

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2018

or

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

Commission File Number 000-51446



CONSOLIDATED COMMUNICATIONS HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

| | |
|--|--|
| <u>Delaware</u> (State or other jurisdiction of incorporation or organization) | <u>02-0636095</u> (I.R.S. Employer Identification No.) |
| <u>121 South 17th Street, Mattoon, Illinois</u> (Address of principal executive offices) | <u>61938-3987</u> (Zip Code) |

(217) 235-3311

(Registrant's telephone number, including area code)

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with 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

On April 30, 2018, the registrant had 71,252,576 shares of Common Stock outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CONSOLIDATED COMMUNICATIONS HOLDINGS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited; Amounts in thousands except per share amounts)

| | <u>Quarter Ended March 31,</u> | |
|--|--------------------------------|-------------------|
| | <u>2018</u> | <u>2017</u> |
| Net revenues | \$ 356,039 | \$ 169,935 |
| Operating expense: | | |
| Cost of services and products (exclusive of depreciation and amortization) | 152,916 | 71,032 |
| Selling, general and administrative expenses | 85,618 | 36,300 |
| Acquisition and other transaction costs | 731 | 1,329 |
| Depreciation and amortization | <u>107,899</u> | <u>42,195</u> |
| Income from operations | 8,875 | 19,079 |
| Other income (expense): | | |
| Interest expense, net of interest income | (32,716) | (29,671) |
| Investment income | 7,789 | 5,278 |
| Other, net | <u>606</u> | <u>(565)</u> |
| Loss before income taxes | (15,446) | (5,879) |
| Income tax benefit | <u>(4,248)</u> | <u>(2,174)</u> |
| Net loss | (11,198) | (3,705) |
| Less: net income (loss) attributable to noncontrolling interest | 100 | (20) |
| Net loss attributable to common shareholders | <u>\$ (11,298)</u> | <u>\$ (3,685)</u> |
| Net loss per basic and diluted common shares attributable to common shareholders | <u>\$ (0.16)</u> | <u>\$ (0.07)</u> |
| Dividends declared per common share | <u>\$ 0.39</u> | <u>\$ 0.39</u> |

See accompanying notes.

CONSOLIDATED COMMUNICATIONS HOLDINGS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited; Amounts in thousands)

| | <u>Quarter Ended March 31,</u> | |
|---|--------------------------------|-------------------|
| | <u>2018</u> | <u>2017</u> |
| Net loss | \$ (11,198) | \$ (3,705) |
| Pension and post-retirement obligations: | | |
| Amortization of actuarial losses and prior service credit to earnings, net of tax | 922 | 862 |
| Derivative instruments designated as cash flow hedges: | | |
| Change in fair value of derivatives, net of tax | 4,737 | (56) |
| Reclassification of realized loss to earnings, net of tax | 265 | 205 |
| Comprehensive loss | <u>(5,274)</u> | <u>(2,694)</u> |
| Less: comprehensive income (loss) attributable to noncontrolling interest | 100 | (20) |
| Total comprehensive loss attributable to common shareholders | <u>\$ (5,374)</u> | <u>\$ (2,674)</u> |

See accompanying notes.

CONSOLIDATED COMMUNICATIONS HOLDINGS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited; Amounts in thousands except share and per share amounts)

| | <u>March 31,</u> <u>2018</u> | <u>December 31,</u> <u>2017</u> |
|--|---------------------------------|------------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 11,140 | \$ 15,657 |
| Accounts receivable, net of allowance for doubtful accounts | 134,095 | 121,528 |
| Income tax receivable | 21,892 | 21,846 |
| Prepaid expenses and other current assets | 40,202 | 33,318 |
| Assets held for sale | <u>21,524</u> | <u>21,310</u> |
| Total current assets | 228,853 | 213,659 |
| Property, plant and equipment, net | 2,019,399 | 2,037,606 |
| Investments | 107,114 | 108,858 |
| Goodwill | 1,032,912 | 1,038,032 |
| Other intangible assets | 292,560 | 306,783 |
| Other assets | <u>28,026</u> | <u>14,188</u> |
| Total assets | <u>\$ 3,708,864</u> | <u>\$ 3,719,126</u> |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 21,014 | \$ 24,143 |
| Advance billings and customer deposits | 43,629 | 42,526 |
| Dividends payable | 27,602 | 27,418 |
| Accrued compensation | 53,689 | 49,770 |
| Accrued interest | 17,689 | 9,343 |
| Accrued expense | 77,331 | 72,041 |
| Current portion of long-term debt and capital lease obligations | 31,554 | 29,696 |
| Liabilities held for sale | <u>1,083</u> | <u>1,003</u> |
| Total current liabilities | 273,591 | 255,940 |
| Long-term debt and capital lease obligations | 2,317,398 | 2,311,514 |
| Deferred income taxes | 214,447 | 209,720 |
| Pension and other post-retirement obligations | 326,825 | 334,193 |
| Other long-term liabilities | <u>32,500</u> | <u>33,817</u> |
| Total liabilities | 3,164,761 | 3,145,184 |
| Commitments and contingencies (Note 11) | | |
| Shareholders' equity: | | |
| Common stock, par value \$0.01 per share; 100,000,000 shares authorized, 71,252,576 and 70,777,354 shares outstanding as of March 31, 2018 and December 31, 2017, respectively | 713 | 708 |
| Additional paid-in capital | 591,092 | 615,662 |
| Accumulated deficit | (11,298) | — |
| Accumulated other comprehensive loss, net | (42,159) | (48,083) |
| Noncontrolling interest | <u>5,755</u> | <u>5,655</u> |
| Total shareholders' equity | <u>544,103</u> | <u>573,942</u> |
| Total liabilities and shareholders' equity | <u>\$ 3,708,864</u> | <u>\$ 3,719,126</u> |

See accompanying notes.

CONSOLIDATED COMMUNICATIONS HOLDINGS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited; Amounts in thousands)

| | Three Months Ended March 31, | |
|--|-------------------------------------|------------------|
| | 2018 | 2017 |
| Net cash provided by operating activities | \$ 90,842 | \$ 51,718 |
| Cash flows from investing activities: | | |
| Purchases of property, plant and equipment, net | (60,808) | (29,025) |
| Proceeds from sale of assets | 144 | 43 |
| Distributions from investments | 233 | — |
| Net cash used in investing activities | <u>(60,431)</u> | <u>(28,982)</u> |
| Cash flows from financing activities: | | |
| Proceeds from issuance of long-term debt | 27,000 | 7,000 |
| Payment of capital lease obligations | (2,923) | (1,289) |
| Payment on long-term debt | (31,588) | (9,250) |
| Share repurchases for minimum tax withholding | — | (41) |
| Dividends on common stock | (27,417) | (19,604) |
| Net cash used in financing activities | <u>(34,928)</u> | <u>(23,184)</u> |
| Change in cash and cash equivalents | (4,517) | (448) |
| Cash and cash equivalents at beginning of period | 15,657 | 27,077 |
| Cash and cash equivalents at end of period | <u>\$ 11,140</u> | <u>\$ 26,629</u> |

See accompanying notes.

CONSOLIDATED COMMUNICATIONS HOLDINGS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business and Basis of Accounting

Consolidated Communications Holdings, Inc. (the “Company”, “we” or “our”) is a holding company with operating subsidiaries (collectively “Consolidated”) that provide communication solutions to consumer, commercial and carrier customers across a 24-state service area.

Leveraging our advanced fiber network spanning more than 36,000 fiber route miles, we offer a wide range of communications solutions including data, voice, video, managed services, cloud computing and wireless backhaul. As of March 31, 2018, we had approximately 955,000 voice connections, 785,000 data connections and 101,000 video connections.

In the opinion of management, the accompanying unaudited condensed consolidated balance sheets and related condensed consolidated statements of operations, comprehensive income (loss) and cash flows include all adjustments, consisting only of normal recurring items, necessary for their fair presentation in conformity with accounting principles generally accepted in the United States (“US GAAP” or “GAAP”) for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with US GAAP have been condensed or omitted pursuant to such SEC rules and regulations and accounting principles applicable for interim periods. Events subsequent to the balance sheet date have been evaluated for inclusion in the accompanying condensed consolidated financial statements through the date of issuance. Management believes that the disclosures made are adequate to make the information presented not misleading. Interim results are not necessarily indicative of results for a full year. The information presented in this Form 10-Q should be read in conjunction with Management’s Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and the accompanying notes to the financial statements (“Notes”) thereto included in our 2017 Annual Report on Form 10-K filed with the SEC.

Recent Business Developments

On July 3, 2017, we completed our acquisition of FairPoint Communications, Inc. (“FairPoint”), pursuant to the terms of a definitive agreement and plan of merger (as amended, the “Merger Agreement”) and acquired all of the issued and outstanding shares of FairPoint in exchange for shares of our common stock (the “Merger”). As a result of the Merger, FairPoint became a wholly owned subsidiary of the Company. The financial results for FairPoint have been included in our condensed consolidated financial statements as of the acquisition date. For a more complete discussion of the transaction, refer to Note 2.

Revenue Recognition

Effective January 1, 2018, we adopted ASU No. 2014-09 (“ASU 2014-09”, “ASC 606”, or the “new standard”), *Revenue from Contracts with Customers*, using the modified retrospective method for open contracts. Results for reporting periods beginning after January 1, 2018 are presented under ASC 606, while prior period amounts are not adjusted and continue to be reported in accordance with our historic accounting practices under ASC 605 (“legacy GAAP”).

The adoption of the new standard did not result in a material impact to our systems, processes or internal controls. The largest impact of the adoption of the new standard is related to the treatment of contract acquisition costs, which were previously expensed as incurred; however, under the new standard, these costs are now deferred and amortized over the expected customer life. The adoption also resulted in additional disclosures around the nature and timing of the Company’s performance obligations, deferred revenue contract liabilities and deferred contract cost assets, as well as practical expedients used by the Company in applying the new five-step revenue model. During the first quarter of 2018, we recorded a cumulative effect adjustment of \$2.9 million to opening retained earnings related to the adoption.

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Nature of Contracts with Customers

Our revenue contracts with customers may include a promise or promises to deliver services such as broadband, video or voice services. Promised services are considered distinct as the customer can benefit from the services either on their own or together with other resources that are readily available to the customer and the Company's promise to transfer service to the customer is separately identifiable from other promises in the contract. The Company accounts for services as separate performance obligations. Each service is considered a single performance obligation as it is providing a series of distinct services that are substantially the same and have the same pattern of transfer.

The transaction price is determined at contract inception and reflects the amount of consideration to which we expect to be entitled in exchange for transferring service to the customer. This amount is generally equal to the market price of the services promised in the contract and may include promotional discounts. The transaction price excludes amounts collected on behalf of third parties such as sales taxes and regulatory fees. Conversely, nonrefundable up-front fees, such as service activation and set-up fees, are included in the transaction price. In determining the transaction price, we consider our enforceable rights and obligations within the contract. We do not consider the possibility of a contract being cancelled, renewed or modified, which is consistent with ASC 606-10-32-4.

The transaction price is allocated to each performance obligation based on the standalone selling price of the service, net of the related discount, as applicable.

Revenue is recognized when or as performance obligations are satisfied by transferring service to the customer as described below.

Disaggregation of Revenue

The following table summarizes revenue from contracts with customers for the quarters ended March 31, 2018 and 2017:

| <i>(In thousands)</i> | Quarter Ended | |
|---|-------------------|-------------------|
| | March 31, | |
| | 2018 | 2017 |
| Operating Revenues | | |
| Commercial and carrier: | | |
| Data and transport services (includes VoIP) | \$ 86,025 | \$ 50,904 |
| Voice services | 52,161 | 22,026 |
| Other | 11,863 | 3,902 |
| | <u>150,049</u> | <u>76,832</u> |
| Consumer: | | |
| Broadband (VoIP and Data) | 63,111 | 28,393 |
| Video services | 22,834 | 23,104 |
| Voice services | 52,062 | 13,042 |
| | <u>138,007</u> | <u>64,539</u> |
| Subsidies | 25,255 | 10,572 |
| Network access | 39,715 | 14,553 |
| Other products and services | 3,013 | 3,439 |
| Total operating revenues | <u>\$ 356,039</u> | <u>\$ 169,935</u> |

Service revenue is recognized over time, consistent with the transfer of service, as the customer simultaneously receives and consumes the benefits provided by the Company's performance as the Company performs.

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Contract Assets and Liabilities

The following table provides information about receivables, contract assets and contract liabilities from our revenue contracts with customers:

| <i>(In thousands)</i> | Quarter Ended March 31, 2018 | At Adoption |
|--------------------------|------------------------------------|----------------|
| Accounts receivable, net | \$ 134,496 | \$ 121,745 |
| Contracts assets | 4,527 | 1,804 |
| Contracts liabilities | 47,269 | 46,368 |

Contract assets include costs that are incremental to the acquisition of a contract. Incremental costs are those that result directly from obtaining a contract or costs that would not have been incurred if the contract had not been obtained, which primarily relate to sales commissions. These costs are deferred and amortized over the expected customer life. We determined that the expected customer life is the expected period of benefit as the commission on the renewal contract is not commensurate with the commission on the initial contract. During the quarter ended March 31, 2018, the Company recognized expense of \$0.4 million related to deferred contract acquisition costs.

Contract liabilities include deferred revenues related to advanced payments for services and nonrefundable, upfront service activation and set-up fees, which under the new standard are generally deferred and amortized over the expected customer life as the option to renew without paying an upfront fee provides the customer with a material right. During the quarter ended March 31, 2018, the Company recognized revenue of \$87.3 million related to deferred revenues.

A receivable is recognized in the period the Company provides goods or services when the Company's right to consideration is unconditional. Payment terms on invoiced amounts are generally 30-60 days.

Performance Obligations

ASC 606 requires that the Company disclose the aggregate amount of the transaction price that is allocated to remaining performance obligations that are unsatisfied as of March 31, 2018. The guidance provides certain practical expedients that limit this requirement. The service revenue contracts of the Company meet the following practical expedients provided by ASC 606:

1. The performance obligation is part of a contract that has an original expected duration of one year or less.
2. Revenue is recognized from the satisfaction of the performance obligations in the amount billable to the customer in accordance with ASC 606-10-55-18.

Financial Statement Impact of Adopting ASC 606

As described above, the change in accounting for contract acquisition costs was the largest impact to the Company upon adoption of ASC 606. On an ongoing basis, a significant amount of commission costs, which were historically expensed as incurred, will now be deferred and amortized over the expected customer life under the new standard. The accretive benefit to operating income anticipated in 2018 is expected to moderate in future years as the basis of the amortization builds. For the quarter ended March 31, 2018, we recognized commission expense of \$0.4 million under the new standard as compared to \$3.1 million for the same period under legacy GAAP.

Recent Accounting Pronouncements

Effective January 1, 2018, we adopted ASU 2014-09 (also known as ASC 606). 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 disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. For additional information on the new standard and the impact to our results of operations, refer to the Revenue Recognition section above.

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Effective January 1, 2018, we adopted ASU No. 2017-09 (“ASU 2017-09”), *Scope of Modification Accounting*. ASU 2017-09 clarifies the modification accounting guidance for stock compensation included in Topic 718, Compensation – Stock Compensation. ASU 2017-09 provides guidance about which changes to the terms or conditions of a share-based payment award must be accounted for as a modification under Topic 718. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements and related disclosures.

Effective January 1, 2018, we adopted ASU No. 2017-07 (“ASU 2017-07”), *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. ASU 2017-07 requires presentation of the service cost component of net periodic benefit cost within the same income statement line item as other compensation costs arising from services rendered by relevant employees during the period, and presentation of the other cost components of net periodic benefit cost separately and outside of the income from operations subtotal. In addition, only the service cost component is eligible for capitalization. We adopted ASU 2017-07 prospectively for the capitalization of the service cost component of the net periodic benefit cost. ASU 2017-07 was applied retrospectively using the practical expedient for the presentation of the other components of net periodic benefit cost in the statement of operations and as a result, we reclassified \$0.4 million of expense from cost of services and products and \$0.1 million of expense from selling, general and administrative expenses into other, net within non-operating income (expense) for the quarter ended March 31, 2017. See Note 9 for the amount of each component of net periodic pension and post-retirement benefit costs.

Effective January 1, 2018, we adopted ASU No. 2017-05 (“ASU 2017-05”), *Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets*. ASU 2017-05 provides additional guidance to (i) clarify the scope for recognizing gains and losses from the transfer of nonfinancial assets and in substance nonfinancial assets in contracts with non-customers, and (ii) clarify the accounting for partial sales of nonfinancial assets. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements and related disclosures.

Effective January 1, 2018, we adopted ASU No. 2017-04 (“ASU 2017-04”), *Simplifying the Accounting for Goodwill Impairment*. ASU 2017-04 eliminates Step 2 from the goodwill impairment test. Under the updated guidance, the goodwill impairment test will be performed by comparing the fair value of a reporting unit with its carrying amount and an impairment charge will be recognized for the amount by which the carrying amount exceeds the reporting unit’s fair value. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements and related disclosures and is not expected to have a material impact on our testing of goodwill.

Effective January 1, 2018, we adopted ASU No. 2017-01 (“ASU 2017-01”), *Clarifying the Definition of a Business*. ASU 2017-01 clarifies the definition of a business and establishes a screening process to determine whether an integrated set of assets and activities acquired is deemed the acquisition of a business or the acquisition of assets. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements and related disclosures.

Effective January 1, 2018, we adopted ASU No. 2016-16 (“ASU 2016-16”), *Intra-Entity Transfers of Assets Other Than Inventory*. ASU 2016-16 eliminates the existing exception prohibiting the recognition of the income tax consequences for intra-entity asset transfers until the asset has been sold to an outside party. Under ASU 2016-16, entities will be required to recognize the income tax consequences of intra-entity asset transfers other than inventory when the transfer occurs. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements and related disclosures.

Effective January 1, 2018, we adopted ASU No. 2016-15 (“ASU 2016-15”), *Classification of Certain Cash Receipts and Cash Payments*. ASU 2016-15 provides guidance concerning the classification of certain cash receipts and cash payments in the statement of cash flows. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements and related disclosures.

In February 2018, the Financial Accounting Standards Board (the “FASB”) issued ASU No. 2018-02 (“ASU 2018-02”), *Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. ASU 2018-02 provides an option to allow reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017. The new guidance is effective for annual and interim periods beginning after December 15, 2018 with early adoption permitted. We are currently evaluating the impact this update will have on our condensed consolidated financial statements and related disclosures.

In August 2017, the FASB issued ASU Update No. 2017-12 (“ASU 2017-12”), *Targeted Improvements to Accounting for Hedging Activities*. ASU 2017-12 amends current guidance on accounting for hedges mainly to align more closely an entity’s risk management activities and financial reporting relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. In addition, amendments in ASU 2017-12 simplify the application of hedge accounting by allowing more time to prepare hedge documentation and allowing effectiveness assessments to be performed on a qualitative basis after hedge inception. The new guidance is effective for annual and interim periods beginning after December 15, 2018 with early adoption permitted. We are currently evaluating the impact this update will have on our condensed consolidated financial statements and related disclosures.

In June 2016, the FASB issued ASU No. 2016-13 (“ASU 2016-13”), *Measurement of Credit Losses on Financial Instruments*. ASU 2016-13 establishes the new “current expected credit loss” model for measuring and recognizing credit losses on financial assets based on relevant information about past events, including historical experience, current conditions and reasonable and supportable forecasts. The new guidance is effective on a modified retrospective basis for annual and interim periods beginning after December 15, 2019, with early adoption permitted for annual and interim periods beginning after December 15, 2018. We have not yet made a decision on the timing of adoption and are currently evaluating the impact this update will have on our condensed consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU No. 2016-02 (“ASU 2016-02”), *Leases*. ASU 2016-02 establishes a new lease accounting model for leases. Lessees will be required to recognize most leases on their balance sheets but lease expense will be recognized on the income statement in a manner similar to existing requirements. ASU 2016-02 is effective on a modified retrospective basis for annual and interim periods beginning after December 15, 2018, with early adoption permitted. We are currently evaluating the population of our leases and anticipate that most of our operating lease commitments will be recognized on our consolidated balance sheets. We plan to adopt this update effective January 1, 2019 and are continuing to assess the potential impact of this update on our condensed consolidated financial statements and related disclosures.

Reclassifications

Certain amounts in our 2017 condensed consolidated financial statements have been reclassified to conform to the current year presentation. In accordance with the adoption of ASU 2017-07, as described above, certain components of net periodic benefit cost were reclassified from operating expense to non-operating income (expense) in our condensed consolidated statement of operations.

2. ACQUISITIONS AND DIVESTITURES

Acquisitions

FairPoint Communications, Inc.

On July 3, 2017, we completed the Merger with FairPoint and acquired all of the issued and outstanding shares of FairPoint in exchange for shares of our common stock. As a result, FairPoint became a wholly-owned subsidiary of the Company. FairPoint is an advanced communications provider to business, wholesale and residential customers within its service territory, which spans across 17 states. FairPoint owns and operates a robust fiber-based network with more than 22,000 route miles of fiber, including 17,000 route miles of fiber in northern New England. The acquisition reflects our strategy to diversify revenue and cash flows amongst multiple products and to expand our network to new markets.

At the effective time of the Merger, each share of common stock of FairPoint issued and outstanding immediately prior to the effective time of the Merger converted into and became the right to receive 0.7300 shares of common stock of Consolidated and cash in lieu of fractional shares, pursuant to the terms of the Merger Agreement. Based on the closing price of our common stock on the last complete trading day prior to the effective date of the Merger, the total value of the consideration to be exchanged was \$431.0 million, exclusive of debt of approximately \$919.3 million. On the date of the Merger, we issued an approximate aggregate total of 20.1 million shares of our common stock to the former FairPoint stockholders and we assumed approximately 2,615,153 outstanding warrants, each eligible to purchase one share of the

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Company's common stock at an exercise price of \$66.86 per share, subject to adjustment in accordance with the warrant agreement. On January 24, 2018, all of the warrants expired in accordance with their terms without being exercised.

In connection with the Merger, we secured committed debt financing in December 2016 through a \$935.0 million incremental term loan facility, as described in Note 6, that, in addition to cash on hand and other sources of liquidity, was used to repay certain existing indebtedness of FairPoint and to pay the fees and expenses in connection with the Merger.

The acquisition was accounted for in accordance with the acquisition method of accounting for business combinations. The tangible and intangible assets acquired and liabilities assumed were recorded at their estimated fair values as of the date of the acquisition.

The preliminary estimated fair value of the tangible and intangible assets acquired and liabilities assumed are as follows:

| <i>(In thousands)</i> | |
|---|--------------|
| Cash and cash equivalents | \$ 56,980 |
| Accounts receivable | 71,225 |
| Other current assets | 22,012 |
| Assets held for sale | 21,417 |
| Property, plant and equipment | 1,053,562 |
| Intangible assets | 303,180 |
| Other long-term assets | 2,685 |
| Total assets acquired | 1,531,061 |
| Current liabilities | 123,047 |
| Liabilities held for sale | 1,016 |
| Pension and other post-retirement obligations | 219,298 |
| Deferred income taxes | 97,500 |
| Other long-term liabilities | 15,916 |
| Total liabilities assumed | 456,777 |
| Net fair value of assets acquired | 1,074,284 |
| Goodwill | 276,034 |
| Total consideration transferred | \$ 1,350,318 |

The fair values of the assets acquired and liabilities assumed are based on a preliminary valuation, which is subject to change within the measurement period. Upon completion of the final fair value assessment, the fair values of the net assets acquired may differ materially from the preliminary assessment. We are in the process of finalizing the valuation of the net assets acquired, most notably, the valuation of property, plant and equipment, intangible assets, pension and other post-retirement obligations and deferred income taxes. Any changes to the initial estimates of the fair value of the assets acquired and liabilities assumed will be recorded to those assets and liabilities and residual amounts will be allocated to goodwill.

Goodwill recognized from the acquisition primarily relates to the expected contributions of the entity to the overall corporate strategy and the synergies expected to be realized from the acquisition. Amortization of goodwill is not deductible for income tax purposes.

Based on the preliminary valuation analysis, the identifiable intangible assets acquired consisted of customer relationships of \$300.3 million, tradenames of \$1.1 million and non-compete agreements of \$1.8 million. The customer relationships are being amortized using an accelerated amortization method over their preliminary estimated useful lives of seven to eleven years depending on the nature of the customer. The tradenames and non-compete agreements are amortized using the straight-line method over their preliminary estimated useful lives of six months and one year, respectively.

During the quarter ended March 31, 2018, we made certain adjustments to the fair value of the identifiable assets acquired and liabilities assumed which resulted in an increase in accounts receivable of \$8.4 million and deferred income taxes of \$3.3 million. The net impact of the adjustments increased net assets acquired and reduced goodwill by \$5.1 million. The increase in accounts receivable during the quarter ended March 31, 2018 represents the recognition of a contingent asset arising from a pre-acquisition gain contingency related to the approval on April 19, 2018 of our petition filed with the

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Federal Communications Commission (“FCC”) regarding frozen local switching support (“LSS”) for the period from January 1, 2015 through the FairPoint acquisition date. For a more complete discussion of the LSS petition filed with the FCC, refer to Note 11.

As discussed in the “Divestitures” section below, we have committed to a formal plan to sell certain assets of FairPoint and these assets have been classified as held for sale at the acquisition date. In connection with the classification as assets held for sale at the acquisition date, the carrying value of these assets was recorded at their estimated fair value of approximately \$20.4 million, which was determined based on the estimated selling price less costs to sell.

Unaudited Pro Forma Results

The following unaudited pro forma information presents our results of operations as if the acquisition of FairPoint occurred on January 1, 2016. The adjustments to arrive at the pro forma information below included adjustments for depreciation and amortization on the acquired tangible and intangible assets acquired, interest expense on the debt incurred to finance the acquisition and to repay certain existing indebtedness of FairPoint, and the exclusion of certain acquisition related costs. Shares used to calculate the basic and diluted earnings per share were adjusted to reflect the additional shares of common stock issued to fund the acquisition.

| | Quarter Ended |
|--|---------------|
| | March 31, |
| | 2017 |
| <i>(Unaudited; in thousands, except per share amounts)</i> | |
| Operating revenues | \$ 371,843 |
| Income from operations | \$ 11,132 |
| Net loss | \$ (8,548) |
| Less: net loss attributable to noncontrolling interest | (20) |
| Net loss attributable to common stockholders | \$ (8,528) |
| Net loss per common share-basic and diluted | \$ (0.12) |

Transaction costs related to the acquisition of FairPoint were \$1.5 million during the quarter ended March 31, 2017 which are included in acquisition and other transaction costs in the condensed consolidated statements of operations. These costs are considered to be non-recurring in nature and therefore pro forma adjustments have been made to exclude these costs from the pro forma results of operations.

The pro forma information does not purport to present the actual results that would have resulted if the acquisition had in fact occurred at the beginning of the fiscal periods presented, nor does the information project results for any future period. The pro forma information does not include the impact of any future cost savings or synergies that may be achieved as a result of the acquisition.

Divestitures

In August 2017, we entered into a letter of intent to sell our subsidiaries Peoples Mutual Telephone Company and Peoples Mutual Long Distance Company, (collectively “Peoples”), which were acquired as part of the acquisition of FairPoint. Peoples operates as a local exchange carrier in Virginia and provides telecommunications services to residential and business customers. In November 2017, the Company entered into an agreement to sell all of the issued and outstanding stock of Peoples in exchange for cash of approximately \$21.0 million, subject to certain contractual adjustments. The closing of the transaction is subject to certain regulatory approvals, which are expected to be completed in the second quarter of 2018.

As of the FairPoint acquisition date, the net assets to be sold have been classified as held for sale in the consolidated balance sheet. The expected sale of these assets has not been reported as discontinued operations in the condensed consolidated statements of operations as the annual revenues of these operations is less than 1% of the consolidated operating revenues. The estimated fair value of the net assets held for sale was determined based on the estimated selling price less costs to sell and was classified as Level 2 within the fair value hierarchy at March 31, 2018 and December 31, 2017.

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The classes of assets and liabilities to be sold and classified as held for sale consisted of the following:

| <i>(In thousands)</i> | March 31, 2018 | December 31, 2017 |
|-------------------------------|-------------------|----------------------|
| Current assets | \$ 401 | \$ 227 |
| Property, plant and equipment | 4,294 | 4,254 |
| Goodwill | 16,829 | 16,829 |
| Total assets | <u>\$ 21,524</u> | <u>\$ 21,310</u> |
| Current liabilities | \$ 935 | \$ 701 |
| Deferred taxes | 148 | 302 |
| Total liabilities | <u>\$ 1,083</u> | <u>\$ 1,003</u> |

3. EARNINGS (LOSS) PER SHARE

Basic and diluted earnings (loss) per common share ("EPS") are computed using the two-class method, which is an earnings allocation method that determines EPS for each class of common stock and participating securities considering dividends declared and participation rights in undistributed earnings. The Company's restricted stock awards are considered participating securities because holders are entitled to receive non-forfeitable dividends during the vesting term.

The potentially dilutive impact of the Company's restricted stock awards is determined using the treasury stock method. Under the treasury stock method, if the average market price during the period exceeds the exercise price, these instruments are treated as if they had been exercised with the proceeds of exercise used to repurchase common stock at the average market price during the period. Any incremental difference between the assumed number of shares issued and repurchased is included in the diluted share computation.

Diluted EPS includes securities that could potentially dilute basic EPS during a reporting period. Dilutive securities are not included in the computation of loss per share when a company reports a net loss from continuing operations as the impact would be anti-dilutive.

The computation of basic and diluted EPS attributable to common shareholders computed using the two-class method is as follows:

| <i>(In thousands, except per share amounts)</i> | Quarter Ended March 31, | |
|--|----------------------------|-------------------|
| | 2018 | 2017 |
| Net loss | \$ (11,198) | \$ (3,705) |
| Less: net income (loss) attributable to noncontrolling interest | 100 | (20) |
| Loss attributable to common shareholders before allocation of earnings to participating securities | (11,298) | (3,685) |
| Less: earnings allocated to participating securities | 221 | 49 |
| Net loss attributable to common shareholders, after earnings allocated to participating securities | <u>\$ (11,519)</u> | <u>\$ (3,734)</u> |
| Weighted-average number of common shares outstanding | <u>70,598</u> | <u>50,410</u> |
| Net loss per common share attributable to common shareholders - basic and diluted | <u>\$ (0.16)</u> | <u>\$ (0.07)</u> |

Diluted EPS attributable to common shareholders for each of the quarters ended March 31, 2018 and 2017 excludes 0.3 million and 0.2 million potential common shares, respectively, that could be issued under our share-based compensation plan, because the inclusion of the potential common shares would have an antidilutive effect.

4. INVESTMENTS

Our investments are as follows:

| <i>(In thousands)</i> | March 31, 2018 | December 31, 2017 |
|---|-------------------|----------------------|
| Cash surrender value of life insurance policies | \$ 2,404 | \$ 2,272 |
| Investments at cost: | | |
| GTE Mobilnet of South Texas Limited Partnership (2.34% interest) | 21,450 | 21,450 |
| Pittsburgh SMSA Limited Partnership (3.60% interest) | 22,950 | 22,950 |
| CoBank, ACB Stock | 9,097 | 9,105 |
| Other | 336 | 343 |
| Equity method investments: | | |
| GTE Mobilnet of Texas RSA #17 Limited Partnership (20.51% interest) | 16,649 | 17,375 |
| Pennsylvania RSA 6(I) Limited Partnership (16.67% interest) | 6,895 | 7,300 |
| Pennsylvania RSA 6(II) Limited Partnership (23.67% interest) | 27,333 | 28,063 |
| Totals | \$ 107,114 | \$ 108,858 |

Investments at Cost

We own 2.34% of GTE Mobilnet of South Texas Limited Partnership (the “Mobilnet South Partnership”). The principal activity of the Mobilnet South Partnership is providing cellular service in the Houston, Galveston and Beaumont, Texas metropolitan areas. We also own 3.60% of Pittsburgh SMSA Limited Partnership, which provides cellular service in and around the Pittsburgh metropolitan area. Because of our limited influence over these partnerships, we account for these investments at our initial cost less any impairment because fair value is not readily available for these investments. No factors of impairment existed for any of the investments during the quarters ended March 31, 2018 or 2017. For these investments, we adjust the carrying value for any purchases or sales of our ownership interests. We record distributions received from these investments as investment income in non-operating income (expense). For the quarters ended March 31, 2018 and 2017, we received cash distributions from these partnerships totaling \$3.0 million and \$1.6 million, respectively.

CoBank, ACB (“CoBank”) is a cooperative bank owned by its customers. On an annual basis, CoBank distributes patronage in the form of cash and stock in the cooperative based on the Company’s outstanding loan balance with CoBank, which has traditionally been a significant lender in the Company’s credit facility. The investment in CoBank represents the accumulation of the equity patronage paid by CoBank to the Company.

Equity Method

We own 20.51% of GTE Mobilnet of Texas RSA #17 Limited Partnership (“RSA #17”), 16.67% of Pennsylvania RSA 6(I) Limited Partnership (“RSA 6(I)”) and 23.67% of Pennsylvania RSA 6(II) Limited Partnership (“RSA 6(II)”). RSA #17 provides cellular service to a limited rural area in Texas. RSA 6(I) and RSA 6(II) provide cellular service in and around our Pennsylvania service territory. Because we have significant influence over the operating and financial policies of these three entities, we account for the investments using the equity method. For the quarters ended March 31, 2018 and 2017, we received cash distributions from these partnerships totaling \$6.5 million and \$4.0 million, respectively.

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The unaudited results of operations and financial position of our equity investment in RSA #17, which was deemed significant for the periods, is summarized below:

| <i>(In thousands)</i> | Quarter Ended March 31, | |
|-------------------------|----------------------------|-----------|
| | 2018 | 2017 |
| Total revenues | \$ 33,284 | \$ 32,503 |
| Income from operations | 10,993 | 10,168 |
| Net income before taxes | 10,708 | 9,825 |
| Net income | 10,708 | 9,825 |

| <i>(In thousands)</i> | March 31, | December 31, |
|-------------------------|-----------|--------------|
| | 2018 | 2017 |
| Current assets | \$ 27,070 | \$ 37,439 |
| Non-current assets | 52,867 | 52,732 |
| Current liabilities | 9,129 | 9,816 |
| Non-current liabilities | 40,718 | 40,785 |
| Partnership equity | 30,090 | 39,570 |

5. FAIR VALUE MEASUREMENTS

Our derivative instruments related to interest rate swap agreements are required to be measured at fair value on a recurring basis. The fair values of the interest rate swaps are determined using valuation models and are categorized within Level 2 of the fair value hierarchy as the valuation inputs are based on quoted prices and observable market data of similar instruments. See Note 7 for further discussion regarding our interest rate swap agreements.

Our interest rate swap agreements measured at fair value on a recurring basis as of March 31, 2018 and December 31, 2017 were as follows:

| <i>(In thousands)</i> | Total | As of March 31, 2018 | | |
|--|----------|--|---|--|
| | | Quoted Prices In Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Current interest rate swap assets | \$ 694 | \$ — | \$ 694 | \$ — |
| Long-term interest rate swap assets | 6,479 | — | 6,479 | — |
| Long-term interest rate swap liabilities | (3,284) | — | (3,284) | — |
| Total | \$ 3,889 | \$ — | \$ 3,889 | \$ — |

| <i>(In thousands)</i> | Total | As of December 31, 2017 | | |
|--|----------|--|---|--|
| | | Quoted Prices In Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Long-term interest rate swap assets | \$ 1,256 | \$ — | \$ 1,256 | \$ — |
| Current interest rate swap liabilities | (27) | — | (27) | — |
| Long-term interest rate swap liabilities | (1,761) | — | (1,761) | — |
| Total | \$ (532) | \$ — | \$ (532) | \$ — |

We have not elected the fair value option for any of our financial assets or liabilities. The carrying value of other financial instruments, including cash, accounts receivable, accounts payable and accrued liabilities approximate fair value due to

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their short maturities. The following table presents the other financial instruments that are not carried at fair value but which require fair value disclosure as of March 31, 2018 and December 31, 2017.

| <i>(In thousands)</i> | As of March 31, 2018 | | As of December 31, 2017 | |
|--|----------------------|--------------|-------------------------|--------------|
| | Carrying Value | Fair Value | Carrying Value | Fair Value |
| Investments, equity basis | \$ 50,877 | n/a | \$ 52,738 | n/a |
| Investments, at cost | \$ 53,833 | n/a | \$ 53,848 | n/a |
| Long-term debt, excluding capital leases | \$ 2,327,311 | \$ 2,252,569 | \$ 2,331,400 | \$ 2,253,545 |

Cost & Equity Method Investments

Our investments as of March 31, 2018 and December 31, 2017 accounted for at cost and under the equity method consisted primarily of minority positions in various cellular telephone limited partnerships and our investment in CoBank. It is impracticable to determine the fair value of these investments.

Long-term Debt

The fair value of our senior notes was based on quoted market prices, and the fair value of borrowings under our credit facility was determined using current market rates for similar types of borrowing arrangements. We have categorized the long-term debt as Level 2 within the fair value hierarchy.

6. LONG-TERM DEBT

Long-term debt, presented net of unamortized discounts, consisted of the following:

| <i>(In thousands)</i> | March 31, 2018 | December 31, 2017 |
|---|---------------------|----------------------|
| Senior secured credit facility: | | |
| Term loans, net of discounts of \$8,010 and \$8,344 at March 31, 2018 and December 31, 2017, respectively | \$ 1,808,815 | \$ 1,813,069 |
| Revolving loan | 22,000 | 22,000 |
| 6.50% Senior notes due 2022, net of discount of \$3,504 and \$3,669 at March 31, 2018 and December 31, 2017, respectively | 496,496 | 496,331 |
| Capital leases | 35,058 | 23,890 |
| | 2,362,369 | 2,355,290 |
| Less: current portion of long-term debt and capital leases | (31,554) | (29,696) |
| Less: deferred debt issuance costs | (13,417) | (14,080) |
| Total long-term debt | <u>\$ 2,317,398</u> | <u>\$ 2,311,514</u> |

Credit Agreement

In October 2016, the Company, through certain of its wholly owned subsidiaries, entered into a Third Amended and Restated Credit Agreement with various financial institutions (as amended, the "Credit Agreement"). The Credit Agreement consists of a \$110.0 million revolving credit facility, an initial term loan in the aggregate amount of \$900.0 million (the "Initial Term Loan") and an incremental term loan in the aggregate amount of \$935.0 million (the "Incremental Term Loan"), collectively (the "Term Loans"). The Incremental Term Loan was issued on July 3, 2017 upon completion of the FairPoint Merger, as described below. The Credit Agreement also includes an incremental loan facility which provides the ability to borrow, subject to certain terms and conditions, incremental loans in an aggregate amount of up to the greater of (a) \$300.0 million and (b) an amount which would cause its senior secured leverage ratio not to exceed 3.00:1.00 (the "Incremental Facility"). Borrowings under the Credit Agreement are secured by substantially all of the assets of the Company and its subsidiaries, including certain of the FairPoint subsidiaries acquired in the Merger, with the exception of Consolidated Communications of Illinois Company and our majority-owned subsidiary, East Texas Fiber Line Incorporated.

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The Initial Term Loan was issued in an original aggregate principal amount of \$900.0 million with a maturity date of October 5, 2023, but is subject to earlier maturity on March 31, 2022 if the Company's unsecured Senior Notes due in October 2022 are not repaid in full or redeemed in full on or prior to March 31, 2022. The Initial Term Loan contains an original issuance discount of 0.25% or \$2.3 million, which is being amortized over the term of the loan. The Initial Term Loan requires quarterly principal payments of \$2.25 million and has an interest rate of 3.00% plus the London Interbank Offered Rate ("LIBOR") subject to a 1.00% LIBOR floor.

In connection with the execution of the Merger Agreement, in December 2016, the Company entered into two amendments to its Credit Agreement to secure committed financing related to the acquisition of FairPoint. On December 14, 2016, we entered into Amendment No. 1 to the Credit Agreement and on December 21, 2016, the Company entered into Amendment No. 2 to the Credit Agreement, pursuant to which a syndicate of lenders agreed to provide an incremental term loan in an aggregate principal amount of up to \$935.0 million under the Credit Agreement, subject to the satisfaction of certain conditions. The Incremental Term Loan was made pursuant to the Incremental Facility set forth in the Credit Agreement. Fees of \$2.5 million paid to the lenders in connection with Amendment No. 1 are reflected as an additional discount on the Initial Term Loan and are being amortized over the term of the debt as interest expense. Ticking fees accrued on the incremental term loan commitments from January 15, 2017 through the July 3, 2017 Merger closing date at a rate of 3.00% plus LIBOR subject to a 1.00% LIBOR floor and became due and payable on the closing date. In connection with entering into the committed financing, commitment fees of \$14.0 million were capitalized in December 2016 and were amortized to interest expense over the term of the commitment period through July 2017.

On July 3, 2017, the Merger with FairPoint was completed and the net proceeds from the incurrence of the Incremental Term Loan were used, in part, to repay and redeem certain existing indebtedness of FairPoint and to pay certain fees and expenses in connection with the Merger and the related financing. The Incremental Term Loan included an original issue discount of 0.50% and has the same maturity date and interest rate as the Initial Term Loan. The Incremental Term Loan requires quarterly principal payments of \$2.34 million which began in December 2017.

In addition, effective contemporaneously with the Merger, the Company entered into Amendment No. 3 to the Credit Agreement to increase the permitted amount of outstanding letters of credit from \$15.0 million to \$20.0 million and to provide that certain existing letters of credit of FairPoint be deemed to be letters of credit under the Credit Agreement.

Our revolving credit facility has a maturity date of October 5, 2021 and an applicable margin (at our election) of between 2.50% and 3.25% for LIBOR-based borrowings or between 1.50% and 2.25% for alternate base rate borrowings, in each case depending on our total net leverage ratio. Based on our leverage ratio as of March 31, 2018, the borrowing margin for the three month period ending June 30, 2018 will be at a weighted-average margin of 3.00% for a LIBOR-based loan or 2.00% for an alternate base rate loan. The applicable borrowing margin for the revolving credit facility is adjusted quarterly to reflect the leverage ratio from the prior quarter-end. As of March 31, 2018, alternate base rate borrowings of \$22.0 million were outstanding under the revolving credit facility. At December 31, 2017, there were borrowings of \$22.0 million outstanding under the revolving credit facility, which consisted of LIBOR-based borrowings of \$17.0 million and alternate base rate borrowings of \$5.0 million. Stand-by letters of credit of \$18.2 million were outstanding under our revolving credit facility as of March 31, 2018. The stand-by letters of credit are renewable annually and reduce the borrowing availability under the revolving credit facility. As of March 31, 2018, \$69.8 million was available for borrowing under the revolving credit facility.

The weighted-average interest rate on outstanding borrowings under our credit facility was 4.90% and 4.58% as of March 31, 2018 and December 31, 2017, respectively. Interest is payable at least quarterly.

Credit Agreement Covenant Compliance

The Credit Agreement contains various provisions and covenants, including, among other items, restrictions on the ability to pay dividends, incur additional indebtedness and issue certain capital stock. We have agreed to maintain certain financial ratios, including interest coverage and total net leverage ratios, all as defined in the Credit Agreement. As of March 31, 2018, we were in compliance with the Credit Agreement covenants.

In general, our Credit Agreement restricts our ability to pay dividends to the amount of our available cash as defined in our Credit Agreement. As of March 31, 2018, and including the \$27.4 million dividend paid on May 1, 2018, we had \$265.3 million in dividend availability under the credit facility covenant.

Under our Credit Agreement, if our total net leverage ratio, as defined in the Credit Agreement, as of the end of any fiscal quarter is greater than 5.10:1.00, we will be required to suspend dividends on our common stock unless otherwise permitted by an exception for dividends that may be paid from the portion of proceeds of any sale of equity not used to fund acquisitions or make other investments. During any dividend suspension period, we will be required to repay debt in an amount equal to 50.0% of any increase in available cash, among other things. In addition, we will not be permitted to pay dividends if an event of default under the Credit Agreement has occurred and is continuing. Among other things, it will be an event of default if our total net leverage ratio or interest coverage ratio as of the end of any fiscal quarter is greater than 5.25:1.00 or less than 2.25:1.00, respectively. As of March 31, 2018, our total net leverage ratio under the Credit Agreement was 4.15:1.00, and our interest coverage ratio was 5.01:1.00.

Senior Notes

6.50% Senior Notes due 2022

In September 2014, we completed an offering of \$200.0 million aggregate principal amount of 6.50% Senior Notes due in October 2022 (the “Existing Notes”). The Existing Notes were priced at par, which resulted in total gross proceeds of \$200.0 million. On June 8, 2015, we completed an additional offering of \$300.0 million in aggregate principal amount of 6.50% Senior Notes due 2022 (the “New Notes” and together with the Existing Notes, the “Senior Notes”). The New Notes were issued as additional notes under the same indenture pursuant to which the Existing Notes were previously issued on in September 2014. The New Notes were priced at 98.26% of par with a yield to maturity of 6.80% and resulted in total gross proceeds of approximately \$294.8 million, excluding accrued interest. The discount is being amortized using the effective interest method over the term of the notes.

The Senior Notes mature on October 1, 2022 and interest is payable semi-annually on April 1 and October 1 of each year. Consolidated Communications, Inc. (“CCI”) is the primary obligor under the Senior Notes, and we and certain of our wholly-owned subsidiaries, including certain FairPoint subsidiaries, have fully and unconditionally guaranteed the Senior Notes. The Senior Notes are senior unsecured obligations of the Company.

In October 2015, we completed an exchange offer to register all of the Senior Notes under the Securities Act of 1933 (“Securities Act”). The terms of the registered Senior Notes are substantially identical to those of the Senior Notes prior to the exchange, except that the Senior Notes are now registered under the Securities Act and the transfer restrictions and registration rights previously applicable to the Senior Notes no longer apply to the registered Senior Notes. The exchange offer did not impact the aggregate principal amount or the remaining terms of the Senior Notes outstanding.

Senior Notes Covenant Compliance

Subject to certain exceptions and qualifications, the indenture governing the Senior Notes contains customary covenants that, among other things, limits CCI’s and its restricted subsidiaries’ ability to: incur additional debt or issue certain preferred stock; pay dividends or make other distributions on capital stock or prepay subordinated indebtedness; purchase or redeem any equity interests; make investments; create liens; sell assets; enter into agreements that restrict dividends or other payments by restricted subsidiaries; consolidate, merge or transfer all or substantially all of its assets; engage in transactions with its affiliates; or enter into any sale and leaseback transactions. The indenture also contains customary events of default.

Among other matters, the Senior Notes indenture provides that CCI may not pay dividends or make other restricted payments, as defined in the indenture, if its total net leverage ratio is 4.75:1.00 or greater. This ratio is calculated differently than the comparable ratio under the Credit Agreement; among other differences, it takes into account, on a pro forma basis, synergies expected to be achieved as a result of certain acquisitions not yet reflected in historical results. As of March 31, 2018, this ratio was 4.21:1.00. If this ratio is met, dividends and other restricted payments may be made from cumulative consolidated cash flow since April 1, 2012, less 1.75 times fixed charges, less dividends and other restricted payments

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made since May 30, 2012. Dividends may be paid and other restricted payments may also be made from a “basket” of \$50.0 million, none of which has been used to date, and pursuant to other exceptions identified in the indenture. Since dividends of \$460.9 million have been paid since May 30, 2012, including the quarterly dividend declared in February 2018 and paid on May 1, 2018, there was \$935.4 million of the \$1,396.4 million of cumulative consolidated cash flow since May 30, 2012 available to pay dividends as of March 31, 2018. As of March 31, 2018, the Company was in compliance with all terms, conditions and covenants under the indenture governing the Senior Notes.

Capital Leases

We lease certain facilities and equipment under various capital leases which expire between 2018 and 2027. As of March 31, 2018, the present value of the minimum remaining lease commitments was approximately \$35.1 million, of which \$13.2 million was due and payable within the next twelve months. The leases require total remaining rental payments of \$41.7 million as of March 31, 2018, of which \$2.6 million will be paid to LATEL LLC, a related party entity.

7. DERIVATIVE FINANCIAL INSTRUMENTS

We use derivative financial instruments to manage our exposure to the risks associated with fluctuations in interest rates. Our interest rate swap agreements effectively convert a portion of our floating-rate debt to a fixed-rate basis, thereby reducing the impact of interest rate changes on future cash interest payments. Derivative financial instruments are recorded at fair value in our condensed consolidated balance sheets. We may designate certain of our interest rate swaps as cash flow hedges of our expected future interest payments. For derivative instruments designated as a cash flow hedge, the effective portion of the change in the fair value is recognized as a component of accumulated other comprehensive income (loss) (“AOCI”) and is recognized as an adjustment to earnings over the period in which the hedged item impacts earnings. When an interest rate swap agreement terminates, any resulting gain or loss is recognized over the shorter of the remaining original term of the hedging instrument or the remaining life of the underlying debt obligation. If a derivative instrument is de-designated, the remaining gain or loss in AOCI on the date of de-designation is amortized to earnings over the remaining term of the hedging instrument. For derivative financial instruments that are not designated as a hedge, including those that have been de-designated, changes in fair value are recognized on a current basis in earnings. The ineffective portion of the change in fair value of any hedging derivative is recognized immediately in earnings. Cash flows from hedging activities are classified under the same category as the cash flows from the hedged items in our condensed consolidated statements of cash flows.

The following interest rate swaps were outstanding as of March 31, 2018:

| <i>(In thousands)</i> | Notional Amount | 2018 Balance Sheet Location | Fair Value |
|---|----------------------------|---|-------------------|
| Cash Flow Hedges: | | | |
| Fixed to 1-month floating LIBOR (with floor) | \$ 650,000 | Prepaid expenses and other current assets | \$ 694 |
| Fixed to 1-month floating LIBOR (with floor) | \$ 50,000 | Other assets | 730 |
| Series of forward starting fixed to 1-month floating LIBOR (with floor) | \$ 2,010,000 | Other assets | 5,749 |
| De-designated Hedges: | | | |
| Fixed to 1-month floating LIBOR (with floor) | \$ 500,000 | Other long-term liabilities | (3,284) |
| Total Fair Values | | | <u>\$ 3,889</u> |

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The following interest rate swaps were outstanding as of December 31, 2017:

| <i>(In thousands)</i> | Notional Amount | 2017 Balance Sheet Location | Fair Value |
|---|----------------------------|------------------------------------|-------------------|
| Cash Flow Hedges: | | | |
| Fixed to 1-month floating LIBOR (with floor) | \$ 600,000 | Other assets | \$ 873 |
| Fixed to 1-month floating LIBOR (with floor) | \$ 150,000 | Accrued expense | (27) |
| Forward starting fixed to 1-month floating LIBOR (with floor) | \$ 600,000 | Other assets | 383 |
| Series of forward starting fixed to 1-month floating LIBOR (with floor) | \$ 1,410,000 | Other long-term liabilities | (1,761) |
| Total Fair Values | | | <u>\$ (532)</u> |

The counterparties to our various swaps are highly rated financial institutions. None of the swap agreements provide for either us or the counterparties to post collateral nor do the agreements include any covenants related to the financial condition of Consolidated or the counterparties. The swaps of any counterparty that is a lender, as defined in our credit facility, are secured along with the other creditors under the credit facility. Each of the swap agreements provides that, in the event of a bankruptcy filing by either Consolidated or the counterparty, any amounts owed between the two parties would be offset in order to determine the net amount due between parties.

In connection with the acquisition of FairPoint, during the quarter ended June 30, 2017, we entered into a series of four deal contingent forward-starting interest rate swap agreements each with a term of one year which began at various dates between July 2017 and July 2020 and mature between July 2018 and July 2021. The forward starting interest rate swap agreements have a notional value ranging from \$450.0 million to \$705.0 million. These interest rate swap agreements have been designated as cash flow hedges.

During the quarter ended March 31, 2018, we entered into an interest rate swap agreement with a notional value of \$500.0 million and a term of five years. The interest rate swap agreement was designated as a cash flow hedge. On March 12, 2018, we completed a syndication of a portion of the \$500.0 million interest rate swap agreement with five new counterparties. On the date of the syndication, the interest rate swap agreements were de-designated due to changes in critical terms as a result of the syndication. Prior to de-designation, the effective portion of the change in fair value of the interest rate swap was recognized in AOCI. The balance of the unrealized loss included in AOCI as of the date the swaps were de-designated is being amortized to earnings over the remaining term of the interest rate swap agreements. Changes in fair value of the de-designated swaps were immediately recognized in earnings as interest expense. During the quarter ended March 31, 2018, a loss of \$2.9 million was recognized as an increase to interest expense for the change in fair value of the de-designated swaps. During the quarter ended June 30, 2018, the interest rate swap agreements were re-designated as a cash flow hedge.

As of March 31, 2018 and December 31, 2017, the total pre-tax unrealized gains related to our interest rate swap agreements included in AOCI was \$7.4 million and \$0.6 million, respectively. From the balance in AOCI as of March 31, 2018, we expect to recognize a loss of approximately \$1.5 million in earnings in the next twelve months.

Information regarding our cash flow hedge transactions is as follows:

| <i>(In thousands)</i> | Quarter Ended March 31, | |
|--|------------------------------------|-------------|
| | 2018 | 2017 |
| Unrealized gain (loss) recognized in AOCI, pretax | \$ 6,423 | \$ (91) |
| Deferred losses reclassified from AOCI to interest expense | \$ (356) | \$ (333) |
| Gain recognized in interest expense from ineffectiveness | \$ 1,030 | \$ 235 |

8. EQUITY

Share-Based Compensation

Our Board of Directors may grant share-based awards from our shareholder approved Amended and Restated Consolidated Communications Holdings, Inc. 2005 Long-Term Incentive Plan (the “Plan”). The Plan permits the issuance of awards in the form of stock options, stock appreciation rights, stock grants, stock unit grants and other equity-based awards to eligible directors and employees at the discretion of the Compensation Committee of the Board of Directors. On April 30, 2018, the shareholders approved an amendment to the Plan to increase by 2,000,000 the number of shares of our common stock authorized for issuance under the Plan and extend the term of the Plan through April 30, 2028. With the amendment, approximately 4,650,000 shares of our common stock are authorized for issuance under the Plan, provided that no more than 300,000 shares may be granted in the form of stock options or stock appreciation rights to any eligible employee or director in any calendar year. Unless terminated sooner, the Plan will continue in effect until April 30, 2028.

The following table summarizes total compensation costs recognized for share-based payments during the quarters ended March 31, 2018 and 2017:

| <i>(In thousands)</i> | Quarter Ended March 31, | |
|-----------------------|----------------------------|--------|
| | 2018 | 2017 |
| Restricted stock | \$ 435 | \$ 376 |
| Performance shares | 243 | 162 |
| Total | \$ 678 | \$ 538 |

Share-based compensation expense is included in selling, general and administrative expenses in the accompanying condensed consolidated statements of operations.

As of March 31, 2018, total unrecognized compensation cost related to non-vested Restricted Stock Awards (“RSAs”) and Performance Share Awards (“PSAs”) was \$13.7 million and will be recognized over a weighted-average period of approximately 2.0 years.

The following table summarizes the RSA and PSA activity for the three-month period ended March 31, 2018:

| | RSAs | | PSAs | |
|---|---------|--|---------|--|
| | Shares | Weighted Average Grant Date Fair Value | Shares | Weighted Average Grant Date Fair Value |
| Non-vested shares outstanding - January 1, 2018 | 102,181 | \$ 23.32 | 77,528 | \$ 21.46 |
| Shares granted | 478,210 | \$ 12.45 | — | \$ — |
| Shares forfeited, cancelled or retired | (1,851) | \$ 22.93 | (1,137) | \$ 21.80 |
| Non-vested shares outstanding - March 31, 2018 | 578,540 | \$ 14.34 | 76,391 | \$ 21.46 |

Accumulated Other Comprehensive Loss

The following table summarizes the changes in accumulated other comprehensive loss, net of tax, by component for the three-month period ended March 31, 2018:

| <i>(In thousands)</i> | Pension and Post-Retirement Obligations | Derivative Instruments | Total |
|--|---|---------------------------|--------------------|
| Balance at December 31, 2017 | \$ (48,464) | \$ 381 | \$ (48,083) |
| Other comprehensive income before reclassifications | — | 4,737 | 4,737 |
| Amounts reclassified from accumulated other comprehensive loss | 922 | 265 | 1,187 |
| Net current period other comprehensive income | 922 | 5,002 | 5,924 |
| Balance at March 31, 2018 | \$ (47,542) | \$ 5,383 | \$ (42,159) |

The following table summarizes reclassifications from accumulated other comprehensive loss for the quarters ended March 31, 2018 and 2017:

| <i>(In thousands)</i> | Quarter Ended March 31, | | Affected Line Item in the Statement of Income |
|---|-------------------------|-----------------|--|
| | 2018 | 2017 | |
| Amortization of pension and post-retirement items: | | | |
| Prior service credit | \$ 199 | \$ 244 | (a) |
| Actuarial loss | (1,451) | (1,661) | (a) |
| | (1,252) | (1,417) | Total before tax |
| | 330 | 555 | Tax benefit |
| | <u>\$ (922)</u> | <u>\$ (862)</u> | Net of tax |
| Loss on cash flow hedges: | | | |
| Interest rate derivatives | \$ (356) | \$ (333) | Interest expense |
| | 91 | 128 | Tax benefit |
| | <u>\$ (265)</u> | <u>\$ (205)</u> | Net of tax |

These items are included in the components of net periodic benefit cost for our pension and other post-retirement benefit plans. See Note 9 for further discussion regarding our pension and other post-retirement benefit plans.

9. PENSION PLAN AND OTHER POST-RETIREMENT BENEFITS

Defined Benefit Plans

We sponsor a qualified defined benefit pension plan (“Retirement Plan”) that is non-contributory covering certain of our hourly employees under collective bargaining agreements who fulfill minimum age and service requirements. Certain salaried employees are also covered by the Retirement Plan, although these benefits are frozen. The Retirement Plan is closed to all new entrants. Benefits for eligible participants under collective bargaining agreements are accrued based on a cash balance benefit plan.

As part of our acquisition of FairPoint, we assumed sponsorship of its two non-contributory qualified defined benefit pension plans (together, the “Qualified Pension Plan”). The Qualified Pension Plan for certain non-management employees under collective bargaining agreements is closed to new participants and benefits are frozen. For existing participants, benefit accruals are capped at 30 years of total credited service. The Qualified Pension Plan for certain management employees is frozen and all future benefit accruals for existing participants have ceased.

We also have two non-qualified supplemental retirement plans (the “Supplemental Plans” and, together with the Retirement Plan and the Qualified Pension Plan, the “Pension Plans”). The Supplemental Plans provide supplemental retirement benefits to certain former employees by providing for incremental pension payments to partially offset the reduction of the amount that would have been payable under the qualified defined benefit pension plans if it were not for

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limitations imposed by federal income tax regulations. The Supplemental Plans are frozen so that no person is eligible to become a new participant. These plans are unfunded and have no assets. The benefits paid under the Supplemental Plans are paid from the general operating funds of the Company.

The following table summarizes the components of net periodic pension cost for our Pension Plans for the quarters ended March 31, 2018 and 2017:

| <i>(In thousands)</i> | Quarter Ended March 31, | |
|---------------------------------------|----------------------------|---------------|
| | 2018 | 2017 |
| Service cost | \$ 1,535 | \$ 87 |
| Interest cost | 7,139 | 3,613 |
| Expected return on plan assets | (9,667) | (4,905) |
| Net amortization loss | 1,472 | 1,704 |
| Net prior service credit amortization | (61) | (114) |
| Net periodic pension cost | <u>\$ 418</u> | <u>\$ 385</u> |

The components of net periodic pension cost other than the service cost component are included in other, net within other income (expense) in the condensed consolidated statements of operations.

Other Non-qualified Deferred Compensation Agreements

We are also liable for deferred compensation agreements with former members of the board of directors and certain other former employees of acquired companies. Depending on the plan, benefits are payable in monthly or annual installments for a period of time based on the terms of the agreement, which range from five years up to the life of the participant or to the beneficiary upon the death of the participant, and may begin as early as age 55. Participants accrue no new benefits as these plans had previously been frozen. Payments related to the deferred compensation agreements totaled approximately \$0.2 million and \$0.1 million for the quarters ended March 31, 2018 and 2017, respectively. The net present value of the remaining obligations was approximately \$1.7 million and \$1.9 million as of March 31, 2018 and December 31, 2017, respectively, and is included in pension and other post-retirement benefit obligations in the accompanying condensed consolidated balance sheets.

We also maintain 25 life insurance policies on certain of the participating former directors and employees. We did not recognize any life insurance proceeds during the quarters ended March 31, 2018 or 2017. The excess of the cash surrender value of the remaining life insurance policies over the notes payable balances related to these policies totaled \$2.4 million and \$2.3 million as of March 31, 2018 and December 31, 2017, respectively. These amounts are included in investments in the accompanying condensed consolidated balance sheets. Cash principal payments for the policies and any proceeds from the policies are classified as operating activities in the condensed consolidated statements of cash flows.

Post-retirement Benefit Obligations

We sponsor various healthcare and life insurance plans (“Post-retirement Plans”) that provide post-retirement medical and life insurance benefits to certain groups of retired employees. Certain plans are frozen so that no person is eligible to become a new participant. Retirees share in the cost of healthcare benefits, making contributions that are adjusted periodically—either based upon collective bargaining agreements or because total costs of the program have changed. Covered expenses for retiree health benefits are paid as they are incurred. Post-retirement life insurance benefits are fully insured. A majority of the healthcare plans are unfunded and have no assets, and benefits are paid from the general operating funds of the Company. However, a plan acquired in the purchase of another company is funded by assets that are separately designated within the Retirement Plan for the sole purpose of providing payments of retiree medical benefits for this specific plan.

In connection with the acquisition of FairPoint, we acquired its post-retirement benefit plan as of the date of acquisition. The post-retirement benefit plan provides medical, dental and life insurance benefits to certain eligible employees and in

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some instances, to their spouses and families. The post-retirement benefit plan is unfunded and the Company funds the benefits that are paid.

The following table summarizes the components of the net periodic cost for our Post-retirement Plans for the quarters ended March 31, 2018 and 2017:

| <i>(In thousands)</i> | Quarter Ended | |
|---|---------------|---------------|
| | March 31, | |
| | 2018 | 2017 |
| Service cost | \$ 127 | \$ 123 |
| Interest cost | 1,029 | 395 |
| Expected return on plan assets | (36) | (28) |
| Net amortization gain | (21) | (43) |
| Net prior service credit amortization | (138) | (130) |
| Net periodic post-retirement benefit cost | <u>\$ 961</u> | <u>\$ 317</u> |

The components of net periodic post-retirement benefit cost other than the service cost component are included in other, net within other income (expense) in the condensed consolidated statements of operations.

Contributions

We expect to contribute approximately \$26.9 million to our Pension Plans and \$10.0 million to our Post-retirement Plans in 2018. As of March 31, 2018, we have contributed \$4.9 million and \$2.5 million of the annual contribution to the Pension Plans and Post-retirement Plans, respectively.

10. INCOME TAXES

Our unrecognized tax benefits as of March 31, 2018 and December 31, 2017 were \$4.5 million and \$4.3 million, respectively. The increase of \$0.2 million to unrecognized tax benefits during the quarter ended March 31, 2018 was primarily due to the acquisition of FairPoint and was recorded in purchase accounting. There was no material effect on the Company's effective tax rate. The net amount of unrecognized tax benefits that, if recognized, would result in an impact to the effective tax rate is \$4.3 million as of March 31, 2018 and \$4.1 million as of December 31, 2017. We do not expect any material change in our unrecognized tax benefits during the remainder of 2018.

Our practice is to recognize interest and penalties related to income tax matters in interest expense and selling, general and administrative expenses, respectively. As of March 31, 2018, we did not have a material liability for interest or penalties and had no material interest or penalty expense.

The periods subject to examination for our federal return are years 2014 through 2016. The periods subject to examination for our state returns are years 2013 through 2016. We do not expect any settlement or payment that may result from the examination to have a material effect on our results or cash flows.

Our effective tax rate was 27.5% and 37.0% for the quarters ended March 31, 2018 and 2017, respectively. The primary driver of the lower rate in 2018, compared to the same period in 2017, is the change in the corporate tax rate from 35% to 21% due to the enactment of the Tax Cuts and Jobs Act of 2017. The effective tax rate differed from the federal and state statutory rates primarily due to various permanent income tax differences and differences in allocable income for the Company's state tax filings.

ASC 740 requires us to recognize the effect of the tax law changes in the period of enactment. However, on December 22, 2017, Staff Accounting Bulletin No. 118 ("SAB 118") was issued to address the application of US GAAP in situations when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the Act. SAB 118 will allow us to record provisional amounts during a measurement period which is similar to the measurement period used when accounting for business combinations. SAB 118 would allow for a measurement period of up to one year after the enactment date of the

new tax legislation to finalize the recording of the related tax impacts. Any subsequent adjustment to these amounts will be recorded to tax expense in 2018 when the analysis is complete. For the quarter ended March 31, 2018, no adjustments were made to the provisional estimates that were recorded and disclosed as of December 31, 2017.

11. COMMITMENTS AND CONTINGENCIES

Litigation, Regulatory Proceedings and Other Contingencies

Local Switching Support

In 2015, FairPoint filed a Petition with the FCC requesting the FCC to direct National Exchange Carrier Association (“NECA”) to stop subtracting frozen LSS from FairPoint’s intercarrier compensation (“ICC”) Eligible Recovery for FairPoint’s rate of return Incumbent Local Exchange Carriers (“ILECs”) that participate in the NECA pooling process. This issue is unique to rate of return affiliates of price cap carriers because such companies are considered price cap carriers for the FCC’s Connect America Fund (“CAF”) funding, but remain rate of return for ICC purposes. Effective January 1, 2012, FairPoint rate of return ILECs were placed under the price cap CAF Phase I interim support mechanism, whereby the ILECs continued to receive frozen Universal Service Fund (“USF”) support for all forms of USF support received during 2011, including LSS. The rate of return rules for ICC included LSS support in that mechanism as well; therefore, NECA subtracted the frozen LSS support from the ICC Eligible Recovery amounts in accordance with FCC rules prohibiting duplicate recovery. When FairPoint accepted CAF Phase II support effective January 1, 2015, there was no longer any duplicate support and FairPoint requested NECA to stop subtracting LSS from FairPoint’s ICC Eligible Recovery. NECA declined to make that change, which led to FairPoint filing a Petition with the FCC asking the FCC to direct NECA to comply with FCC rules on ICC Eligible Recovery for rate of return ILECs. This issue also applies to Consolidated’s operations in Minnesota, which are also rate of return ILECs associated with a price cap company. The combined LSS support for the period from January 1, 2015 through December 31, 2017 is approximately \$12.4 million. Our ongoing ICC Eligible Recovery support for 2018 would increase by approximately \$3.6 million, and thereafter, decline by 5% per year through 2021. On March 31, 2018, we obtained the required votes necessary for an approved order and on April 19, 2018, the FCC issued its order approving our petition. As a result, during the quarter ended March 31, 2018, we recognized subsidies revenue of \$4.9 million and a contingent asset of \$8.4 million as a pre-acquisition gain contingency for the FairPoint LSS revenue prior to the acquisition date.

Access Charges

In 2014, Sprint Communications Company L.P. (“Sprint”) along with MCI Communications Services, Inc. and Verizon Select Services Inc. (collectively, “Verizon”) filed lawsuits against certain entities of the Company including FairPoint, and many other Local Exchange Carriers (collectively, “LECs”) throughout the country challenging the switched access charges LECs assessed Sprint and Verizon, as interexchange carriers (“IXCs”), for certain calls originating from or terminating to mobile devices that are routed to or from these LECs through these IXCs. The plaintiffs’ position is based on their interpretation of federal law, among other things, and they are seeking refunds of past access charges paid for such calls. The disputed amounts total \$4.8 million and cover periods dating back as far as 2006. CenturyLink, Inc. and its LEC subsidiaries (collectively “CenturyLink”), requested that the U.S. Judicial Panel on Multidistrict Litigation (the “Panel”), which has the authority to transfer the pretrial proceedings to a single court for multiple civil cases involving common questions of fact, transfer and consolidate these cases in one court. The Panel granted CenturyLink’s request and ordered that these cases be transferred to and centralized in the U.S. District Court for the Northern District of Texas (the “U.S. District Court”). On November 17, 2015, the U.S. District Court dismissed these complaints based on its interpretation of federal law and held that LECs could assess switched access charges for the calls at issue (the “November 2015 Order”). The November 2015 Order also allowed the plaintiffs to amend their complaints to assert claims that arise under state laws independent of the dismissed claims asserted under federal law. While Verizon did not make such a filing, on May 16, 2016, Sprint filed amended complaints and on June 30, 2016, the LEC defendants named in such complaints filed, among other things, a Joint Motion to Dismiss them, which the U.S. District Court granted on May 3, 2017. Certain FairPoint entities filed counterclaims against Sprint and Verizon.

Relatedly, in 2016, numerous LECs across the country, including a number of our LEC entities and FairPoint, filed complaints in various U.S. district courts against Level 3 Communications, LLC and certain of its affiliates (collectively,

“Level 3”) for its failure to pay access charges for certain calls that the November 2015 Order held could be assessed by LECs. The total amount of the Company’s LEC entities including FairPoint, seek from Level 3 in this proceeding is at least approximately \$1.3 million, excluding late payment charges/penalties and attorneys’ fees. These complaint cases were transferred to and included in the above-referenced consolidated proceeding before the U.S. District Court. Level 3 filed a Motion to Dismiss these complaints that, in part, repeated arguments the November 2015 Order rejected. On March 22, 2017, the U.S. District Court denied Level 3’s Motion to Dismiss (“March 2017 Order”).

On March 12, 2018, a motion for summary judgement was filed by various LECs with counterclaims against Verizon and Sprint. On March 26, 2018, a motion for summary judgement was filed by various LECs with claims against Level 3. Once the U.S. District Court issues final and appealable decisions on these motions, Sprint, Verizon, and Level 3 are expected to appeal the U.S. District Court’s November 2015 and March 2017 Orders. Absent a decision by an appellate court that overturns these orders, it could be difficult for Sprint or Verizon to succeed on its claims against us or for Level 3 to avoid paying the access charges it disputes in this litigation. Therefore, we do not expect any potential settlement or judgment to have a material adverse impact on our financial results or cash flows.

Gross Receipts Tax

Two of our subsidiaries, Consolidated Communications of Pennsylvania Company LLC (“CCPA”) and Consolidated Communications Enterprise Services Inc. (“CCES”), have, at various times, received assessment notices from the Commonwealth of Pennsylvania Department of Revenue (“DOR”) increasing the amounts owed for Pennsylvania Gross Receipts Tax, and/or have had audits performed for the tax years of 2008 through 2016. For our CCES and CCPA subsidiaries, the total additional tax liability calculated by the DOR auditors for the tax years 2008 through 2016, including interest, is approximately \$6.3 million and \$7.5 million, respectively. We filed Petitions for Reassessment with the DOR’s Board of Appeals for the tax years 2008 through 2015, contesting these audit assessments. We expect to appeal the audit findings for each subsidiary for the 2016 tax year when the respective Audit Assessment Notices are issued.

In May 2017, we entered into an agreement to guarantee any potential liability to the DOR up to \$5.0 million. We believe that certain of the DOR’s findings regarding the Company’s additional tax liability for the tax years 2008 through 2015, for which we have filed appeals, continue to lack merit. However, in January 2018, CCES and CCPA submitted initial settlement offers to the Pennsylvania Office of Attorney General proposing to settle the intrastate and interstate cases at a reduced tax liability of the total assessed tax liability under dispute for the tax years 2008 through 2013. The settlement offers are currently under review and consideration by the Commonwealth of Pennsylvania. We expect to receive responses to our offers during the second quarter of 2018. While we continue to believe a settlement of all disputed claims is possible, we cannot anticipate at this time what the ultimate resolution of these cases will be, nor can we evaluate the likelihood of a favorable or unfavorable outcome or the potential losses (or gains) should such an outcome occur.

Based on the initial settlement offers for the tax years 2008 through 2013 and the Company’s best estimate of the potential additional tax liabilities for 2014 through 2018, we have reserved \$3.2 million and \$1.4 million, including interest, for our CCES and CCPA subsidiaries, respectively. We do not believe that the outcome of these claims will have a material adverse impact on our financial results or cash flows.

From time to time we may be involved in litigation that we believe is of the type common to companies in our industry, including regulatory issues. While the outcome of these claims cannot be predicted with certainty, we do not believe that the outcome of any of these legal matters will have a material adverse impact on our business, results of operations, financial condition or cash flows.

12. CONDENSED CONSOLIDATING FINANCIAL INFORMATION

Consolidated Communications, Inc. is the primary obligor under the unsecured Senior Notes. We and substantially all of our subsidiaries, including our FairPoint subsidiaries, have jointly and severally guaranteed the Senior Notes. All of the subsidiary guarantors are 100% direct or indirect wholly owned subsidiaries of the parent, and all guarantees are full, unconditional and joint and several with respect to principal, interest and liquidated damages, if any. As such, we present condensed consolidating balance sheets as of March 31, 2018 and December 31, 2017, condensed consolidating statements of operations for the quarters ended March 31, 2018 and 2017 and condensed consolidating statements of cash flows for the three-month periods ended March 31, 2018 and 2017 for each of the Company (Parent), Consolidated Communications,

Inc. (Subsidiary Issuer), guarantor subsidiaries and other non-guarantor subsidiaries with any consolidating adjustments. See Note 6 for more information regarding our Senior Notes.

Condensed Consolidating Balance Sheets
(In thousands)

| | March 31, 2018 | | | | | |
|---|--------------------|--------------------|--------------------|-------------------|----------------------|---------------------|
| | Parent | Subsidiary Issuer | Guarantors | Non-Guarantors | Eliminations | Consolidated |
| ASSETS | | | | | | |
| Current assets: | | | | | | |
| Cash and cash equivalents | \$ — | \$ 10,115 | \$ 1,024 | \$ 1 | \$ — | \$ 11,140 |
| Accounts receivable, net | — | — | 128,050 | 7,159 | (1,114) | 134,095 |
| Income taxes receivable | 16,351 | 4,743 | 2,084 | — | (1,286) | 21,892 |
| Prepaid expenses and other current assets | — | 694 | 39,385 | 123 | — | 40,202 |
| Assets held for sale | — | — | — | 21,524 | — | 21,524 |
| Total current assets | 16,351 | 15,552 | 170,543 | 28,807 | (2,400) | 228,853 |
| Property, plant and equipment, net | — | — | 1,952,334 | 67,065 | — | 2,019,399 |
| Intangibles and other assets: | | | | | | |
| Investments | — | 8,673 | 98,441 | — | — | 107,114 |
| Investments in subsidiaries | 3,629,617 | 2,139,303 | 18,461 | — | (5,787,381) | — |
| Goodwill | — | — | 966,731 | 66,181 | — | 1,032,912 |
| Other intangible assets | — | — | 283,473 | 9,087 | — | 292,560 |
| Advances due to/from affiliates, net | — | 2,430,033 | 596,146 | 79,298 | (3,105,477) | — |
| Deferred income taxes | 22,584 | — | — | — | (22,584) | — |
| Other assets | 2,938 | 6,530 | 18,521 | 37 | — | 28,026 |
| Total assets | <u>\$3,671,490</u> | <u>\$4,600,091</u> | <u>\$4,104,650</u> | <u>\$ 250,475</u> | <u>\$(8,917,842)</u> | <u>\$ 3,708,864</u> |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | | | |
| Current liabilities: | | | | | | |
| Accounts payable | \$ — | \$ — | \$ 21,014 | \$ — | \$ — | \$ 21,014 |
| Advance billings and customer deposits | — | — | 42,088 | 1,541 | — | 43,629 |
| Dividends payable | 27,602 | — | — | — | — | 27,602 |
| Accrued compensation | — | — | 52,756 | 933 | — | 53,689 |
| Accrued interest | — | 16,999 | 690 | — | — | 17,689 |
| Accrued expense | 63 | 1,114 | 74,843 | 2,425 | (1,114) | 77,331 |
| Income tax payable | — | — | — | 1,286 | (1,286) | — |
| Current portion of long term debt and capital lease obligations | — | 18,350 | 13,023 | 181 | — | 31,554 |
| Liabilities held for sale | — | — | — | 1,083 | — | 1,083 |
| Total current liabilities | 27,665 | 36,463 | 204,414 | 7,449 | (2,400) | 273,591 |
| Long-term debt and capital lease obligations | — | 2,295,543 | 21,485 | 370 | — | 2,317,398 |
| Advances due to/from affiliates, net | 3,105,477 | — | — | — | (3,105,477) | — |
| Deferred income taxes | — | 2,529 | 213,342 | 21,160 | (22,584) | 214,447 |
| Pension and postretirement benefit obligations | — | — | 308,959 | 17,866 | — | 326,825 |
| Other long-term liabilities | — | 3,284 | 28,224 | 992 | — | 32,500 |
| Total liabilities | 3,133,142 | 2,337,819 | 776,424 | 47,837 | (3,130,461) | 3,164,761 |
| Shareholders' equity: | | | | | | |
| Common Stock | 713 | — | 17,411 | 30,000 | (47,411) | 713 |
| Other shareholders' equity | 537,635 | 2,262,272 | 3,305,060 | 172,638 | (5,739,970) | 537,635 |
| Total Consolidated Communications Holdings, Inc. shareholders' equity | 538,348 | 2,262,272 | 3,322,471 | 202,638 | (5,787,381) | 538,348 |
| Noncontrolling interest | — | — | 5,755 | — | — | 5,755 |
| Total shareholders' equity | 538,348 | 2,262,272 | 3,328,226 | 202,638 | (5,787,381) | 544,103 |
| Total liabilities and shareholders' equity | <u>\$3,671,490</u> | <u>\$4,600,091</u> | <u>\$4,104,650</u> | <u>\$ 250,475</u> | <u>\$(8,917,842)</u> | <u>\$ 3,708,864</u> |

Condensed Consolidating Balance Sheet
(In thousands)

| | December 31, 2017 | | | | | |
|---|--------------------|----------------------|--------------------|--------------------|----------------------|---------------------|
| | Parent | Subsidiary Issuer | Guarantors | Non- Guarantors | Eliminations | Consolidated |
| ASSETS | | | | | | |
| Current assets: | | | | | | |
| Cash and cash equivalents | \$ — | \$ 8,919 | \$ 6,738 | \$ — | \$ — | \$ 15,657 |
| Accounts receivable, net | — | — | 114,303 | 7,701 | (476) | 121,528 |
| Income taxes receivable | 20,275 | — | 1,571 | — | — | 21,846 |
| Prepaid expenses and other current assets | — | — | 33,188 | 130 | — | 33,318 |
| Assets held for sale | — | — | — | 21,310 | — | 21,310 |
| Total current assets | 20,275 | 8,919 | 155,800 | 29,141 | (476) | 213,659 |
| Property, plant and equipment, net | — | — | 1,972,190 | 65,416 | — | 2,037,606 |
| Intangibles and other assets: | | | | | | |
| Investments | — | 8,495 | 100,363 | — | — | 108,858 |
| Investments in subsidiaries | 3,643,930 | 2,133,049 | 35,374 | — | (5,812,353) | — |
| Goodwill | — | — | 971,851 | 66,181 | — | 1,038,032 |
| Other intangible assets | — | — | 297,696 | 9,087 | — | 306,783 |
| Advances due to/from affiliates, net | — | 2,441,690 | 555,332 | 92,615 | (3,089,637) | — |
| Deferred income taxes | 21,244 | — | — | — | (21,244) | — |
| Other assets | — | 1,307 | 12,844 | 37 | — | 14,188 |
| Total assets | <u>\$3,685,449</u> | <u>\$4,593,460</u> | <u>\$4,101,450</u> | <u>\$ 262,477</u> | <u>\$(8,923,710)</u> | <u>\$ 3,719,126</u> |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | | | |
| Current liabilities: | | | | | | |
| Accounts payable | \$ — | \$ — | \$ 24,143 | \$ — | \$ — | \$ 24,143 |
| Advance billings and customer deposits | — | — | 41,026 | 1,500 | — | 42,526 |
| Dividends payable | 27,418 | — | — | — | — | 27,418 |
| Accrued compensation | — | — | 48,795 | 975 | — | 49,770 |
| Accrued interest | — | 8,824 | 519 | — | — | 9,343 |
| Accrued expense | 107 | 504 | 70,976 | 930 | (476) | 72,041 |
| Current portion of long term debt and capital lease obligations | — | 18,350 | 11,150 | 196 | — | 29,696 |
| Liabilities held for sale | — | — | — | 1,003 | — | 1,003 |
| Total current liabilities | 27,525 | 27,678 | 196,609 | 4,604 | (476) | 255,940 |
| Long-term debt and capital lease obligations | — | 2,298,970 | 12,139 | 405 | — | 2,311,514 |
| Advances due to/from affiliates, net | 3,089,637 | — | — | — | (3,089,637) | — |
| Deferred income taxes | — | 750 | 209,116 | 21,098 | (21,244) | 209,720 |
| Pension and postretirement benefit obligations | — | — | 315,129 | 19,064 | — | 334,193 |
| Other long-term liabilities | — | 1,761 | 31,030 | 1,026 | — | 33,817 |
| Total liabilities | 3,117,162 | 2,329,159 | 764,023 | 46,197 | (3,111,357) | 3,145,184 |
| Shareholders' equity: | | | | | | |
| Common Stock | 708 | — | 17,411 | 30,000 | (47,411) | 708 |
| Other shareholders' equity | 567,579 | 2,264,301 | 3,314,361 | 186,280 | (5,764,942) | 567,579 |
| Total Consolidated Communications Holdings, Inc. shareholders' equity | 568,287 | 2,264,301 | 3,331,772 | 216,280 | (5,812,353) | 568,287 |
| Noncontrolling interest | — | — | 5,655 | — | — | 5,655 |
| Total shareholders' equity | 568,287 | 2,264,301 | 3,337,427 | 216,280 | (5,812,353) | 573,942 |
| Total liabilities and shareholders' equity | <u>\$3,685,449</u> | <u>\$4,593,460</u> | <u>\$4,101,450</u> | <u>\$ 262,477</u> | <u>\$(8,923,710)</u> | <u>\$ 3,719,126</u> |

Condensed Consolidating Statements of Operations
(In thousands)

| | Quarter Ended March 31, 2018 | | | | | |
|--|------------------------------|----------------------|------------|--------------------|--------------|--------------|
| | Parent | Subsidiary Issuer | Guarantors | Non- Guarantors | Eliminations | Consolidated |
| Net revenues | \$ — | \$ — | \$ 344,311 | \$ 14,877 | \$ (3,149) | \$ 356,039 |
| Operating expenses: | | | | | | |
| Cost of services and products (exclusive of depreciation and amortization) | — | — | 151,762 | 4,201 | (3,047) | 152,916 |
| Selling, general and administrative expenses | 581 | — | 81,901 | 3,238 | (102) | 85,618 |
| Acquisition and other transaction costs | 731 | — | — | — | — | 731 |
| Depreciation and amortization | — | — | 105,288 | 2,611 | — | 107,899 |
| Operating income (loss) | (1,312) | — | 5,360 | 4,827 | — | 8,875 |
| Other income (expense): | | | | | | |
| Interest expense, net of interest income | (26) | (32,932) | 192 | 50 | — | (32,716) |
| Intercompany interest income (expense) | — | 14,727 | (14,712) | (15) | — | — |
| Investment income | — | 178 | 7,611 | — | — | 7,789 |
| Equity in earnings of subsidiaries, net | (10,311) | 2,975 | 423 | — | 6,913 | — |
| Other, net | — | — | 587 | 19 | — | 606 |
| Income (loss) before income taxes | (11,649) | (15,052) | (539) | 4,881 | 6,913 | (15,446) |
| Income tax expense (benefit) | (351) | (4,741) | (440) | 1,284 | — | (4,248) |
| Net income (loss) | (11,298) | (10,311) | (99) | 3,597 | 6,913 | (11,198) |
| Less: net income attributable to noncontrolling interest | — | — | 100 | — | — | 100 |
| Net income (loss) attributable to Consolidated Communications Holdings, Inc. | \$ (11,298) | \$ (10,311) | \$ (199) | \$ 3,597 | \$ 6,913 | \$ (11,298) |
| Total comprehensive income (loss) attributable to common shareholders | \$ (5,374) | \$ (4,387) | \$ 553 | \$ 3,767 | \$ 67 | \$ (5,374) |

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| | Quarter Ended March 31, 2017 | | | | | |
|--|-------------------------------------|------------------------------|-------------------|----------------------------|---------------------|---------------------|
| | Parent | Subsidiary Issuer | Guarantors | Non- Guarantors | Eliminations | Consolidated |
| Net revenues | \$ — | \$ — | \$ 158,832 | \$ 14,289 | \$ (3,186) | \$ 169,935 |
| Operating expenses: | | | | | | |
| Cost of services and products (exclusive of depreciation and amortization) | — | — | 71,615 | 2,496 | (3,079) | 71,032 |
| Selling, general and administrative expenses | 745 | 10 | 32,545 | 3,107 | (107) | 36,300 |
| Acquisition and other transaction costs | 1,329 | — | — | — | — | 1,329 |
| Depreciation and amortization | — | — | 39,520 | 2,675 | — | 42,195 |
| Operating income (loss) | (2,074) | (10) | 15,152 | 6,011 | — | 19,079 |
| Other income (expense): | | | | | | |
| Interest expense, net of interest income | 6 | (29,487) | (206) | 16 | — | (29,671) |
| Intercompany interest income (expense) | — | 14,727 | (14,708) | (19) | — | — |
| Investment income | — | 157 | 5,121 | — | — | 5,278 |
| Equity in earnings of subsidiaries, net | (2,305) | 7,738 | (55) | — | (5,378) | — |
| Other, net | — | 1 | (485) | (81) | — | (565) |
| Income (loss) before income taxes | (4,373) | (6,874) | 4,819 | 5,927 | (5,378) | (5,879) |
| Income tax expense (benefit) | (688) | (4,569) | 1,230 | 1,853 | — | (2,174) |
| Net income (loss) | (3,685) | (2,305) | 3,589 | 4,074 | (5,378) | (3,705) |
| Less: net income attributable to noncontrolling interest | — | — | (20) | — | — | (20) |
| Net income (loss) attributable to Consolidated Communications Holdings, Inc. | <u>\$ (3,685)</u> | <u>\$ (2,305)</u> | <u>\$ 3,609</u> | <u>\$ 4,074</u> | <u>\$ (5,378)</u> | <u>\$ (3,685)</u> |
| Total comprehensive income (loss) attributable to common shareholders | <u>\$ (2,674)</u> | <u>\$ (1,294)</u> | <u>\$ 4,311</u> | <u>\$ 4,234</u> | <u>\$ (7,251)</u> | <u>\$ (2,674)</u> |

Condensed Consolidating Statements of Cash Flows
(In thousands)

| | Three Months Ended March 31, 2018 | | | | |
|---|-----------------------------------|----------------------|------------|--------------------|--------------|
| | Parent | Subsidiary Issuer | Guarantors | Non- Guarantors | Consolidated |
| Net cash (used in) provided by operating activities | \$ (707) | \$ (5,873) | \$ 89,008 | \$ 8,414 | \$ 90,842 |
| Cash flows from investing activities: | | | | | |
| Purchases of property, plant and equipment | — | — | (57,039) | (3,769) | (60,808) |
| Proceeds from sale of assets | — | — | 142 | 2 | 144 |
| Distributions from investments | — | — | 233 | — | 233 |
| Net cash used in investing activities | — | — | (56,664) | (3,767) | (60,431) |
| Cash flows from financing activities: | | | | | |
| Proceeds from issuance of long-term debt | — | 27,000 | — | — | 27,000 |
| Payment of capital lease obligation | — | — | (2,872) | (51) | (2,923) |
| Payment on long-term debt | — | (31,588) | — | — | (31,588) |
| Dividends on common stock | (27,417) | — | — | — | (27,417) |
| Transactions with affiliates, net | 28,124 | 11,657 | (35,186) | (4,595) | — |
| Net cash provided by (used in) financing activities | 707 | 7,069 | (38,058) | (4,646) | (34,928) |
| Increase (decrease) in cash and cash equivalents | — | 1,196 | (5,714) | 1 | (4,517) |
| Cash and cash equivalents at beginning of period | — | 8,919 | 6,738 | — | 15,657 |
| Cash and cash equivalents at end of period | \$ — | \$ 10,115 | \$ 1,024 | \$ 1 | \$ 11,140 |

| | Three Months Ended March 31, 2017 | | | | |
|---|-----------------------------------|----------------------|------------|--------------------|--------------|
| | Parent | Subsidiary Issuer | Guarantors | Non- Guarantors | Consolidated |
| Net cash (used in) provided by operating activities | \$ (1,476) | \$ 2,710 | \$ 41,366 | \$ 9,118 | \$ 51,718 |
| Cash flows from investing activities: | | | | | |
| Purchases of property, plant and equipment | — | — | (26,089) | (2,936) | (29,025) |
| Proceeds from sale of assets | — | — | 18 | 25 | 43 |
| Net cash provided by (used in) investing activities | — | — | (26,071) | (2,911) | (28,982) |
| Cash flows from financing activities: | | | | | |
| Proceeds from issuance of long-term debt | — | 7,000 | — | — | 7,000 |
| Payment of capital lease obligation | — | — | (1,244) | (45) | (1,289) |
| Payment on long-term debt | — | (9,250) | — | — | (9,250) |
| Share repurchases for minimum tax withholding | (41) | — | — | — | (41) |
| Dividends on common stock | (19,604) | — | — | — | (19,604) |
| Transactions with affiliates, net | 21,121 | (908) | (14,051) | (6,162) | — |
| Net cash provided by (used in) financing activities | 1,476 | (3,158) | (15,295) | (6,207) | (23,184) |
| Increase (decrease) in cash and cash equivalents | — | (448) | — | — | (448) |
| Cash and cash equivalents at beginning of period | — | 27,064 | 13 | — | 27,077 |
| Cash and cash equivalents at end of period | \$ — | \$ 26,616 | \$ 13 | \$ — | \$ 26,629 |

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The Securities and Exchange Commission (“SEC”) encourages companies to disclose forward-looking information so that investors can better understand a company’s future prospects and make informed investment decisions. Certain statements in this Quarterly Report on Form 10-Q, including those which relate to the impact on future revenue sources, pending and future regulatory orders, continued expansion of the telecommunications network and expected changes in the sources of our revenue and cost structure resulting from our entrance into new communications markets, are forward-looking statements and are made pursuant to the safe harbor provisions of the Securities Litigation Reform Act of 1995. These forward-looking statements reflect, among other things, our current expectations, plans, strategies and anticipated financial results. There are a number of risks, uncertainties and conditions that may cause our actual results to differ materially from those expressed or implied by these forward-looking statements. Many of these circumstances are beyond our ability to control or predict. Moreover, forward-looking statements necessarily involve assumptions on our part. These forward-looking statements generally are identified by the words “believe”, “expect”, “anticipate”, “estimate”, “project”, “intend”, “plan”, “should”, “may”, “will”, “would”, “will be”, “will continue” or similar expressions. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of Consolidated Communications Holdings, Inc. and its subsidiaries (“Consolidated”, the “Company”, “we” or “our”) to be different from those expressed or implied in the forward-looking statements. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements that appear throughout this report. A detailed discussion of these and other risks and uncertainties that could cause actual results and events to differ materially from such forward-looking statements is included in our 2017 Annual Report on Form 10-K filed with the SEC. Furthermore, undue reliance should not be placed on forward-looking statements, which speak only as of the date they are made. Except as required under federal securities laws or the rules and regulations of the SEC, we disclaim any intention or obligation to update or revise publicly any forward-looking statements. Management’s Discussion and Analysis (“MD&A”) should be read in conjunction with our unaudited condensed consolidated financial statements and accompanying notes to the financial statements (“Notes”) as of and for the quarter ended March 31, 2018 included in Item 1 of Part I of this Quarterly Report on Form 10-Q.

Throughout this MD&A, we refer to certain measures that are not measures of financial performance in accordance with accounting principles generally accepted in the United States (“US GAAP” or “GAAP”). We believe the use of these non-GAAP measures on a consolidated basis provides the reader with additional information that is useful in understanding our operating results and trends. These measures should be viewed in addition to, rather than as a substitute for, those measures prepared in accordance with GAAP. See the “Non-GAAP Measures” section below for a more detailed discussion on the use and calculation of these measures.

Overview

Consolidated Communications is a broadband and business communications provider offering a wide range of communication solutions to consumer, commercial and carrier customers across a 24-state service area and an advanced fiber network spanning more than 36,000 fiber route miles. We offer residential Internet, video, phone and home security services as well as multi-service residential and small business bundles. Our business product suite includes data and Internet solutions, voice, data center services, security services, managed and IT Services, and an expanded suite of cloud services. We provide wholesale solutions to carriers and other service providers including data, voice and network connections.

We generate the majority of our consolidated operating revenues primarily from subscriptions to our video, data and transport services (collectively “broadband services”) to business and residential customers. Commercial and carrier services represent the largest source of our operating revenues and are expected to be key growth areas in the future. We continue to focus on broadband and commercial growth opportunities and are continually enhancing our broadband services and expanding our commercial product offerings for both small and large businesses in order to capitalize on technological advances in the industry. Our recent acquisition of FairPoint Communications, Inc. (“FairPoint”), as described below, provides us significantly greater scale and an expanded fiber network which allows for additional growth opportunities and expansion. We leverage our advanced fiber networks and tailor our services for business customers by

developing solutions to fit their specific needs. In addition, we are expanding our suite of cloud services, which increases efficiency and enables greater scalability and reliability for businesses. We anticipate future momentum in commercial and carrier services as these products gain traction as well as from the demand from customers for additional bandwidth and data-based services.

We market our residential services by leading with broadband or bundled services. Our “triple play” bundle includes Internet, video and phone services. As consumer demands for bandwidth continue to increase, our focus is on enhancing our broadband services, and progressively increasing consumer data speeds. We offer data speeds of up to 1 Gbps in select markets, and up to 100 Mbps in markets where 1 Gbps is not yet available, depending on the geographical region. As of March 31, 2018, approximately 42% of the homes we serve on our legacy network had availability to broadband speeds of up to 100 Mbps. The majority of the homes in our recently acquired FairPoint service territories have availability to broadband speeds of 20 mbps or less. As part of our integration initiatives of FairPoint, we plan to increase broadband speeds to more than 500,000 residents and small businesses across the Northern New England service area by the end of 2018. The upgrades are expected to enable customers to receive broadband speeds up to three times the speeds currently available and provide nearly 100,000 additional homes with access to data speeds of 1 Gbps.

Our competitive consumer broadband speeds allow us to continue to meet the needs of our customers and the demand for higher speeds driven by Over-The-Top (“OTT”) content viewing. The availability of higher broadband speeds also complements our TV Everywhere service, which allows our video subscribers to watch their favorite shows, movies and livestreams on any device. In addition, we offer other in-demand OTT content, such as fubo, HBO Now, DirecTV Now and other sports and entertainment.

The consumer demand for OTT services either to augment their current video subscription viewing or to entirely replace their video subscription may impact our future video subscriber base, which could result in a decline in video revenue as well as a reduction in video programing costs. Excluding FairPoint, total video connections decreased 8% as of March 31, 2018 compared to the same period in 2017. We believe the trend in changing consumer viewing habits will continue to impact our business results and complement our strategy of providing consumers higher broadband speed to facilitate OTT content viewing.

Operating revenues also continue to be impacted by the anticipated industry-wide trend of a decline in voice services, access lines and related network access revenue. Many customers are choosing to subscribe to alternative communication services and competition for these subscribers continues to increase. Excluding FairPoint, total voice connections decreased 4% as of March 31, 2018 compared to the same period in 2017. Competition from wireless providers, Competitive Local Exchange Carriers and cable television providers has increased in recent years in the markets we serve. We have been able to mitigate some of the access line losses through marketing initiatives and product offerings, such as our VoIP service.

As discussed in the “Regulatory Matters” section below, our operating revenues are impacted by legislative or regulatory changes at the federal and state levels, which could reduce or eliminate the current subsidies revenue we receive. A number of proceedings and recent orders relate to universal service reform, intercarrier compensation and network access charges. There are various ongoing legal challenges to the orders that have been issued. As a result, it is not yet possible to fully determine the impact of the regulatory changes on our operations.

Significant Recent Developments

Acquisitions

FairPoint Communications, Inc.

On July 3, 2017, we completed our merger with FairPoint (the “Merger”) and, pursuant to the terms of a definitive agreement and plan of merger (as amended, the “Merger Agreement”), acquired all the issued and outstanding shares of FairPoint in exchange for shares of our common stock. As a result, FairPoint became a wholly-owned subsidiary of the Company. FairPoint is an advanced communications provider to business, wholesale and residential customers within its service territory, which spans across 17 states. FairPoint owns and operates a robust fiber-based network with more than

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22,000 route miles of fiber, including 17,000 route miles of fiber in northern New England. The financial results for FairPoint have been included in our consolidated financial statements as of the acquisition date. The acquisition reflects our strategy to diversify revenue and cash flows among multiple products and to expand our network to new markets.

At the effective time of the Merger, each share of common stock of FairPoint issued and outstanding immediately prior to the effective time of the Merger converted into and became the right to receive 0.7300 shares of common stock of Consolidated and cash in lieu of fractional shares, pursuant to the terms of the Merger Agreement. Based on the closing price of our common stock on the last complete trading day prior to the effective date of the Merger, the total value of the consideration exchanged was approximately \$431.0 million, exclusive of debt of approximately \$919.3 million. On the date of the Merger, we issued an approximate aggregate total of 20.1 million shares of our common stock to the former FairPoint stockholders and we assumed approximately 2,615,153 outstanding warrants, each eligible to purchase one share of the Company's common stock at an exercise price of \$66.86 per share, subject to adjustment in accordance with the warrant agreement. On January 24, 2018, all of the warrants expired in accordance with their terms without being exercised.

To finance the Merger, in December 2016, we secured committed debt financing through a \$935.0 million incremental term loan facility, as described in the "Liquidity and Capital Resources" section below, that, in addition to cash on hand and other sources of liquidity, was used to repay and redeem certain existing indebtedness of FairPoint and pay the fees and expenses in connection with the Merger.

Divestitures

In connection with our acquisition of FairPoint, in August 2017, we entered into a letter of intent to sell our subsidiaries Peoples Mutual Telephone Company and Peoples Mutual Long Distance Company (collectively, "Peoples"), which were acquired as part of the acquisition of FairPoint. Peoples operates as a local exchange carrier in Virginia and provides telecommunications services to residential and business customers. In November 2017, the Company entered into an agreement to sell all of the issued and outstanding stock of Peoples in exchange for cash of approximately \$21.0 million, subject to certain contractual adjustments. The closing of the transaction is subject to certain regulatory approvals, which are expected to be completed in the second quarter of 2018.

Results of Operations

The following tables reflect our financial results on a consolidated basis and key operating metrics as of and for the quarters ended March 31, 2018 and 2017.

Financial Data

| <i>(In millions, except for percentages)</i> | Quarter Ended March 31, | | | |
|--|-------------------------|-----------------|-----------------|--------------|
| | 2018 | 2017 | \$ Change | % Change |
| Operating Revenues | | | | |
| Commercial and carrier: | | | | |
| Data and transport services (includes VoIP) | \$ 86.0 | \$ 50.9 | \$ 35.1 | 69 % |
| Voice services | 52.1 | 22.0 | 30.1 | 137 |
| Other | 11.9 | 3.9 | 8.0 | 205 |
| | <u>150.0</u> | <u>76.8</u> | <u>73.2</u> | <u>95</u> |
| Consumer: | | | | |
| Broadband (VoIP and Data) | 63.1 | 28.4 | 34.7 | 122 |
| Video services | 22.8 | 23.1 | (0.3) | (1) |
| Voice services | 52.1 | 13.1 | 39.0 | 298 |
| | <u>138.0</u> | <u>64.6</u> | <u>73.4</u> | <u>114</u> |
| Subsidies | 25.3 | 10.6 | 14.7 | 139 |
| Network access | 39.7 | 14.5 | 25.2 | 174 |
| Other products and services | 3.0 | 3.4 | (0.4) | (12) |
| Total operating revenues | <u>356.0</u> | <u>169.9</u> | <u>186.1</u> | <u>110</u> |
| Operating Expenses | | | | |
| Cost of services and products (exclusive of depreciation and amortization) | 152.9 | 71.0 | 81.9 | 115 |
| Selling, general and administrative costs | 85.6 | 36.3 | 49.3 | 136 |
| Acquisition and other transaction costs | 0.7 | 1.3 | (0.6) | (46) |
| Depreciation and amortization | 107.9 | 42.2 | 65.7 | 156 |
| Total operating expenses | <u>347.1</u> | <u>150.8</u> | <u>196.3</u> | <u>130</u> |
| Income from operations | 8.9 | 19.1 | (10.2) | (53) |
| Interest expense, net | (32.7) | (29.7) | (3.0) | (10) |
| Other income | 8.4 | 4.7 | 3.7 | 79 |
| Income tax benefit | (4.2) | (2.2) | (2.0) | (91) |
| Net loss | (11.2) | (3.7) | (7.5) | (203) |
| Net income attributable to noncontrolling interest | 0.1 | — | 0.1 | 100 |
| Net loss attributable to common shareholders | <u>\$ (11.3)</u> | <u>\$ (3.7)</u> | <u>\$ (7.6)</u> | <u>(205)</u> |
| Adjusted EBITDA ⁽¹⁾ | \$ 135.1 | \$ 71.1 | \$ 64.0 | 90 % |

⁽¹⁾ A non-GAAP measure. See the “Non-GAAP Measures” section below for additional information and reconciliation to the most directly comparable GAAP measure.

Key Operating Statistics

| | As of March 31, | | | |
|--------------------|-----------------|-----------|---------|----------|
| | 2018 | 2017 | Change | % Change |
| Consumer customers | 661,758 | 248,796 | 412,962 | 166 % |
| Voice connections | 955,419 | 453,332 | 502,087 | 111 |
| Data connections | 785,230 | 477,180 | 308,050 | 65 |
| Video connections | 100,570 | 102,906 | (2,336) | (2) |
| Total connections | 1,841,219 | 1,033,418 | 807,801 | 78 % |

The comparability of our consolidated results of operations and key operating statistics was impacted by the FairPoint acquisition that closed on July 3, 2017, as described above. FairPoint's results are included in our consolidated financial statements as of the date of the acquisition.

Revenue from Contracts with Customers

We account for revenue in accordance with ASC 606 ("ASC 606" or the "new standard"), *Revenue from Contracts with Customers*, which we adopted on January 1, 2018. Promised services in our revenue contracts with customers are considered distinct and are accounted for as separate performance obligations. Revenue is recognized when or as performance obligations are satisfied. The impact on revenue as a result of the adoption of ASC 606 was not material.

In accordance with ASC 606, contract acquisition costs are deferred and amortized over the expected customer life. Historically, these costs were expensed as incurred. The change in accounting for contract acquisition costs was the largest impact to the Company upon adoption of ASC 606.

For a more complete discussion of the adoption impacts, refer to Note 1 to the Condensed Consolidated Financial Statements, included in this report in Part I - Item 1 "Financial Statements".

Operating Revenues

Commercial and Carrier

Data and Transport Services

We provide a variety of business communication services to small, medium and large business customers, including many services over our advanced fiber network. The services we offer include scalable high speed broadband Internet access and VoIP phone services, which range from basic service plans to virtual hosted systems. In addition to Internet and VoIP services, we also offer private line data services to businesses that include dedicated Internet access through our Metro Ethernet network. Wide Area Network products include point-to-point and multi-point deployments from 2.5 Mbps to 10 Gbps to accommodate the growth patterns of our business customers. Data center and disaster recovery solutions provide a reliable and local colocation option for commercial customers. We also offer wholesale services to regional and national interexchange and wireless carriers, including cellular backhaul and other fiber transport solutions.

Data and transport services revenues increased \$35.1 million during the quarter ended March 31, 2018 compared to the same period in 2017 primarily due to the acquisition of FairPoint, which accounted for \$32.8 million of the increase. Excluding the addition of FairPoint revenues, data and transport services revenues increased \$2.3 million, during the quarter ended March 31, 2018 compared to the same period in 2017, primarily due to continued growth in Metro Ethernet and VoIP services as connections increased 7%.

Voice Services

Voice services include basic local phone and long-distance service packages for business customers. The plans include options for voicemail, conference calling, linking multiple office locations and other custom calling features such as caller ID, call forwarding, speed dialing and call waiting. Services can be charged at a fixed monthly rate, a measured rate or can be bundled with selected services at a discounted rate. Through the acquisition of FairPoint, we are now a full service 9-1-1 provider and 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 are expected to provide the foundation to handle future communication modes such as texting and video.

Voice services revenues increased \$30.1 million during the quarter ended March 31, 2018 compared to the same period in 2017 primarily due to additional revenue of \$31.2 million from the acquisition of FairPoint. Excluding FairPoint, voice services revenues decreased \$1.1 million during the quarter ended March 31, 2018 due to a 6% decline in access lines as commercial customers are increasingly choosing alternative technologies, including our own VoIP product, and the broad range of features that Internet based voice services can offer.

Other

Other services include business equipment sales and related hardware and maintenance support, rental income of customer premise equipment, video services and other miscellaneous revenues. Other services revenues increased \$8.0 million during the quarter ended March 31, 2018 compared to the same period in 2017 due to the acquisition of FairPoint, which accounted for the entire increase.

Consumer

Broadband Services

Broadband services include revenues from residential customers for subscriptions to our VoIP and data products. We offer high speed Internet access at speeds of up to 1 Gbps, depending on the nature of the network facilities that are available, the level of service selected and the location. Our VoIP digital phone service is also available in certain markets as an alternative to the traditional telephone line. Broadband services revenues increased \$34.7 million during the quarter ended March 31, 2018 compared to the same period in 2017 primarily due to additional revenue of \$34.5 million from the acquisition of FairPoint. Excluding FairPoint, broadband services revenues increased \$0.2 million during the quarter ended March 31, 2018 due to growth in data services despite a 5% decrease in data connections as a result of price increases implemented since the prior year quarter. VoIP revenue also declined during the quarter ended March 31, 2018 compared to the same period in 2017 due to a 10% decline in connections as more consumers continue to rely exclusively on wireless service.

Video Services

Depending on geographic market availability, our video services range from limited basic service to advanced digital television, which includes several plans, each with hundreds of local, national and music channels including premium and pay-per-view channels as well as video on-demand service. Certain customers may also subscribe to our advanced video services, which consist of high-definition television, digital video recorders ("DVR") and/or a whole home DVR. Video services revenues decreased \$0.3 million or \$1.9 million, excluding the additional revenue from FairPoint of \$1.6 million during the quarter ended March 31, 2018 compared to the same period in 2017 primarily due to a 10% decrease in connections as consumers are choosing to subscribe to alternative video services such as OTT content.

Voice Services

We offer several different basic local phone service packages and long-distance calling plans, including unlimited flat-rate calling plans. The plans include options for voicemail and other custom calling features such as caller ID, call forwarding and call waiting. Voice services revenues increased \$39.0 million during the quarter ended March 31, 2018 compared to

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the same period in 2017 primarily due to additional revenue of \$40.1 million from the acquisition of FairPoint. Excluding FairPoint, voice services revenues decreased \$1.1 million during the quarter ended March 31, 2018 primarily due to an 8% decline in access lines. The number of local access lines in service directly affects the recurring revenues we generate from end users and continues to be impacted by the industry-wide decline in access lines. We expect to continue to experience erosion in voice connections due to competition from alternative technologies, including our own competing VoIP product.

Subsidies

Subsidies consist of both federal and state subsidies, which are designed to promote widely available, quality broadband services at affordable prices with higher data speeds in rural areas. Subsidies revenues increased \$14.7 million during the quarter ended March 31, 2018 compared to the same period in 2017 primarily due to additional revenue of \$11.8 million from the acquisition of FairPoint and a settlement for frozen local switching support (“LSS”) of \$4.9 million recognized during the quarter ended March 31, 2018. The increase was reduced in part by the scheduled reduction in the annual Connect America Fund (“CAF”) Phase II funding rate in August 2017 and a decrease in state funding support for our Texas Incumbent Local Exchange Carrier (“ILEC”). See the “Regulatory Matters” section below for further discussion of the LSS matter as well as the subsidies we receive.

Network Access Services

Network access services include interstate and intrastate switched access revenues, network special access services and end user access. Switched access revenues include access services to other communications carriers to terminate or originate long-distance calls on our network. Special access circuits provide dedicated lines and trunks to business customers and interexchange carriers. Network access revenues increased \$25.2 million during the quarter ended March 31, 2018 compared to the same period in 2017 primarily due to additional revenue of \$26.7 million from the acquisition of FairPoint. Excluding FairPoint, network access services revenues decreased \$1.5 million during the quarter ended March 31, 2018 primarily as a result of the continuing decline in minutes of use, voice connections and carrier circuits; however, a portion of the decrease can be attributed to carriers shifting to our fiber Metro Ethernet product, contributing to the growth in that area.

Other Products and Services

Other products and services include revenues from telephone directory publishing, video advertising, billing and support services and other miscellaneous revenue. Other products and services revenues decreased \$0.4 million or \$0.7 million excluding the additional revenue from FairPoint of \$0.3 million during the quarter ended March 31, 2018 compared to the same period in 2017 primarily due to a decline in telephone directory advertising revenues.

Operating Expenses

Cost of Services and Products

Cost of services and products increased \$81.9 million during the quarter ended March 31, 2018 compared to the same period in 2017 due to the acquisition of FairPoint which accounted for \$79.2 million of the increase. Excluding FairPoint, cost of services and products increased \$2.7 million during the quarter ended March 31, 2018, primarily due to an increase in employee salaries and benefits in 2018. Access expense also increased due to new recurring circuit and co-location costs as a result of an increase in commercial services. However, video programming costs decreased as a result of an 8% decline in video connections, which was offset in part by an increase in programming costs per channel as costs continue to rise as a result of annual rate increases.

Selling, General and Administrative Costs

Selling, general and administrative costs increased \$49.3 million during the quarter ended March 31, 2018 compared to the same period in 2017. The acquisition of FairPoint contributed \$47.0 million of the increase. Excluding FairPoint, selling, general and administrative costs increased \$2.3 million during the quarter ended March 31, 2018 primarily due to

an increase in professional fees for legal, audit and tax services. Advertising expense also increased due to an increase in radio advertising and marketing promotions in 2018. In addition, regulatory fees increased for additional reserves in 2018 related to disputed tax assessments. However, sales commissions declined as a result of the adoption of ASC 606 in 2018, which requires contract acquisition costs to be deferred and amortized over the contract performance period. In 2017, these costs were expensed as incurred.

Acquisition and Other Transaction Costs

Acquisition and other transaction costs decreased \$0.6 million during the quarter ended March 31, 2018 compared to the same period in 2017 as a result of the acquisition of FairPoint, which closed in July 2017. Transaction costs consist primarily of legal, finance and other professional fees incurred in connection with the Merger as well as expenses related to change-in-control payments to former employees of the acquired company.

Depreciation and Amortization

Depreciation and amortization expense increased \$65.7 million during the quarter ended March 31, 2018 compared to the same period in 2017, primarily as a result of the acquisition of FairPoint which accounted for \$69.7 million of the increase. Excluding FairPoint, depreciation and amortization expense decreased \$4.0 million during the quarter ended March 31, 2018 due to certain assets and intangibles becoming fully depreciated or amortized in 2017, which was offset in part by ongoing capital expenditures related to network enhancements and success-based capital projects for consumer and commercial services.

Reclassifications

Certain amounts in our 2017 condensed consolidated financial statements have been reclassified to conform to the current year presentation. In accordance with the adoption of ASU No. 2017-07, *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*, certain components of net periodic benefit cost were reclassified from operating expense to non-operating income (expense) in our condensed consolidated statement of operations. In addition, the classifications of certain operating revenues have been reclassified based on a new methodology following the acquisition of FairPoint. These reclassifications had no effect on total revenue or net income.

Regulatory Matters

Our revenues are subject to broad federal and/or state regulation, which include such telecommunications services as local telephone service, network access service and toll service and are derived from various sources, including:

- Business and residential subscribers of basic exchange services;
- Surcharges mandated by state commissions and the Federal Communications Commission (“FCC”);
- Long distance carriers for network access service;
- Competitive access providers and commercial customers for network access service; and
- Support payments from federal or state programs.

The telecommunications industry is subject to extensive federal, state and local regulation. Under the Telecommunications Act of 1996, federal and state regulators share responsibility for implementing and enforcing statutes and regulations designed to encourage competition and to preserve and advance widely available, quality telephone service at affordable prices.

At the federal level, the FCC generally exercises jurisdiction over facilities and services of local exchange carriers, such as our rural telephone companies, to the extent they are used to provide, originate or terminate interstate or international communications. The FCC has the authority to condition, modify, cancel, terminate or revoke our operating authority for

failure to comply with applicable federal laws or FCC rules, regulations and policies. Fines or penalties also may be imposed for any of these violations.

State regulatory commissions generally exercise jurisdiction over carriers' facilities and services to the extent they are used to provide, originate or terminate intrastate communications. In particular, state regulatory agencies have substantial oversight over interconnection and network access by competitors of our incumbent local exchange companies. In addition, municipalities and other local government agencies regulate the public rights-of-way necessary to install and operate networks. State regulators can sanction our rural telephone companies or revoke our certifications if we violate relevant laws or regulations.

FCC Matters

In general, telecommunications service in rural areas is more costly to provide than service in urban areas. The lower customer density means that switching and other facilities serve fewer customers and loops are typically longer, requiring greater expenditures per customer to build and maintain. By supporting the high-cost of operations in rural markets, Universal Service Fund ("USF") subsidies promote widely available, quality telephone service at affordable prices in rural areas.

An order adopted by the FCC in 2011 (the "Order") has significantly impacted the amount of support revenue we receive from the USF, CAF and intercarrier compensation ("ICC"). The Order reformed core parts of the USF, broadly recast the existing ICC scheme, established the CAF to replace support revenues provided by the current USF and redirected support from voice services to broadband services. In 2012, CAF Phase I was implemented, which froze USF support to price cap carriers until the FCC implemented a broadband cost model to shift support from voice services to broadband services. The Order also modified the methodology used for ICC traffic exchanged between carriers. The initial phase of ICC reform was effective on July 1, 2012, beginning the transition of our terminating switched access rates to bill-and-keep over a seven year period for our price cap study areas and nine years for our rate of return study areas, and as a result, we anticipate that our network access revenue for 2018 will be reduced by approximately \$3.0 million.

In December 2014, the FCC released a report and order that addressed, among other things, the transition to CAF Phase II funding for price cap carriers and the acceptance criteria for CAF Phase II funding. For companies that accept the CAF Phase II funding, there is a three year transition period in instances in which their current CAF Phase I funding exceeds the CAF Phase II funding. If CAF Phase II funding exceeds CAF Phase I funding, the transitional support is waived and CAF Phase II funding begins immediately. Companies are required to commit to a statewide build out requirement to 10 Mbps downstream and 1 Mbps upstream in funded locations.

We accepted the CAF Phase II funding in August 2015, which was effective as of January 1, 2015. The annual funding under CAF Phase I of \$36.6 million was replaced by annual funding under CAF Phase II of \$13.9 million through 2020. With the sale of our Iowa ILEC in 2016, this amount was further reduced to \$11.5 million through 2020. Subsequently, with the acquisition of FairPoint, this amount increased to \$48.9 million through 2020. FairPoint accepted the annual CAF Phase II funding of \$37.4 million through 2020 in August 2015. This includes CAF Phase II support in all of FairPoint's operating states except Colorado and Kansas where the offered CAF Phase II support was declined. We continue to receive frozen CAF Phase I support in Colorado and Kansas until such time as the FCC CAF Phase II auction assigns support to another provider. The acceptance of CAF Phase II funding at a level lower than the frozen CAF Phase I support results in CAF Phase II transitional funding over a three year period based on the difference between the CAF Phase I funding and the CAF Phase II funding at the rates of 75% in the first year, 50% in the second year and 25% in the third year.

The specific obligations associated with CAF Phase II funding include the obligation to serve approximately 126,900 locations 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 Mbps per second down and 1 Mbps 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. The Company met this milestone for 2017 and as of March 31, 2018, we are on target to achieve the 2018 milestone.

Local Switching Support

In 2015, FairPoint filed a Petition with the FCC asking the FCC to direct National Exchange Carrier Association (“NECA”) to stop subtracting frozen LSS from FairPoint’s ICC Eligible Recovery for FairPoint’s rate of return ILECs that participate in the NECA pooling process. This issue is unique to rate of return affiliates of price cap carriers because such companies are considered price cap carriers for the FCC’s CAF funding, but remain rate of return for ICC purposes. Effective January 1, 2012, FairPoint rate of return ILECs were placed under the price cap CAF Phase I interim support mechanism, whereby the ILECs continued to receive frozen USF support for all forms of USF support received during 2011, including LSS. The rate of return rules for ICC included LSS support in that mechanism as well; therefore, NECA subtracted the frozen LSS support from the ICC Eligible Recovery amounts in accordance with FCC rules prohibiting duplicate recovery. When FairPoint accepted CAF Phase II support effective January 1, 2015, there was no longer any duplicate support and FairPoint requested NECA to stop subtracting LSS from FairPoint’s ICC Eligible Recovery. NECA declined to make that change, which led to FairPoint filing a Petition with the FCC asking the FCC to direct NECA to comply with FCC rules on ICC Eligible Recovery for rate of return ILECs. This issue also applies to Consolidated’s operations in Minnesota, which are also rate of return ILECs associated with a price cap company. The combined LSS support for the period from January 1, 2015 through December 31, 2017 is approximately \$12.4 million. Our ongoing ICC Eligible Recovery support for 2018 would increase by approximately \$3.6 million, and thereafter, decline by 5% per year through 2021. On March 31, 2018, we obtained the required votes necessary for an approved order and on April 19, 2018, the FCC issued its order approving our petition. As a result, during the quarter ended March 31, 2018, we recognized subsidies revenue of \$4.9 million and a contingent asset of \$8.4 million as a pre-acquisition gain contingency for the FairPoint LSS revenue prior to the acquisition date.

FCC Rules for Business Data Services

On April 20, 2017, the FCC adopted new rules for Business Data Services (“BDS”) which went into effect August 1, 2017. BDS services are high speed data services provided on a point to point basis. The rules apply to interstate BDS services in areas served by price cap carriers. Under the new BDS rules, all packet-switched services and all transport services, channel terminations connecting wholesale customers to our networks and end user channel terminations in counties deemed competitive are competitive. End user channel terminations for DS0, DS1 and DS3 services are non-competitive in counties deemed by the FCC to be non-competitive, but are eligible for Phase I price flexibility. The FCC published a list of counties deemed competitive and non-competitive. Geographic areas previously under Phase II price flexibility will not be rate regulated for any BDS services.

In our price cap operations we can continue to offer competitive BDS services under tariff or we can remove the services from tariff. All competitive services must be detariffed within three years of the effective date of the BDS rules. We have complete price flexibility for BDS services deemed competitive.

BDS services are subject to vigorous competition. We cannot determine the impact of the BDS rules on our revenues or operations.

State Matters

California

In an ongoing proceeding relating to the New Regulatory Framework, the California Public Utilities Commission (“CPUC”) adopted Decision 06-08-030 in 2006, which grants carriers broader pricing freedom in the provision of telecommunications services, bundling of services, promotions and customer contracts. This decision adopted a new regulatory framework, the Uniform Regulatory Framework (“URF”), which among other things (i) eliminates price regulation and allows full pricing flexibility for all new and retail services, (ii) allows new forms of bundles and promotional packages of telecommunication services, (iii) allocates all gains and losses from the sale of assets to shareholders and (iv) eliminates almost all elements of rate of return regulation, including the calculation of shareable earnings. In December 2010, the CPUC issued a ruling to initiate a new proceeding to assess whether, or to what extent, the level of competition in the telecommunications industry is sufficient to control prices for the four largest ILECs in the state. Subsequently, the CPUC issued a ruling temporarily deferring the proceeding. When the CPUC may open this

proceeding is unclear and on hold at this time. The CPUC's actions in this and future proceedings could lead to new rules and an increase in government regulation. The Company will continue to monitor this matter.

Texas

The Texas Public Utilities Regulatory Act ("PURA") directs the Public Utilities Commission of Texas ("PUCT") to adopt and enforce rules requiring local exchange carriers to contribute to a state universal service fund that helps telecommunications providers offer basic local telecommunications service at reasonable rates in high-cost rural areas. The Texas Universal Service Fund is also used to reimburse telecommunications providers for revenues lost by providing lifeline service. Our Texas rural telephone companies receive disbursements from this fund.

Our Texas ILECs have historically received support from two state funds, the small and rural incumbent local exchange company plan High Cost Fund ("HCF") and the High Cost Assistance Fund ("HCAF"). The HCF is a line-based fund used to keep local rates low. The rate is applied on all residential lines and up to five single business lines. The amount we receive from the HCAF is a frozen monthly amount that was originally developed to offset high intrastate toll rates.

In September 2011, the Texas state legislature passed Senate Bill No. 980/House Bill No. 2603 which, among other things, mandated the PUCT to review the Universal Service Fund and issue recommendations by January 1, 2013 with the intent to effectively reduce the size of the Universal Service Fund. This would be accomplished by implementing an urban floor to offset state funding reductions with a phase-in period of four years. The PUCT recommended that (i) frozen line counts be lifted effective September 1, 2013 and (ii) rural and urban local rate benchmarks be developed. The large company fund review was completed in September 2012 and the PUCT addressed the small fund participants in Docket 41097 *Rate Rebalancing* ("Docket 41097"), as discussed below.

In June 2013, the Texas state legislature passed Senate Bill No. 583 ("SB 583"). The provisions of SB 583 were effective September 1, 2013 and froze HCF and HCAF support for the remainder of 2013. As of January 1, 2014, our annual \$1.4 million HCAF support was eliminated and the frozen HCF support returned to funding on a per line basis. In July 2013, the Company entered into a settlement agreement with the PUCT on Docket 41097, which was approved by the PUCT in August 2013. In accordance with the provisions of the settlement agreement, the HCF draw will be reduced by approximately \$1.2 million annually over a four year period beginning June 1, 2014 through 2018. However, we have the ability to fully offset this reduction with increases to residential rates where market conditions allow.

In addition, the PUCT is required to develop a needs test for post-2017 funding and has held workshops on various proposals. The PUCT issued its recommendation to the Texas state commissioners in May 2014, which was approved in December 2014. The needs test allows for a one-time disaggregation of line rates from a per line flat rate, then a competitive test must be met to receive funding. The Company filed its submission for the needs test on December 28, 2016. The PUCT issued docket 46699 on January 4, 2017 to review the filing and a decision was granted in the second quarter of 2017. The order eliminated per line support for two of our exchanges resulting in a decline in annual revenues of approximately \$0.4 million in 2018. All other exchanges continue to receive per line support.

New York

With the acquisition of FairPoint, we assumed grants from the NY Broadband Program (the "NYBB"). In 2015, New York established the \$500 million NYBB to provide state grant funding to support projects that deliver high-speed Internet access to unserved and underserved areas with a goal of achieving statewide broadband access in New York by the end of 2018.

FairPoint received and accepted award letters in March 2017 for grant awards totaling \$36.7 million from the NYBB Phase 2 grants. These grants will support, in part, the extension and upgrading of high-speed broadband services to over 10,321 locations in our New York service territory. During the second quarter of 2017, a bid for Phase 3 grants was submitted by FairPoint, the final phase of the NYBB grants. On January 31, 2018, the state notified us that we were awarded a portion of our Phase 3 bid, and we are currently reviewing the grant. We expect to treat the Phase 2 reimbursements as a contribution in aid of construction given the nature of the arrangement.

To be eligible for the grant, the network must be capable of delivering speeds of 100 Mbps or greater in unserved and underserved locations. As a condition of the grant, we are required to offer the NYBB's Required Pricing Tier as a service option to residential users for a period of five years from completion of construction of the network. This pricing requirement will provide for broadband Internet service at minimum speeds of 25/4 Mbps (download/upload).

FairPoint Merger Requirements

As part of our acquisition of FairPoint, we have regulatory commitments that vary by state, some of which require capital investments in our network over several years through 2020. The requirements include improved data speeds and other service quality improvements in select locations primarily in our Northern New England, New York and Illinois markets. In New Hampshire and Vermont, we are required to invest 13% and 14%, respectively, of total state revenues in capital improvements per year for 2018, 2019 and 2020. For our service territory in Maine, we are required to make capital expenditures of \$16.4 million per year from 2018 through 2020. In addition, we are required to invest an incremental \$1.0 million per year in each of these three states for service quality improvements. In New York, we are required to invest \$4.0 million over three years to expand the broadband network to over 300 locations. In Illinois, we are required to invest an additional \$1.0 million by December 31, 2018 to increase broadband availability and speeds in areas we serve by the FairPoint Illinois ILECs. We achieved all of the 2017 requirements and, as of March 31, 2018, we expect to achieve all of the 2018 requirements.

Other Regulatory Matters

We are also subject to a number of regulatory proceedings occurring at the federal and state levels that may have a material impact on our operations. The FCC and state commissions have authority to issue rules and regulations related to our business. A number of proceedings are pending or anticipated that are related to such telecommunications issues as competition, interconnection, access charges, intercarrier compensation, broadband deployment, consumer protection and universal service reform. Some proceedings may authorize new services to compete with our existing services. Proceedings that relate to our cable television operations include rulemakings on set top boxes, carriage of programming, industry consolidation and ways to promote additional competition. There are various on-going legal challenges to the scope or validity of FCC orders that have been issued. As a result, it is not yet possible to fully determine the impact of the related FCC rules and regulations on our operations.

Non-Operating Items

Other Income and Expense, Net

Interest expense, net of interest income, increased \$3.0 million during the quarter ended March 31, 2018 compared to the same period in 2017 primarily due to the issuance of the \$935.0 million incremental term loan during the quarter ended September 30, 2017, which was reduced in part by the ticking fees and the amortization of commitment fees incurred in 2017 related to the committed financing secured for the acquisition of FairPoint, as described in the "Liquidity and Capital Resources" section below. Interest expense also increased as a result of a loss recognized on the change in fair value of our de-designated interest rate swap agreements during the quarter ended March 31, 2018.

Other income increased \$3.7 million during the quarter ended March 31, 2018 compared to the same period in 2017 primarily due to an increase in investment income of \$2.5 million from our wireless partnership interests and a decrease in pension and post-retirement expense in the current year period of \$0.8 million.

Income Taxes

Income taxes decreased \$2.0 million during the quarter ended March 31, 2018 compared to the same period in 2017. Our effective tax rate was 27.5% and 37.0% for the quarters ended March 31, 2018 and 2017, respectively. The primary driver of the lower rate in 2018, compared to the same period in 2017, is the change in the corporate tax rate from 35% to 21% due to the enactment of the Tax Cuts and Jobs Act of 2017. The effective tax rate differed from the federal and state statutory rates primarily due to various permanent income tax differences and differences in allocable income for the Company's state tax filings.

Non-GAAP Measures

In addition to the results reported in accordance with US GAAP, we also use certain non-GAAP measures such as EBITDA and adjusted EBITDA to evaluate operating performance and to facilitate the comparison of our historical results and trends. These financial measures are not measures of financial performance under US GAAP and should not be considered in isolation or as a substitute for net income as a measure of performance and net cash provided by operating activities as a measure of liquidity. They are not, on their own, necessarily indicative of cash available to fund cash needs as determined in accordance with GAAP. The calculation of these non-GAAP measures may not be comparable to similarly titled measures used by other companies. Reconciliations of these non-GAAP measures to the most directly comparable financial measures presented in accordance with GAAP are provided below.

EBITDA is defined as net earnings before interest expense, income taxes and depreciation and amortization. Adjusted EBITDA is comprised of EBITDA, adjusted for certain items as permitted or required under our credit facility as described in the reconciliations below. These measures are a common measure of operating performance in the telecommunications industry and are useful, with other data, as a means to evaluate our ability to fund our estimated uses of cash.

The following table is a reconciliation of net income (loss) to adjusted EBITDA for the quarters ended March 31, 2018 and 2017:

| <i>(In thousands, unaudited)</i> | Quarter Ended March 31, | |
|---|----------------------------|------------------|
| | 2018 | 2017 |
| Net loss | \$ (11,198) | \$ (3,705) |
| Add (subtract): | | |
| Interest expense, net of interest income | 32,716 | 29,671 |
| Income tax benefit | (4,248) | (2,174) |
| Depreciation and amortization | <u>107,899</u> | <u>42,195</u> |
| EBITDA | 125,169 | 65,987 |
| Adjustments to EBITDA: | | |
| Other, net ⁽¹⁾ | (265) | (1,045) |
| Investment distributions ⁽²⁾ | 9,470 | 5,644 |
| Non-cash, stock-based compensation ⁽³⁾ | 678 | 538 |
| Adjusted EBITDA | <u>\$ 135,052</u> | <u>\$ 71,124</u> |

(1) Includes the equity earnings from our investments, dividend income, income attributable to noncontrolling interests in subsidiaries, acquisition and transaction related costs, including severance, non-cash pension and post-retirement benefits and certain other miscellaneous items.

(2) Includes all cash dividends and other cash distributions received from our investments.

(3) Represents compensation expenses in connection with the issuance of stock awards, which, because of the non-cash nature of these expenses, are excluded from adjusted EBITDA.

Liquidity and Capital Resources

Outlook and Overview

Our operating requirements have historically been funded from cash flows generated from our business and borrowings under our credit facilities. We expect that our future operating requirements will continue to be funded from cash flows from operating activities, existing cash and cash equivalents and, if needed, borrowings under our revolving credit facility and our ability to obtain future external financing. We anticipate that we will continue to use a substantial portion of our cash flow to fund capital expenditures, meet scheduled payments of long-term debt, make dividend payments and invest in future business opportunities.

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The following table summarizes our cash flows:

| <i>(In thousands)</i> | Three Months Ended March 31, | |
|---------------------------------------|------------------------------|-----------|
| | 2018 | 2017 |
| Cash flows provided by (used in): | | |
| Operating activities | \$ 90,842 | \$ 51,718 |
| Investing activities | (60,431) | (28,982) |
| Financing activities | (34,928) | (23,184) |
| Decrease in cash and cash equivalents | \$ (4,517) | \$ (448) |

Cash Flows Provided by Operating Activities

Net cash provided by operating activities was \$90.8 million during the three-month period ended March 31, 2018, an increase of \$39.1 million compared to the same period in 2017. Cash flows provided by operating activities increased primarily as a result of the additional cash flows provided by the addition of the FairPoint operations in 2018 as well as additional transaction costs paid in 2017 related to the acquisition of FairPoint. Cash distributions received from our wireless partnerships also increased \$3.9 million during the three-month period ended March 31, 2018 compared to the same period in 2017.

Cash Flows Used In Investing Activities

Net cash used in investing activities was \$60.4 million during the three-month period ended March 31, 2018 and consisted primarily of cash used for capital expenditures.

Capital Expenditures

Capital expenditures continue to be our primary recurring investing activity and were \$60.8 million during the three-month period ended March 31, 2018, an increase of \$31.8 million compared to the same period in 2017 driven by the acquisition of FairPoint in the quarter ended September 30, 2017. Capital expenditures for the remainder of 2018 are expected to be \$175.0 million to \$180.0 million, of which approximately 50% is planned for success-based capital projects for consumer and commercial initiatives. Capital expenditures for the remainder of 2018 and subsequent years will depend on various factors, including competition, changes in technology, regulatory changes and the timing in the deployment of new services. We expect to continue to invest in existing and new services and the expansion of our fiber network in order to retain and acquire more customers through a broader set of products and an expanded network footprint.

Cash Flows Used In Financing Activities

Net cash used in financing activities consists primarily of our proceeds from and principal payments on long-term borrowings and the payment of dividends.

Long-term Debt

Credit Agreement

In October 2016, the Company, through certain of its wholly owned subsidiaries, entered into a Third Amended and Restated Credit Agreement with various financial institutions (as amended, the "Credit Agreement"). The Credit Agreement consists of a \$110.0 million revolving credit facility, an initial term loan in the aggregate amount of \$900.0 million (the "Initial Term Loan") and an incremental term loan in the aggregate amount of \$935.0 million (the "Incremental Term Loan"), collectively (the "Term Loans"). The Incremental Term Loan was issued on July 3, 2017 upon completion of the FairPoint Merger, as described below. The Credit Agreement also includes an incremental loan facility which provides the ability to borrow, subject to certain terms and conditions, incremental loans in an aggregate amount of up to the greater of (a) \$300.0 million and (b) an amount which would cause its senior secured leverage ratio not to exceed 3.00:1.00 (the "Incremental Facility"). Borrowings under the Credit Agreement are secured by substantially all of the

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assets of the Company and its subsidiaries, including certain of the FairPoint subsidiaries acquired in the Merger, with the exception of Consolidated Communications of Illinois Company and our majority-owned subsidiary, East Texas Fiber Line Incorporated.

The Initial Term Loan was issued in an original aggregate principal amount of \$900.0 million with a maturity date of October 5, 2023, but is subject to earlier maturity on March 31, 2022 if the Company's unsecured Senior Notes due in October 2022 are not repaid in full or redeemed in full on or prior to March 31, 2022. The Initial Term Loan contains an original issuance discount of 0.25% or \$2.3 million, which is being amortized over the term of the loan. The Initial Term Loan requires quarterly principal payments of \$2.25 million and has an interest rate of 3.00% plus the London Interbank Offered Rate ("LIBOR") subject to a 1.00% LIBOR floor.

In connection with the execution of the Merger Agreement, in December 2016, the Company entered into two amendments to its Credit Agreement to secure committed financing related to the acquisition of FairPoint. On December 14, 2016, we entered into Amendment No. 1 to the Credit Agreement and on December 21, 2016, the Company entered into Amendment No. 2 to the Credit Agreement, pursuant to which a syndicate of lenders agreed to provide an incremental term loan in an aggregate principal amount of up to \$935.0 million under the Credit Agreement, subject to the satisfaction of certain conditions. The Incremental Term Loan was made pursuant to the Incremental Facility set forth in the Credit Agreement. Fees of \$2.5 million paid to the lenders in connection with Amendment No. 1 are reflected as an additional discount on the Initial Term Loan and are being amortized over the term of the debt as interest expense. Ticking fees accrued on the incremental term loan commitments from January 15, 2017 through the July 3, 2017 Merger closing date at a rate of 3.00% plus LIBOR subject to a 1.00% LIBOR floor and became due and payable on the closing date. In connection with entering into the committed financing, commitment fees of \$14.0 million were capitalized in December 2016 and were amortized to interest expense over the term of the commitment period through July 2017.

On July 3, 2017, the Merger with FairPoint was completed and the net proceeds from the incurrence of the Incremental Term Loan were used, in part, to repay and redeem certain existing indebtedness of FairPoint and to pay certain fees and expenses in connection with the Merger and the related financing. The Incremental Term Loan included an original issue discount of 0.50% and has the same maturity date and interest rate as the Initial Term Loan. The Incremental Term Loan requires quarterly principal payments of \$2.34 million which began in December 2017.

In addition, effective contemporaneously with the Merger, the Company entered into Amendment No. 3 to the Credit Agreement to increase the permitted amount of outstanding letters of credit from \$15.0 million to \$20.0 million and to provide that certain existing letters of credit of FairPoint be deemed to be letters of credit under the Credit Agreement.

Our revolving credit facility has a maturity date of October 5, 2021 and an applicable margin (at our election) of between 2.50% and 3.25% for LIBOR-based borrowings or between 1.50% and 2.25% for alternate base rate borrowings, in each case depending on our total net leverage ratio. Based on our leverage ratio as of March 31, 2018, the borrowing margin for the three month period ending June 30, 2018 will be at a weighted-average margin of 3.00% for a LIBOR-based loan or 2.00% for an alternate base rate loan. The applicable borrowing margin for the revolving credit facility is adjusted quarterly to reflect the leverage ratio from the prior quarter-end. As of March 31, 2018, alternate base rate borrowings of \$22.0 million were outstanding under the revolving credit facility. At December 31, 2017, there were borrowings of \$22.0 million outstanding under the revolving credit facility, which consisted of LIBOR-based borrowings of \$17.0 million and alternate base rate borrowings of \$5.0 million. Stand-by letters of credit of \$18.2 million were outstanding under our revolving credit facility as of March 31, 2018. The stand-by letters of credit are renewable annually and reduce the borrowing availability under the revolving credit facility. As of March 31, 2018, \$69.8 million was available for borrowing under the revolving credit facility.

The weighted-average interest rate on outstanding borrowings under our credit facility was 4.90% and 4.58% as of March 31, 2018 and December 31, 2017, respectively. Interest is payable at least quarterly.

Credit Agreement Covenant Compliance

The Credit Agreement contains various provisions and covenants, including, among other items, restrictions on the ability to pay dividends, incur additional indebtedness and issue certain capital stock. We have agreed to maintain certain financial

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ratios, including interest coverage and total net leverage ratios, all as defined in the Credit Agreement. As of March 31, 2018, we were in compliance with the Credit Agreement covenants.

In general, our Credit Agreement restricts our ability to pay dividends to the amount of our available cash as defined in our Credit Agreement. As of March 31, 2018, and including the \$27.4 million dividend paid on May 1, 2018, we had \$265.3 million in dividend availability under the credit facility covenant.

Under our Credit Agreement, if our total net leverage ratio, as defined in the Credit Agreement, as of the end of any fiscal quarter is greater than 5.10:1.00, we will be required to suspend dividends on our common stock unless otherwise permitted by an exception for dividends that may be paid from the portion of proceeds of any sale of equity not used to fund acquisitions or make other investments. During any dividend suspension period, we will be required to repay debt in an amount equal to 50.0% of any increase in available cash, among other things. In addition, we will not be permitted to pay dividends if an event of default under the Credit Agreement has occurred and is continuing. Among other things, it will be an event of default if our total net leverage ratio or interest coverage ratio as of the end of any fiscal quarter is greater than 5.25:1.00 or less than 2.25:1.00, respectively. As of March 31, 2018, our total net leverage ratio under the Credit Agreement was 4.15:1.00, and our interest coverage ratio was 5.01:1.00.

6.50% Senior Notes due 2022

In September 2014, we completed an offering of \$200.0 million aggregate principal amount of 6.50% Senior Notes due in October 2022 (the “Existing Notes”). The Existing Notes were priced at par, which resulted in total gross proceeds of \$200.0 million. On June 8, 2015, we completed an additional offering of \$300.0 million in aggregate principal amount of 6.50% Senior Notes due 2022 (the “New Notes” and together with the Existing Notes, the “Senior Notes”). The New Notes were issued as additional notes under the same indenture pursuant to which the Existing Notes were previously issued on in September 2014. The New Notes were priced at 98.26% of par with a yield to maturity of 6.80% and resulted in total gross proceeds of approximately \$294.8 million, excluding accrued interest. The discount is being amortized using the effective interest method over the term of the notes.

The Senior Notes mature on October 1, 2022 and interest is payable semi-annually on April 1 and October 1 of each year. Consolidated Communications, Inc. (“CCI”) is the primary obligor under the Senior Notes, and we and certain of our wholly-owned subsidiaries, including certain FairPoint subsidiaries, have fully and unconditionally guaranteed the Senior Notes. The Senior Notes are senior unsecured obligations of the Company.

Senior Notes Covenant Compliance

Subject to certain exceptions and qualifications, the indenture governing the Senior Notes contains customary covenants that, among other things, limits CCI’s and its restricted subsidiaries’ ability to: incur additional debt or issue certain preferred stock; pay dividends or make other distributions on capital stock or prepay subordinated indebtedness; purchase or redeem any equity interests; make investments; create liens; sell assets; enter into agreements that restrict dividends or other payments by restricted subsidiaries; consolidate, merge or transfer all or substantially all of its assets; engage in transactions with its affiliates; or enter into any sale and leaseback transactions. The indenture also contains customary events of default.

Among other matters, the Senior Notes indenture provides that CCI may not pay dividends or make other restricted payments, as defined in the indenture, if its total net leverage ratio is 4.75:1.00 or greater. This ratio is calculated differently than the comparable ratio under the Credit Agreement; among other differences, it takes into account, on a pro forma basis, synergies expected to be achieved as a result of certain acquisitions not yet reflected in historical results. As of March 31, 2018, this ratio was 4.21:1.00. If this ratio is met, dividends and other restricted payments may be made from cumulative consolidated cash flow since April 1, 2012, less 1.75 times fixed charges, less dividends and other restricted payments made since May 30, 2012. Dividends may be paid and other restricted payments may also be made from a “basket” of \$50.0 million, none of which has been used to date, and pursuant to other exceptions identified in the indenture. Since dividends of \$460.9 million have been paid since May 30, 2012, including the quarterly dividend declared in February 2017 and paid on May 1, 2018, there was \$935.4 million of the \$1,396.4 million of cumulative consolidated cash flow

since May 30, 2012 available to pay dividends as of March 31, 2018. As of March 31, 2018, the Company was in compliance with all terms, conditions and covenants under the indenture governing the Senior Notes.

Capital Leases

We lease certain facilities and equipment under various capital leases which expire between 2018 and 2027. As of March 31, 2018, the present value of the minimum remaining lease commitments was approximately \$35.1 million, of which \$13.2 million was due and payable within the next twelve months. The leases require total remaining rental payments of \$41.7 million as of March 31, 2018, of which \$2.6 million will be paid to LATEL LLC, a related party entity.

Dividends

We paid \$27.4 million and \$19.6 million in dividend payments to stockholders during the quarters ended March 31, 2018 and 2017, respectively. In February 2018, our board of directors declared a quarterly dividend of \$0.38738 per common share, which was paid on May 1, 2018 to stockholders of record at the close of business on April 15, 2018. Our current annual dividend rate is approximately \$1.55 per share.

The cash required to fund dividend payments is in addition to our other expected cash needs, which we expect to fund with cash flows from our operations. In addition, we expect we will have sufficient availability under our revolving credit facility to fund dividend payments in addition to any expected fluctuations in working capital and other cash needs, although we do not intend to borrow under this facility to pay dividends.

We believe that our dividend policy will limit, but not preclude, our ability to grow. If we continue paying dividends at the level currently anticipated under our dividend policy, we may not retain a sufficient amount of cash, and may need to seek refinancing to fund a material expansion of our business, including any significant acquisitions or to pursue growth opportunities requiring capital expenditures significantly beyond our current expectations. In addition, because we expect a significant portion of cash available will be distributed to holders of common stock under our dividend policy, our ability to pursue any material expansion of our business will depend more than it otherwise would on our ability to obtain third-party financing.

Sufficiency of Cash Resources

The following table sets forth selected information regarding our financial condition.

| <i>(In thousands, except for ratio)</i> | March 31, 2018 | December 31, 2017 |
|---|-------------------|----------------------|
| Cash and cash equivalents | \$ 11,140 | \$ 15,657 |
| Working capital (deficit) | (44,738) | (42,281) |
| Current ratio | 0.84 | 0.83 |

Our net working capital position declined \$2.5 million as of March 31, 2018 compared to December 31, 2017 primarily as a result of an increase in accrued interest and accrued expense related to the timing of the semi-annual interest payments for our Senior Notes and the timing of expenditures. This increase was reduced in part by an increase in accounts receivable as a result of the LSS settlement of \$13.3 million recognized during the quarter ended March 31, 2018.

Our most significant uses of funds in the remainder of 2018 are expected to be for: (i) dividend payments of approximately \$82.0 million; (ii) interest payments on our indebtedness of approximately \$104.0 million and principal payments on debt of \$13.8 million; and (iii) capital expenditures of between \$175.0 million and \$180.0 million. In the future our ability to use cash may be limited by our other expected uses of cash, including our dividend policy, and our ability to incur additional debt will be limited by our existing and future debt agreements.

We believe that cash flows from operating activities, together with our existing cash and borrowings available under our revolving credit facility, will be sufficient for at least the next twelve months to fund our current anticipated uses of cash. After that, our ability to fund these expected uses of cash and to comply with the financial covenants under our debt agreements will depend on the results of future operations, performance and cash flow. Our ability to fund these expected

uses from the results of future operations will be subject to prevailing economic conditions and to financial, business, regulatory, legislative and other factors, many of which are beyond our control.

We may be unable to access the cash flows of our subsidiaries since certain of our subsidiaries are parties to credit or other borrowing agreements, or are subject to statutory or regulatory restrictions, that restrict the payment of dividends or making intercompany loans and investments, and those subsidiaries are likely to continue to be subject to such restrictions and prohibitions for the foreseeable future. In addition, future agreements that our subsidiaries may enter into governing the terms of indebtedness may restrict our subsidiaries' ability to pay dividends or advance cash in any other manner to us.

To the extent that our business plans or projections change or prove to be inaccurate, we may require additional financing or require financing sooner than we currently anticipate. Sources of additional financing may include commercial bank borrowings, other strategic debt financing, sales of nonstrategic assets, vendor financing or the private or public sales of equity and debt securities. There can be no assurance that we will be able to generate sufficient cash flows from operations in the future, that anticipated revenue growth will be realized or that future borrowings or equity issuances will be available in amounts sufficient to provide adequate sources of cash to fund our expected uses of cash. Failure to obtain adequate financing, if necessary, could require us to significantly reduce our operations or level of capital expenditures which could have a material adverse effect on our financial condition and the results of operations.

Surety Bonds

In the ordinary course of business, we enter into surety, performance and similar bonds as required by certain jurisdictions in which we provide services. As of March 31, 2018, we had approximately \$5.0 million of these bonds outstanding.

Defined Benefit Pension Plans

As required, we contribute to a qualified defined pension plan (the "Retirement Plan") and non-qualified supplemental retirement plans (the "Supplemental Plans") and other post-retirement benefit plans, which provide retirement benefits to certain eligible employees. In connection with the acquisition of FairPoint, we have assumed sponsorship of its two non-contributory qualified defined benefit pension plans (collectively with the Retirement Plan and Supplemental Plans, the "Pension Plans") and post-retirement benefit plan as of the date of acquisition as described in the Note 9 to the Condensed Consolidated Financial Statements, included in this report in Part I – Item 1 "Financial Statements". Contributions are intended to provide for benefits attributed to service to date. Our funding policy is to contribute annually an actuarially determined amount consistent with applicable federal income tax regulations.

The cost to maintain our Pension Plans and future funding requirements are affected by several factors including the expected return on investment of the assets held by the Pension Plans, changes in the discount rate used to calculate pension expense and the amortization of unrecognized gains and losses. Returns generated on the Pension Plans assets have historically funded a significant portion of the benefits paid under the Pension Plans. We estimate the weighted average long-term rate of return on assets will be 7.03%. The Pension Plans invest in marketable equity securities which are exposed to changes in the financial markets. If the financial markets experience a downturn and returns fall below our estimate, we could be required to make a material contribution to the Pension Plans, which could adversely affect our cash flows from operations.

In 2018, we expect to make contributions totaling approximately \$26.9 million to our Pension Plans and \$10.0 million to our other post-retirement benefit plans, which represents an increase of \$17.9 million from the total contributions made in 2017 of which \$12.0 million is attributable to the acquisition of FairPoint. As of March 31, 2018, we have contributed \$4.9 million and \$2.5 million to our Pension Plans and our other post-retirement benefit plans, respectively. Our contribution amounts meet the minimum funding requirements as set forth in employee benefit and tax laws.

Income Taxes

The timing of cash payments for income taxes, which is governed by the Internal Revenue Service and other taxing jurisdictions, will differ from the timing of recording tax expense and deferred income taxes, which are reported in accordance with GAAP. For example, tax laws in effect regarding accelerated or "bonus" depreciation for tax reporting

resulted in less cash payments than the GAAP tax expense. Acceleration of tax deductions could eventually result in situations where cash payments will exceed GAAP tax expense.

Regulatory Matters

As discussed in the “Regulatory Matters” section above, in December 2014, the FCC released a report and order that significantly impacts the amount of support revenue we receive from the USF, CAF and ICC by redirecting support from voice services to broadband services. The annual funding under CAF Phase I of \$36.6 million was replaced by annual funding under CAF Phase II of \$13.9 million through 2020. With the sale of our Iowa ILEC in 2016, this amount was further reduced to \$11.5 million through 2020. Subsequently, with the acquisition of FairPoint, this amount increased to \$48.9 million through 2020. FairPoint accepted the annual CAF Phase II funding of \$37.4 million through 2020 in August 2015. This includes CAF Phase II support in all of FairPoint’s operating states except Colorado and Kansas where the offered CAF Phase II support was declined. We continue to receive frozen CAF Phase I support in Colorado and Kansas until such time as the FCC CAF Phase II auction assigns support to another provider. The acceptance of CAF Phase II funding at a level lower than the frozen CAF Phase I support results in CAF Phase II Transitional funding over a three year period based on the difference between the CAF Phase I funding and the CAF Phase II funding at the rates of 75% in the first year, 50% in the second year and 25% in the third year.

The Order also modifies the methodology used for ICC traffic exchanged between carriers. As a result of implementing the provisions of the Order, our network access revenue decreased approximately \$0.8 million for the quarter ended March 31, 2018 compared to the same period in 2017. We anticipate that network access revenue will continue to decline as a result of the Order through 2018 by as much as \$3.0 million.

In accordance with the provisions of SB 583, as discussed in the “Regulatory Matters” section above, our annual \$1.4 million Texas HCAF support was eliminated effective January 1, 2014. In addition, in accordance with the provisions of the settlement agreement reached with the PUCT, the HCF draw will be reduced by approximately \$1.2 million annually over a four year period beginning June 1, 2014 through 2018. However, we have the ability to fully offset this reduction with increases to residential rates where market conditions allow.

Critical Accounting Estimates

Our condensed consolidated financial statements and accompanying notes are prepared in accordance with US GAAP. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. These estimates and assumptions are affected by management’s application of accounting policies. Our judgments are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making estimates about the carrying values of assets and liabilities that are not readily apparent from other sources. For a full discussion of our accounting estimates and assumptions that we have identified as critical in the preparation of our condensed consolidated financial statements, refer to our 2017 Annual Report on Form 10-K filed with the SEC.

Recent Accounting Pronouncements

For information regarding the impact of certain recent accounting pronouncements, see Note 1 “Summary of Significant Accounting Policies” to the Condensed Consolidated Financial Statements, included in this report in Part I - Item 1 “Financial Statements”.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our exposure to market risk is primarily related to the impact of interest rate fluctuations on our debt obligations. Market risk is the potential loss arising from adverse changes in market interest rates on our variable rate obligations. In order to manage the volatility relating to changes in interest rates, we utilize derivative financial instruments such as interest rate swaps to maintain a mix of fixed and variable rate debt. We do not use derivatives for trading or speculative purposes. Our interest rate swap agreements effectively convert a portion of our floating-rate debt to a fixed-rate basis, thereby reducing the impact of interest rate changes on future cash interest payments. We calculate the potential change in interest

expense caused by changes in market interest rates by determining the effect of the hypothetical rate increase on the portion of our variable rate debt that is not subject to a variable rate floor or hedged through the interest rate swap agreements.

As of March 31, 2018, the majority of our variable rate debt was subject to a 1.00% London Interbank Offered Rate floor thereby reducing the impact of fluctuations in interest rates. Based on our variable rate debt outstanding as of March 31, 2018, a 1.00% change in market interest rates would increase or decrease annual interest expense by approximately \$6.1 million and \$5.4 million, respectively.

As of March 31, 2018, the fair value of our interest rate swap agreements amounted to a net asset of \$3.9 million. Total pre-tax deferred gains related to our interest rate swap agreements included in accumulated other comprehensive loss was \$7.4 million as of March 31, 2018.

ITEM 4. CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (“Exchange Act”) that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. In connection with the filing of this Form 10-Q, management evaluated, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of the design to provide reasonable assurance of achieving their objectives and operation of our disclosure controls and procedures as of March 31, 2018. Based upon that evaluation and subject to the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective as of March 31, 2018.

Changes in Internal Control Over Financial Reporting

Based upon the evaluation performed by our management, which was conducted with the participation of our Chief Executive Officer and Chief Financial Officer, there has been no change in our internal controls over financial reporting during the quarter ended March 31, 2018 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting, except as noted below.

During the quarter ended March 31, 2018, we completed our migration of the enterprise resource planning (“ERP”) system used by FairPoint for financial reporting and human resources to the Company’s ERP system. This effort now provides a single platform for the Company to process financial information and human resources. The combined processes include accounts payable, purchasing, inventory, property, plant and equipment, payroll, general ledger and financial reporting. We believe that the migration to the single ERP system did not result in a negative impact on our internal controls over financial reporting or disclosure controls and procedures. As of March 31, 2018, management is in the process of integrating FairPoint’s internal controls over financial reporting.

Limitations on the Effectiveness of Controls

We are responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control systems are designed to provide reasonable assurance to the Company’s management, Board of Directors and Audit Committee regarding the reliability of financial reporting and the preparation of published financial statements in accordance with generally accepted accounting principles.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time we may be involved in litigation that we believe is of the type common to companies in our industry, including regulatory issues. While the outcome of these claims cannot be predicted with certainty, we do not believe that the outcome of any of these legal matters will have a material adverse impact on our business, results of operations, financial condition or cash flows. See Note 11 to the Condensed Consolidated Financial Statements, included in this report in Part I - Item 1 "Financial Statements" for a discussion of recent developments related to these legal proceedings.

ITEM 6. EXHIBITS

- 31.1 [Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
- 31.2 [Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)
- 32.1 [Certification of the 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 The following financial information from Consolidated Communications Holdings, Inc. Quarterly Report on Form 10-Q for the quarter ended March 31, 2018, formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Statements of Operations, (ii) Condensed Consolidated Statements of Comprehensive Income (Loss), (iii) Condensed Consolidated Balance Sheets, (iv) Condensed Consolidated Statements of Cash Flows, and (v) Notes to Unaudited Condensed Consolidated Financial Statements.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CONSOLIDATED COMMUNICATIONS HOLDINGS, INC.
(Registrant)

May 4, 2018

By: /s/ C. Robert Udell Jr.
C. Robert Udell Jr.,
Chief Executive Officer
(Principal Executive Officer)

May 4, 2018

By: /s/ Steven L. Childers
Steven L. Childers,
Chief Financial Officer
(Principal Financial Officer and Chief Accounting Officer)

CHIEF EXECUTIVE OFFICER CERTIFICATION

I, C. Robert Udell Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Consolidated Communications Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

May 4, 2018

/s/ C. Robert Udell Jr.

C. Robert Udell Jr.
President and Chief Executive Officer
(Principal Executive Officer)

CHIEF FINANCIAL OFFICER CERTIFICATION

I, Steven L. Childers, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Consolidated Communications Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

May 4, 2018

/s/ Steven L. Childers

Steven L. Childers
Chief Financial Officer
(Principal Financial Officer and Chief Accounting Officer)

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 ("Section 906"), C. Robert Udell Jr. and Steven L. Childers, President and Chief Executive Officer and Chief Financial Officer, respectively, of Consolidated Communications Holdings, Inc., each certify that to his knowledge (i) the Quarterly Report on Form 10-Q for the period ended March 31, 2018 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and (ii) the information contained in such report fairly presents, in all material respects, the financial condition and results of operations of Consolidated Communications Holdings, Inc.

/s/ C. Robert Udell Jr.
C. Robert Udell Jr.
President and Chief Executive Officer
(Principal Executive Officer)
May 4, 2018

/s/ Steven L. Childers
Steven L. Childers
Chief Financial Officer
(Principal Financial Officer and Chief Accounting Officer)
May 4, 2018
