stock. Does not include shares beneficially owned by Mr. Sabherwal or Mr. Tomae because they are no longer current executive officers.
- (19) Based solely on information contained in the Schedule 13D filed with the SEC on May 20, 2011 by Angelo, Gordon & Co., L.P. (address: 245 Park Avenue, 26<sup>th</sup> Floor, New York, New York 10167) and the number of outstanding shares of our common stock on February 27, 2017. The Angelo, Gordon & Co., L.P. Schedule 13D reported sole voting power and sole dispositive power of 5,128,325 shares.
- (20) Based solely on information contained in the Schedule 13G filed on February 10, 2017 with the SEC as of December 31, 2016 by The Vanguard Group (address: 100 Vanguard Boulevard, Malvern, Pennsylvania 19355) and the number of outstanding shares of our common stock on February 27, 2017. The Vanguard Group Schedule 13G reported an aggregate amount beneficially owned by each reporting person of 2,312,969 shares.
- (21) Based solely on information contained in the Schedule 13G filed on December 5, 2016 with the SEC as of December 5, 2016 by Maglan Capital LP (address: 25 West 39th Street, 2nd Floor, New York, New York 10018) and the number of outstanding shares of our common stock on February 27, 2017. The Maglan Capital LP Schedule 13G reported shared voting power and shared dispositive power of 2,062,812 shares.
- (22) Based solely on information contained in the Schedule 13G filed on January 30, 2017 with the SEC as of December 31, 2016 by BlackRock, Inc. (address: 55 East 52nd Street, New York, New York 10055) and the number of outstanding shares of our

common stock on February 27, 2017. The BlackRock, Inc. Schedule 13G reported an aggregate amount beneficially owned by each reporting person of 1,594,606 shares.

- (23) Based solely on information contained in the Schedule 13G filed on February 14, 2017 with the SEC as of December 15, 2016 by Renaissance Technologies LLC (address: 800 Third Avenue, New York, New York 10022) and the number

of outstanding shares of our common stock on February 27, 2017. The Renaissance Technologies LLC Schedule 13G reported an aggregate amount beneficially owned by each reporting person of 1,477,800 shares.

- (24) Based solely on information contained in the Schedule 13G filed on February 13, 2017 with the SEC as of December 31, 2016 by Vanguard World Funds (address: 100 Vanguard Boulevard, Malvern, Pennsylvania 19355) and the number of outstanding shares of our common stock on February 27, 2017. The Vanguard World Funds Schedule 13G reported sole voting power of 1,426,565 shares.

## ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

### Certain Relationships and Related Transactions

Our code of business conduct and ethics, which is posted on our website at [www.fairpoint.com](http://www.fairpoint.com), prohibits directors and executive officers from engaging in transactions on behalf of us with a family member or with a company with which they are or their family member is a significant owner or associated or employed in a significant role. Our audit committee must review and approve in advance all material related party transactions or business or professional relationships. All instances involving potential related party transactions or business or professional relationships must be reported to our legal department which will assess the materiality of the transaction or relationship and elevate the matter to the audit committee as appropriate. Any dealings with a related party must be conducted in such a way as to avoid preferential treatment and assure that the terms obtained by us are no less favorable than could be obtained from unrelated parties on an arm's-length basis. Directors and officers are not permitted to enter into, develop or continue any such material transaction or relationship without obtaining prior approval from the audit committee.

Michael K. Robinson, a member of our board of directors, serves as the CEO of Broadview. From time to time, Broadview purchases services from us in the ordinary course of business. In 2016, we provided wholesale services, specifically the resale of access on our network and unbundled network elements, as well as full end-to-end circuit platforms, to Broadview, totaling approximately \$1.0 million in the aggregate. This amount is less than 1% of Broadview's gross revenue for 2016. Such services were provided on an arm's-length basis.

### Director Independence

The board of directors considered transactions and relationships between each director or any member of his or her immediate family and the Company and its subsidiaries and affiliates. Our board of directors has determined that, other than Paul H. Sunu, all of our directors are independent under the criteria for independence set forth in the listing standards of the Nasdaq and accordingly are independent directors with no material relationship to us other than being a director or shareholder of FairPoint. Therefore, we satisfy the Nasdaq requirement that a majority of our board of directors be comprised of independent directors.

## ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The following table sets forth the aggregate fees paid or payable relating to services rendered for our fiscal years ended December 31, 2016 and 2015:

	Year Ended December 31, 2016	Year Ended December 31, 2015
Audit Fees (1)	\$ 1,070,000	\$ 1,985,000
Audit-related Fees (2)	—	135,000
All Other Fees (3)	—	2,000
<b>Total</b>	<b>\$ 1,070,000</b>	<b>\$ 2,122,000</b>

- (1) Audit fees include amounts related to annual financial statement audit work and quarterly financial statement reviews. These amounts also include the review of documents filed with the SEC, accounting consultations related to the annual audit and preparation of letters for underwriters and other requesting parties as well as fees associated with the joint proxy statement/prospectus in connection with the Merger.
- (2) Audit-related fees consist of amounts related to the Statement on Standards for Attestation Engagements No. 16 examination of our data center colocation services.
- (3) All Other Fees consist of amounts billed to us related to an online research tool for 2015.

*Audit Committee Pre-Approval Policy*

In accordance with our audit committee pre-approval policy, all audit and non-audit services performed for us by our independent accountants were pre-approved by our audit committee.

Our audit committee's pre-approval policy provides that our independent registered public accounting firm shall not provide services that have the potential to impair or appear to impair the independence of the audit role. The pre-approval policy requires our independent registered public accounting firm to provide an annual engagement letter to our audit committee outlining the scope of the audit services proposed to be performed during the fiscal year. Upon the audit committee's acceptance of and agreement with such engagement letter, the services within the scope of the proposed audit services shall be deemed pre-approved pursuant to the policy.

The pre-approval policy provides for categorical pre-approval of specified audit and permissible non-audit services and requires the specific pre-approval by the audit committee, prior to engagement, of such services, other than audit services covered by the annual engagement letter. In addition, services to be provided by our independent registered public accounting firm that are not within the category of pre-approved services must be approved by the audit committee prior to engagement, regardless of the service being requested or the dollar amount involved.

Requests or applications for services that require specific separate approval by the audit committee are required to be submitted to the audit committee by both management and the independent registered public accounting firm and must include a detailed description of the services to be provided and a joint statement confirming that the provision of the proposed services does not impair the independence of the independent registered public accounting firm.

The audit committee may delegate pre-approval authority to one or more of its members. The member or members to whom such authority is delegated shall report any pre-approval decisions to the audit committee at its next scheduled meeting. The audit committee is prohibited from delegating to management its responsibilities to pre-approve services to be performed by our independent registered public accounting firm.

**PART IV****ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES***(a) Financial Statements*

The financial statements filed as part of this Annual Report are listed in the index to the financial statements under "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Annual Report, which index to the financial statements is incorporated herein by reference.

*(b) Exhibits*

The exhibits filed as part of this Annual Report are listed in the index to exhibits found hereafter, which index to exhibits is incorporated herein by reference.

**ITEM 16. FORM 10-K SUMMARY**

None.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

FAIRPOINT COMMUNICATIONS, INC.

By: /s/ Paul H. Sunu Date: March 6, 2017  
Paul H. Sunu, Chief Executive Officer and Director

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By: /s/ Paul H. Sunu Date: March 6, 2017  
Paul H. Sunu, Chief Executive Officer and Director  
(Principal Executive Officer)

By: /s/ Karen D. Turner Date: March 6, 2017  
Karen D. Turner, Executive Vice President and Chief Financial Officer  
(Principal Financial Officer)

By: /s/ John T. Hogshire Date: March 6, 2017  
John T. Hogshire, Senior Vice President and Controller  
(Principal Accounting Officer)

By: /s/ Peter D. Aquino Date: March 6, 2017  
Peter D. Aquino, Director

By: /s/ Dennis J. Austin Date: March 6, 2017  
Dennis J. Austin, Director

By: /s/ Peter C. Gingold Date: March 6, 2017  
Peter C. Gingold, Director

By: /s/ Edward D. Horowitz Date: March 6, 2017  
Edward D. Horowitz, Chairman of the Board of Directors

By: /s/ Michael J. Mahoney Date: March 6, 2017  
Michael J. Mahoney, Director

By: /s/ Michael K. Robinson Date: March 6, 2017  
Michael K. Robinson, Director

By: /s/ David L. Treadwell Date: March 6, 2017  
David L. Treadwell, Director

By: /s/ Wayne Wilson

Date: March 6, 2017

Wayne Wilson, Director

## Exhibit Index

Exhibit No.	Description
2.1	Third Amended Joint Plan of Reorganization Under chapter 11 of title 11 of the United States Code.(1)
2.2	Agreement and Plan of Merger, dated as of December 3, 2016, by and among Consolidated Communications Holdings, Inc., FairPoint Communications, Inc. and Falcon Merger Sub, Inc. (19) **
2.3	First Amendment to Agreement and Plan of Merger, dated as of January 20, 2017, by and among Consolidated Communications Holdings, Inc., FairPoint Communications, Inc. and Falcon Merger Sub, Inc. *
3.1	Ninth Amended and Restated Certificate of Incorporation of FairPoint.(2)
3.2	Second Amended and Restated By-Laws of FairPoint.(2)
4.1	Warrant Agreement, dated as of January 24, 2011, by and between FairPoint and The Bank of New York Mellon.(3)
4.2	Specimen Stock Certificate.(2)
4.3	Specimen Warrant Certificate.(3)
4.4	Indenture, dated as of February 14, 2013, among FairPoint, the subsidiary guarantors party thereto, U.S. Bank National Association, as trustee, and U.S. Bank National Association, as collateral agent.(7)
4.5	First Supplemental Indenture, dated as of September 16, 2013, among FairPoint, the subsidiary guarantors party thereto and U.S. Bank National Association, as trustee.(10)
10.1	Security Agreement, dated as of February 14, 2013, among FairPoint, the subsidiary guarantors party thereto and U.S. Bank National Association, as collateral agent.(7)
10.2	Pledge Agreement, dated as of February 14, 2013, among FairPoint, the subsidiary guarantors party thereto and U.S. Bank National Association, as collateral agent.(7)
10.3	Credit Agreement, dated as of February 14, 2013, among FairPoint, the lenders party thereto from time to time and Morgan Stanley Senior Funding, Inc., as administrative agent and letter of credit issuer.(7)
10.4	Pledge Agreement, dated as of February 14, 2013, made by FairPoint and the subsidiary guarantors party thereto in favor of Morgan Stanley Senior Funding, Inc., as administrative agent.(7)
10.5	Security Agreement, dated as of February 14, 2013, among FairPoint, the subsidiary guarantors party thereto and Morgan Stanley Senior Funding, Inc., as administrative agent.(7)
10.6	Continuing Guaranty, dated as of February 14, 2013, made by the subsidiary guarantors party thereto in favor of Morgan Stanley Senior Funding, Inc., as administrative agent.(7)
10.7	Registration Rights Agreement, dated as of January 24, 2011, by and between FairPoint Communications, Inc. and Angelo, Gordon & Co., L.P.(3)
10.8	FairPoint Litigation Trust Agreement, dated as of January 24, 2011.(3)
10.9	Form of Director Indemnity Agreement.(4)
10.10	Amended and Restated Employment Agreement, dated as of April 9, 2013, by and between FairPoint and Paul H. Sunu.†(9)
10.11	First Amendment to April 9, 2013 Amended and Restated Employment Agreement, effective as of August 14, 2015, by and between FairPoint and Paul H. Sunu.†(15)
10.12	Employment Agreement, made and entered into as of January 22, 2013, by and between FairPoint and Ajay

Sabherwal.†(8)

10.13 First Amendment to January 22, 2013 Employment Agreement, effective as of August 14, 2015, by and between FairPoint and Ajay Sabherwal.†(15)

10.14 Second Amendment to January 22, 2013 Employment Agreement, effective as of May 16, 2016, by and between FairPoint and Ajay Sabherwal.†(17)

Exhibit No.	Description
10.15	Employment Agreement, made and entered into as of January 22, 2013, by and between FairPoint and Shirley J. Linn.†(8)
10.16	First Amendment to January 22, 2013 Employment Agreement, effective as of August 14, 2015, by and between FairPoint and Shirley J. Linn.†(15)
10.17	Employment Agreement, made and entered into as of January 22, 2013, by and between FairPoint and Peter G. Nixon.†(8)
10.18	First Amendment to January 22, 2013 Employment Agreement, effective as of August 14, 2015, by and between FairPoint and Peter G. Nixon.†(15)
10.19	Second Amendment to January 22, 2013 Employment Agreement, effective as of May 16, 2016, by and between FairPoint and Peter G. Nixon.†(17)
10.20	Employment Agreement, made and entered into as of November 15, 2012, by and between FairPoint and Anthony A. Tomae.†(8)
10.21	First Amendment to November 15, 2012 Employment Agreement, effective as of August 14, 2015, by and between FairPoint and Anthony A. Tomae.†(15)
10.22	Employment Agreement, made and entered into as of July 1, 2014, by and between FairPoint and John J. Lunny.†(12)
10.23	First Amendment to July 1, 2014 Employment Agreement, effective as of August 14, 2015, by and between FairPoint and John J. Lunny.†(15)
10.24	Second Amendment to July 1, 2014 Employment Agreement, effective as of November 21, 2016, by and between FairPoint and John J. Lunny.†*
10.25	Employment Agreement, made and entered into as of November 20, 2014, by and between FairPoint and Karen D. Turner.†(13)
10.26	First Amendment to November 20, 2014 Employment Agreement, effective as of August 14, 2015, by and between FairPoint and Karen D. Turner.†(15)
10.27	Second Amendment to November 20, 2014 Employment Agreement, effective as of November 21, 2016, by and between FairPoint and Karen D. Turner.†*
10.28	Employment Agreement, made and entered into as of August 10, 2015, by and between FairPoint and Steven G. Rush.†(15)
10.29	First Amendment to August 10, 2015 Employment Agreement, effective as of June 1, 2016, by and between FairPoint and Steven G. Rush.†(17)
10.30	Employment Agreement, made and entered into as of September 6, 2016, by and between FairPoint and Bruce F. Metge.†(18)
10.31	FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan.†(11)
10.32	Form of Non-Incentive Stock Option Award Agreement for directors relating to the FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan.†(11)
10.33	Form of Restricted Share Award Agreement for directors relating to the FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan.†(11)
10.34	Form of Stock Option Award Agreement for employees relating to the FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan.†(11)
10.35	Form of Restricted Share Award Agreement for employees relating to the FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan.†(11)

- 10.36 Form of FairPoint Communications, Inc. Performance Share Award Agreement for Performance Period Beginning January 1, 2015 for employees relating to the FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan.†(14)
- 10.37 Form of FairPoint Communications, Inc. Performance Share Award Agreement for Performance Period Beginning January 1, 2016 for employees relating to the FairPoint Communications, Inc. Amended and Restated 2010 Long Term Incentive Plan.†(16)

Exhibit No.	Description
10.38	FairPoint Communications, Inc. Incentive Recoupment Policy.†(6)
10.39	Form of FairPoint Communications, Inc. Severance in Connection With a Change in Control Agreement for certain employees, effective as of November 5, 2015.†(16)
10.40	Form of First Amendment to November 5, 2015 Severance in Connection With a Change in Control Agreement for certain employees, effective as of January 11, 2017.†*
11	Statement Regarding Computation of Per Share Earnings (included in the financial statements contained in this Annual Report).
14.1	FairPoint Code of Business Conduct and Ethics, as revised November 6, 2015.(16)
14.2	FairPoint Code of Ethics for Financial Professionals.(5)
21	Subsidiaries of FairPoint.*
23.1	Consent of BDO USA, LLP.*
23.2	Consent of Ernst & Young LLP.*
31.1	Certification as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
31.2	Certification as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
32.1	Certification required by 18 United States Code Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.‡
32.2	Certification required by 18 United States Code Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.‡
99.1	Order, dated January 13, 2011, Confirming Debtors' Third Amended Joint Plan of Reorganization Under chapter 11 of title 11 of the United States Code, dated as of December 29, 2010.(1)
99.2	FairPoint Insider Trading Policy, as revised October 30, 2014.(13)
101.INS	XBRL Instance Document.*
101.SCH	XBRL Taxonomy Extension Schema Document.*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.*
*	Filed herewith.
**	Pursuant to Item 601(b)(2) of Regulation S-K, the schedules to the Merger Agreement (identified therein) have been omitted from this Report and will be furnished supplementally to the SEC upon request.
†	Indicates a management contract or compensatory plan or arrangement.
‡	Pursuant to SEC Release No. 33-8238, this certification will be treated as "accompanying" this Annual Report on Form 10-K and not "filed" as part of such report for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of Section 18 of the Exchange Act and this certification will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.
(1)	Incorporated by reference to the Current Report on Form 8-K of FairPoint filed on January 14, 2011.
(2)	Incorporated by reference to the Registration Statement on Form 8-A of FairPoint filed on January 24, 2011.
(3)	Incorporated by reference to the Current Report on Form 8-K of FairPoint filed on January 25, 2011, Film Number 11544980.

- (4) Incorporated by reference to the Current Report on Form 8-K of FairPoint filed on January 25, 2011, Film Number 11544991.
- (5) Incorporated by reference to the Annual Report on Form 10-K of FairPoint for the year ended December 31, 2004.
- (6) Incorporated by reference to the Quarterly Report on Form 10-Q of FairPoint for the period ended March 31,

2012.

- (7) Incorporated by reference to the Current Report on Form 8-K of FairPoint filed on February 14, 2013.
- (8) Incorporated by reference to the Annual Report on Form 10-K of FairPoint for the year ended December 31, 2012.
- (9) Incorporated by reference to the Quarterly Report on Form 10-Q of FairPoint for the period ended March 31, 2013.
- (10) Incorporated by reference to the Quarterly Report on Form 10-Q of FairPoint for the period ended September 30, 2013.
- (11) Incorporated by reference to the Current Report on Form 8-K of FairPoint filed on May 12, 2014.
- (12) Incorporated by reference to the Quarterly Report on Form 10-Q of FairPoint for the period ended June 30, 2014.
- (13) Incorporated by reference to the Annual Report on Form 10-K of FairPoint for the year ended December 31, 2014.
- (14) Incorporated by reference to the Quarterly Report on Form 10-Q of FairPoint for the period ended March 31, 2015.
- (15) Incorporated by reference to the Quarterly Report on Form 10-Q of FairPoint for the period ended September 30, 2015.
- (16) Incorporated by reference to the Annual Report on Form 10-K of FairPoint for the year ended December 31, 2015.
- (17) Incorporated by reference to the Quarterly Report on Form 10-Q of FairPoint for the period ended June 30, 2016.
- (18) Incorporated by reference to the Quarterly Report on Form 10-Q of FairPoint for the period ended September 30, 2016.
- (19) Incorporated by reference to the Current Report on Form 8-K of FairPoint filed on December 5, 2016.

