WINDSTREAM HOLDINGS, INC.
Form 10-Q
August 03, 2017

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

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

For the quarterly period ended June 30, 2017

or

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

Exact name of registrant as specified in its charter	State or other jurisdiction of incorporation or organization	Commission File Number	I.R.S. Employer Identification No.
Windstream Holdings, Inc.	Delaware	001-32422	46-2847717
Windstream Services, LLC	Delaware	001-36093	20-0792300

4001 Rodney Parham Road Little Rock, Arkansas	72212
(Address of principal executive offices)	(Zip Code)

(501) 748-7000
(Registrants' 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.

Windstream Holdings, Inc. ý YES ¨ NO
Windstream Services, LLC ý 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).
Windstream Holdings, Inc. ý YES ¨ NO
Windstream Services, LLC ý 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:

Windstream Holdings, Inc.	Large accelerated filer ý	Accelerated filer ¨
	Non-accelerated filer ¨	(Do not check if a smaller reporting company)
		Smaller reporting company ¨
		Emerging growth company ¨
Windstream Services, LLC	Large accelerated filer ¨	Accelerated filer ¨
	Non-accelerated filer ý	(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 any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Windstream Holdings, Inc. ¨ YES ¨ NO
Windstream Services, LLC ¨ YES ¨ NO

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

Windstream Holdings, Inc. ¨ YES ý NO
Windstream Services, LLC ¨ YES ý NO

As of July 31, 2017, 190,828,151 shares of common stock of Windstream Holdings, Inc.were outstanding. Windstream Holdings, Inc. holds a 100 percent interest in Windstream Services, LLC.

This Form 10-Q is a combined quarterly report being filed separately by two registrants: Windstream Holdings, Inc. and Windstream Services, LLC. Windstream Services, LLC is a direct, wholly-owned subsidiary of Windstream Holdings, Inc. Accordingly, Windstream Services, LLC meets the conditions set forth in general instruction H(1)(a) and (b) of Form 10-Q and is therefore filing this form with the reduced disclosure format. Unless the context indicates otherwise, the use of the terms “Windstream,” “we,” “us” or “our” shall refer to Windstream Holdings, Inc. and its subsidiaries, including Windstream Services, LLC, and the term “Windstream Services” shall refer to Windstream Services, LLC and its subsidiaries.

The Exhibit Index is located on page 86.

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*No reportable information under this item.

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WINDSTREAM HOLDINGS, INC.
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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

WINDSTREAM HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions, except per share amounts)	2017	2016	2017	2016
Revenues and sales:				
Service revenues	$1,465.6	$1,331.3	$2,810.0	$2,671.9
Product sales	26.0	28.3	47.3	61.1
Total revenues and sales	1,491.6	1,359.6	2,857.3	2,733.0
Costs and expenses:				
Cost of services (exclusive of depreciation and amortization included below)	747.5	667.2	1,429.9	1,336.0
Cost of products sold	29.7	24.2	50.5	53.1
Selling, general and administrative	225.3	196.9	438.6	400.7
Depreciation and amortization	362.4	308.2	700.9	613.0
Merger, integration and other costs	16.4	2.6	73.7	7.6
Restructuring charges	3.5	5.9	10.9	10.3
Total costs and expenses	1,384.8	1,205.0	2,704.5	2,420.7
Operating income	106.8	154.6	152.8	312.3
Dividend income on Uniti common stock	—	—	—	17.6
Other (expense) income, net	(0.1)	(1.9)	0.6	(3.1)
Net gain on disposal of investment in Uniti common stock	—	17.3	—	17.3
Net gain (loss) on early extinguishment of debt	—	37.5	(3.2)	2.1
Other-than-temporary impairment loss on investment in Uniti common stock	—	—	—	(181.9)
Interest expense	(214.4)	(217.4)	(426.2)	(437.1)
Loss before income taxes	(107.7)	(9.9)	(276.0)	(272.8)
Income tax benefit	(39.6)	(11.4)	(96.6)	(42.4)
Net (loss) income	$(68.1)	$1.5	$(179.4)	$(230.4)
Basic and diluted (loss) earnings per share:				
Net (loss) income	($.37)	$.01	($1.15)	($2.48)

See the accompanying notes to the unaudited interim consolidated financial statements.

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WINDSTREAM HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions)	2017	2016	2017	2016
Net (loss) income	$(68.1)	$1.5	$(179.4)	$(230.4)
Other comprehensive (loss) income:				
Available-for-sale securities:				
Unrealized holding gain arising during the period	—	51.5	—	156.1
Gain on disposal recognized in the period	—	(51.5)	—	(51.5)
Other-than-temporary impairment loss recognized in the period	—	—	—	181.9
Change in available-for-sale securities	—	—	—	286.5
Interest rate swaps:				
Unrealized loss on designated interest rate swaps	(5.3)	(3.3)	(1.9)	(11.6)
Amortization of net unrealized losses on de-designated interest rate swaps	1.4	1.0	2.9	2.2
Income tax benefit (expense)	1.5	1.0	(0.4)	3.7
Change in interest rate swaps	(2.4)	(1.3)	0.6	(5.7)
Postretirement and pension plans:				
Change in net actuarial gain for employee benefit plans	1.4	0.4	1.4	0.4
Plan curtailment	—	—	—	(5.5)
Amounts included in net periodic benefit cost:				
Amortization of net actuarial loss	0.1	—	0.1	0.1
Amortization of prior service credits	(0.2)	(0.1)	(0.4)	(0.6)
Income tax (expense) benefit	(0.5)	(0.1)	(0.4)	2.2
Change in postretirement and pension plans	0.8	0.2	0.7	(3.4)
Other comprehensive (loss) income	(1.6)	(1.1)	1.3	277.4
Comprehensive (loss) income	$(69.7)	$0.4	$(178.1)	$47.0

See the accompanying notes to the unaudited interim consolidated financial statements.

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WINDSTREAM HOLDINGS, INC.
CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(Millions, except par value)	June 30, 2017	December 31, 2016
Assets		
Current Assets:		
Cash and cash equivalents	$24.7	$ 59.1
Accounts receivable (less allowance for doubtful accounts of $26.6 and $27.1, respectively)	659.7	618.6
Inventories	90.4	77.5
Prepaid expenses and other	152.1	111.7
Total current assets	926.9	866.9
Goodwill	4,571.1	4,213.6
Other intangibles, net	1,506.8	1,320.5
Net property, plant and equipment	5,558.2	5,283.5
Deferred income taxes	53.5	—
Other assets	89.7	85.5
Total Assets	$12,706.2	$ 11,770.0
Liabilities and Shareholders' Equity		
Current Liabilities:		
Current maturities of long-term debt	$19.3	$ 14.9
Current portion of long-term lease obligations	177.8	168.7
Accounts payable	340.4	390.2
Advance payments and customer deposits	209.3	178.1
Accrued taxes	85.3	78.0
Accrued interest	59.0	58.1
Other current liabilities	336.7	366.6
Total current liabilities	1,227.8	1,254.6
Long-term debt	5,559.9	4,848.7
Long-term lease obligations	4,740.6	4,831.9
Deferred income taxes	—	151.5
Other liabilities	547.7	513.3
Total liabilities	12,076.0	11,600.0
Commitments and Contingencies (See Note 17)		
Shareholders' Equity:		
Common stock, $.0001 par value, 375.0 shares authorized, 190.8 and 96.3 shares issued and outstanding, respectively	—	—
Additional paid-in capital	1,198.0	559.7
Accumulated other comprehensive income	7.2	5.9
Accumulated deficit	(575.0)	(395.6)
Total shareholders' equity	630.2	170.0
Total Liabilities and Shareholders' Equity	$12,706.2	$ 11,770.0

See the accompanying notes to the unaudited interim consolidated financial statements.

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WINDSTREAM HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Six Months Ended June 30,	
(Millions)	2017	2016
Cash Flows from Operating Activities:		
Net loss	$(179.4)	$(230.4)
Adjustments to reconcile net loss to net cash provided from operations:		
Depreciation and amortization	700.9	613.0
Provision for doubtful accounts	19.7	20.5
Share-based compensation expense	32.4	22.6
Deferred income taxes	(97.3)	(40.3)
Net gain on disposal of investment in Uniti common stock	—	(17.3)
Noncash portion of net (gain) loss on early extinguishment of debt	(15.1)	(45.1)
Other-than-temporary impairment loss on investment in Uniti common stock	—	181.9
Plan curtailment	—	(5.5)
Other, net	7.9	(3.1)
Changes in operating assets and liabilities, net		
Accounts receivable	15.7	(2.2)
Prepaid expenses and other	(19.5)	7.0
Accounts payable	(56.3)	(80.9)
Accrued interest	(6.8)	(12.0)
Accrued taxes	2.0	(7.8)
Other current liabilities	(20.1)	24.1
Other liabilities	1.5	(11.7)
Other, net	(31.9)	11.7
Net cash provided from operating activities	353.7	424.5
Cash Flows from Investing Activities:		
Additions to property, plant and equipment	(507.8)	(510.3)
Proceeds from the sale of property	—	6.2
Cash acquired from EarthLink	5.0	—
Other, net	(11.8)	(4.3)
Net cash used in investing activities	(514.6)	(508.4)
Cash Flows from Financing Activities:		
Dividends paid to shareholders	(35.6)	(29.5)
Proceeds from issuance of stock	9.6	—
Repayments of debt and swaps	(1,261.0)	(1,631.5)
Proceeds of debt issuance	1,535.6	1,925.0
Debt issuance costs	(7.3)	(11.7)
Stock repurchases	—	(28.9)
Payments under long-term lease obligations	(82.2)	(74.5)
Payments under capital lease obligations	(22.0)	(47.2)
Other, net	(10.6)	(7.5)
Net cash provided from financing activities	126.5	94.2
(Decrease) increase in cash and cash equivalents	(34.4)	10.3
Cash and Cash Equivalents:		
Beginning of period	59.1	31.3
End of period	$24.7	$41.6

Supplemental Cash Flow Disclosures:		
Interest paid, net of interest capitalized	$417.7	$446.7
Income taxes paid, net	$1.3	$7.9

See the accompanying notes to the unaudited interim consolidated financial statements.

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WINDSTREAM HOLDINGS, INC.
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY (UNAUDITED)

(Millions, except per share amounts)	Common Stock and Additional Paid-In Capital	Accumulated Other Comprehensive Income	Accumulated Deficit	Total
Balance at December 31, 2016	$ 559.7	$ 5.9	$ (395.6)	$ 170.0
Net loss	—	—	(179.4)	(179.4)
Other comprehensive income (loss), net of tax:				
Change in postretirement and pension plans	—	0.7	—	0.7
Amortization of unrealized losses on de-designated interest rate swaps	—	1.8	—	1.8
Change in designated interest rate swaps	—	(1.2)	—	(1.2)
Comprehensive income (loss)	—	1.3	(179.4)	(178.1)
Share-based compensation	22.3	—	—	22.3
Stock issued for pension contribution (See Note 7)	9.6	—	—	9.6
Stock issued to employee savings plan (See Note 7)	22.7	—	—	22.7
Stock issued in merger with EarthLink (See Note 2)	642.6	—	—	642.6
Taxes withheld on vested restricted stock and other	(9.8)	—	—	(9.8)
Dividends of $.30 per share declared to shareholders	(49.1)	—	—	(49.1)
Balance at June 30, 2017	$ 1,198.0	$ 7.2	$ (575.0)	$ 630.2

See the accompanying notes to the unaudited interim consolidated financial statements.

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WINDSTREAM SERVICES, LLC
CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

(Millions)	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
Revenues and sales:				
Service revenues	$1,465.6	$1,331.3	$2,810.0	$2,671.9
Product sales	26.0	28.3	47.3	61.1
Total revenues and sales	1,491.6	1,359.6	2,857.3	2,733.0
Costs and expenses:				
Cost of services (exclusive of depreciation and amortization included below)	747.5	667.2	1,429.9	1,336.0
Cost of products sold	29.7	24.2	50.5	53.1
Selling, general and administrative	224.5	196.3	437.5	399.6
Depreciation and amortization	362.4	308.2	700.9	613.0
Merger, integration and other costs	16.4	2.6	73.7	7.6
Restructuring charges	3.5	5.9	10.9	10.3
Total costs and expenses	1,384.0	1,204.4	2,703.4	2,419.6
Operating income	107.6	155.2	153.9	313.4
Dividend income on Uniti common stock	—	—	—	17.6
Other (expense) income, net	(0.1)	(1.9)	0.6	(3.1)
Net gain on disposal of investment in Uniti common stock	—	17.3	—	17.3
Net gain (loss) on early extinguishment of debt	—	37.5	(3.2)	2.1
Other-than-temporary impairment loss on investment in Uniti common stock	—	—	—	(181.9)
Interest expense	(214.4)	(217.4)	(426.2)	(437.1)
Loss before income taxes	(106.9)	(9.3)	(274.9)	(271.7)
Income tax benefit	(39.3)	(11.2)	(96.2)	(42.0)
Net (loss) income	$(67.6)	$1.9	$(178.7)	$(229.7)

See the accompanying notes to the unaudited interim consolidated financial statements.

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WINDSTREAM SERVICES, LLC
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions)	2017	2016	2017	2016
Net (loss) income	$(67.6)	$1.9	$(178.7)	$(229.7)
Other comprehensive (loss) income:				
Available-for-sale securities:				
Unrealized holding gain arising during the period	—	51.5	—	156.1
Gain on disposal recognized in the period	—	(51.5)	—	(51.5)
Other-than-temporary impairment loss recognized in the period	—	—	—	181.9
Change in available-for-sale securities	—	—	—	286.5
Interest rate swaps:				
Unrealized loss on designated interest rate swaps	(5.3)	(3.3)	(1.9)	(11.6)
Amortization of net unrealized losses on de-designated interest rate swaps	1.4	1.0	2.9	2.2
Income tax benefit (expense)	1.5	1.0	(0.4)	3.7
Change in interest rate swaps	(2.4)	(1.3)	0.6	(5.7)
Postretirement and pension plans:				
Change in net actuarial gain for employee benefit plans	1.4	0.4	1.4	0.4
Plan curtailment	—	—	—	(5.5)
Amounts included in net periodic benefit cost:				
Amortization of net actuarial loss	0.1	—	0.1	0.1
Amortization of prior service credits	(0.2)	(0.1)	(0.4)	(0.6)
Income tax (expense) benefit	(0.5)	(0.1)	(0.4)	2.2
Change in postretirement and pension plans	0.8	0.2	0.7	(3.4)
Other comprehensive (loss) income	(1.6)	(1.1)	1.3	277.4
Comprehensive (loss) income	$(69.2)	$0.8	$(177.4)	$47.7

See the accompanying notes to the unaudited interim consolidated financial statements.

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WINDSTREAM SERVICES, LLC
CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(Millions)	June 30, 2017	December 31, 2016
Assets		
Current Assets:		
Cash and cash equivalents	$24.7	$ 59.1
Accounts receivable (less allowance for doubtful accounts of $26.6 and $27.1, respectively)	659.7	618.6
Inventories	90.4	77.5
Prepaid expenses and other	152.1	111.7
Total current assets	926.9	866.9
Goodwill	4,571.1	4,213.6
Other intangibles, net	1,506.8	1,320.5
Net property, plant and equipment	5,558.2	5,283.5
Deferred income taxes	53.5	—
Other assets	89.7	85.5
Total Assets	$12,706.2	$ 11,770.0
Liabilities and Member Equity		
Current Liabilities:		
Current maturities of long-term debt	$19.3	$ 14.9
Current portion of long-term lease obligations	177.8	168.7
Accounts payable	340.4	390.2
Advance payments and customer deposits	209.3	178.1
Payable to Windstream Holdings, Inc.	29.8	15.0
Accrued taxes	85.3	78.0
Accrued interest	59.0	58.1
Other current liabilities	306.9	351.6
Total current liabilities	1,227.8	1,254.6
Long-term debt	5,559.9	4,848.7
Long-term lease obligations	4,740.6	4,831.9
Deferred income taxes	—	151.5
Other liabilities	547.7	513.3
Total liabilities	12,076.0	11,600.0
Commitments and Contingencies (See Note 17)		
Member Equity:		
Additional paid-in capital	1,193.7	556.1
Accumulated other comprehensive income	7.2	5.9
Accumulated deficit	(570.7)	(392.0)
Total member equity	630.2	170.0
Total Liabilities and Member Equity	$12,706.2	$ 11,770.0

See the accompanying notes to the unaudited interim consolidated financial statements.

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WINDSTREAM SERVICES, LLC
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(Millions)	Six Months Ended June 30, 2017	2016
Cash Flows from Operating Activities:		
Net loss	$(178.7)	$(229.7)
Adjustments to reconcile net loss to net cash provided from operations:		
Depreciation and amortization	700.9	613.0
Provision for doubtful accounts	19.7	20.5
Share-based compensation expense	32.4	22.6
Deferred income taxes	(97.3)	(40.3)
Net gain on disposal of investment in Uniti common stock	—	(17.3)
Noncash portion of net (gain) loss on early extinguishment of debt	(15.1)	(45.1)
Other-than-temporary impairment loss on investment in Uniti common stock	—	181.9
Plan curtailment	—	(5.5)
Other, net	7.9	(3.1)
Changes in operating assets and liabilities, net		
Accounts receivable	15.7	(2.2)
Prepaid expenses and other	(19.5)	7.0
Accounts payable	(56.3)	(80.9)
Accrued interest	(6.8)	(12.0)
Accrued taxes	2.0	(7.8)
Other current liabilities	(21.1)	24.1
Other liabilities	1.5	(11.7)
Other, net	(31.9)	11.7
Net cash provided from operating activities	353.4	425.2
Cash Flows from Investing Activities:		
Additions to property, plant and equipment	(507.8)	(510.3)
Proceeds from the sale of property	—	6.2
Cash acquired from EarthLink	5.0	—
Other, net	(11.8)	(4.3)
Net cash used in investing activities	(514.6)	(508.4)
Cash Flows from Financing Activities:		
Distributions to Windstream Holdings, Inc.	(35.3)	(59.1)
Contribution from Windstream Holdings, Inc.	9.6	—
Repayments of debt and swaps	(1,261.0)	(1,631.5)
Proceeds of debt issuance	1,535.6	1,925.0
Debt issuance costs	(7.3)	(11.7)
Payments under long-term lease obligations	(82.2)	(74.5)
Payments under capital lease obligations	(22.0)	(47.2)
Other, net	(10.6)	(7.5)
Net cash provided from financing activities	126.8	93.5
(Decrease) increase in cash and cash equivalents	(34.4)	10.3
Cash and Cash Equivalents:		
Beginning of period	59.1	31.3
End of period	$24.7	$41.6
Supplemental Cash Flow Disclosures:		

Interest paid, net of interest capitalized	$417.7	$446.7
Income taxes paid, net	$1.3	$7.9

See the accompanying notes to the unaudited interim consolidated financial statements.

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WINDSTREAM SERVICES, LLC
CONSOLIDATED STATEMENT OF MEMBER EQUITY (UNAUDITED)

(Millions)	Additional Paid-In Capital	Accumulated Other Comprehensive Income	Accumulated Deficit	Total
Balance at December 31, 2016	$ 556.1	$ 5.9	$ (392.0)	$ 170.0
Net loss	—	—	(178.7)	(178.7)
Other comprehensive income (loss), net of tax:				
Change in postretirement and pension plans	—	0.7	—	0.7
Amortization of unrealized losses on de-designated interest rate swaps	—	1.8	—	1.8
Change in designated interest rate swaps	—	(1.2)	—	(1.2)
Comprehensive income (loss)	—	1.3	(178.7)	(177.4)
Share-based compensation	22.3	—	—	22.3
Contributions from Windstream Holdings, Inc.:				
Cash contribution to pension plan (See Note 7)	9.6	—	—	9.6
Stock contribution to employee savings plan (See Note 7)	22.7	—	—	22.7
Stock contribution for merger with EarthLink (See Note 2)	642.6	—	—	642.6
Taxes withheld on vested restricted stock and other	(9.8)	—	—	(9.8)
Distributions payable to Windstream Holdings, Inc.	(49.8)	—	—	(49.8)
Balance at June 30, 2017	$ 1,193.7	$ 7.2	$ (570.7)	$ 630.2

See the accompanying notes to the unaudited interim consolidated financial statements.

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NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

1. Preparation of Interim Financial Statements:

In these consolidated financial statements, unless the context requires otherwise, the use of the terms “Windstream,” “we,” “us” or “our” shall refer to Windstream Holdings, Inc. and its subsidiaries, including Windstream Services, LLC, and the term “Windstream Services” shall refer to Windstream Services, LLC and its subsidiaries.

Organizational Structure – Windstream Holdings, Inc. (“Windstream Holdings”) is a publicly traded holding company incorporated in the state of Delaware on May 23, 2013, and the parent of Windstream Services, LLC (“Windstream Services”), a Delaware limited liability company organized on March 1, 2004. Windstream Holdings common stock trades on the NASDAQ Global Select Market (“NASDAQ”) under the ticker symbol “WIN”. Windstream Holdings owns a 100 percent interest in Windstream Services. Windstream Services and its guarantor subsidiaries are the sole obligors of all outstanding debt obligations and, as a result also file periodic reports with the Securities and Exchange Commission (“SEC”). Windstream Holdings is not a guarantor of nor subject to the restrictive covenants included in any of Windstream Services’ debt agreements. The Windstream Holdings board of directors and officers oversee both companies.

Description of Business – We are a leading provider of advanced network communications and technology solutions for consumers, businesses, enterprise organizations and wholesale customers across the United States. We provide data, cloud solutions, unified communications and managed services to small business and enterprise clients. We also offer bundled services, including broadband, security solutions, voice and digital television to consumers. Including network assets related to our 2017 acquisitions, we supply core transport solutions on a local and long-haul fiber network spanning approximately 150,000 miles.

Consumer service revenues are generated from the provisioning of high-speed Internet, voice and video services to consumers. Business service revenues include revenues from integrated voice and data services, advanced data and traditional voice and long-distance services provided to enterprise and small business customers. Wholesale revenues include revenues from other communications services providers for special access circuits and fiber connections, voice and data transport services, and revenues from the reselling of our services. Regulatory revenues include switched access revenues, federal and state Universal Service Fund (“USF”) revenues and amounts received from Connect America Fund - Phase II. Other service revenues include revenues from USF surcharges and other miscellaneous services.

Basis of Presentation – The accompanying unaudited consolidated financial statements have been prepared based upon SEC rules that permit reduced disclosure for interim periods. Certain information and footnote disclosures have been condensed or omitted in accordance with those rules and regulations. The accompanying consolidated balance sheet as of December 31, 2016, was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States. In our opinion, these financial statements reflect all adjustments that are necessary for a fair statement of results of operations and financial condition for the interim periods presented including normal recurring accruals and other items. The results for the interim periods are not necessarily indicative of results for the full year. For a more complete discussion of significant accounting policies and certain other information, this report should be read in conjunction with the consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2016, which was filed with the SEC on March 1, 2017.

Windstream Holdings and its domestic subsidiaries, including Windstream Services, file a consolidated federal income tax return. As such, Windstream Services and its subsidiaries are not separate taxable entities for federal and

certain state income tax purposes. In instances when Windstream Services does not file a separate return, income taxes as presented within the accompanying consolidated financial statements attribute current and deferred income taxes of Windstream Holdings to Windstream Services and its subsidiaries in a manner that is systematic, rational and consistent with the asset and liability method. Income tax provisions presented for Windstream Services and its subsidiaries are prepared under the "separate return method." The separate return method represents a hypothetical computation assuming that the reported revenue and expenses of Windstream Services and its subsidiaries were incurred by separate taxable entities.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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1. Preparation of Interim Financial Statements, Continued:

The preparation of financial statements, in accordance with accounting principles generally accepted in the United States ("U.S. GAAP"), requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities. The estimates and assumptions used in the accompanying consolidated financial statements are based upon management's evaluation of the relevant facts and circumstances as of the date of the consolidated financial statements. Actual results may differ from the estimates and assumptions used in preparing the accompanying consolidated financial statements, and such differences could be material.

There are no significant differences between the consolidated results of operations, financial condition, and cash flows of Windstream Holdings and those of Windstream Services other than for certain expenses incurred directly by Windstream Holdings principally consisting of audit, legal and board of director fees, NASDAQ listing fees, other shareholder-related costs, income taxes, common stock activity, and payables from Windstream Services to Windstream Holdings. Earnings per share data has not been presented for Windstream Services, because that entity has not issued publicly held common stock as defined in accordance with U.S. GAAP. Unless otherwise indicated, the note disclosures included herein pertain to both Windstream Holdings and Windstream Services.

Certain prior year amounts have been reclassified to confirm to the current year financial statement presentation. These changes and reclassifications did not impact net loss or comprehensive loss.

Change in Accounting Estimate – The calculation of depreciation and amortization expense is based on the estimated economic useful lives of the underlying property, plant and equipment and finite-lived intangible assets. We periodically obtain updated depreciation studies to evaluate whether certain useful lives remain appropriate in accordance with authoritative guidance. With the assistance of a third-party valuation advisor, we completed analyses of the depreciable lives of assets held for use of certain subsidiaries during 2016. Based on the results of the analyses, we implemented new depreciation rates in the fourth quarter of 2016, the effects of which resulted in an increase to depreciation expense. Additionally, in the fourth quarter of 2016, we reassessed the estimated useful lives of certain fiber assets, extending the useful life of such assets from 20 to 25 years. The net impact of these changes resulted in increases to depreciation expense of $8.9 million and $17.7 million for the three and six month periods ended June 30, 2017, respectively, while our reported net loss increased $5.7 million and $11.2 million, or $.04 and $.07 per share, for the three and six month periods ended June 30, 2017, respectively. We anticipate the net impact of these changes to increase depreciation expense by $17.7 million during the remainder of 2017.

Recently Adopted Accounting Standards

Valuation of Inventory – In July 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory ("ASU 2015-11"). The updated guidance requires that an entity should measure inventory valued using a first-in, first-out or average cost method at the lower of cost and net realizable value. Net realizable value is defined as the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. ASU 2015-11 should be applied on a prospective basis and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. As required, we adopted ASU 2015-11 in the first quarter of 2017. The adoption of ASU 2015-11 did not have a material impact to our consolidated results of operations, financial position or cash flows.

Derivatives and Hedging – In March 2016, the FASB issued ASU No. 2016-05, Derivatives and Hedging (Topic 815): Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships (a consensus of the Emerging Issues Task Force) (“ASU 2016-05”). ASU 2016-05 clarifies that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument does not, in and of itself, require de-designation of that hedging relationship provided that all other hedge accounting criteria continue to be met. ASU 2016-05 is effective for fiscal years beginning after December 15, 2016. As required, we adopted ASU 2016-05 in the first quarter of 2017. The adoption of ASU 2016-05 did not have a material impact to our consolidated results of operations, financial position or cash flows.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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1. Preparation of Interim Financial Statements, Continued:

Employee Share-Based Payment Accounting – In March 2016, the FASB issued ASU No. 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting ("ASU 2016-09"), which simplifies several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. Under the new guidance all excess tax benefits and tax deficiencies, including tax benefits of dividends on share-based payment awards, should be recognized as income tax expense or benefit in the income statement, eliminating the notion of the APIC pool. The excess tax benefits will be classified as operating activities along with other income tax cash flows rather than financing activities in the statement of cash flows. The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. ASU 2016-09 also allows entities to elect to either estimate the total number of awards that are expected to vest or account for forfeitures when they occur. Additionally, ASU 2016-09 clarifies that cash payments to tax authorities in connection with shares withheld to meet statutory tax withholding requirements should be presented as a financing activity in the statement of cash flows. ASU 2016-09 is effective for annual reporting periods beginning after December 15, 2016. We adopted this standard effective January 1, 2017 and maintained our past practice of estimating the total number of awards expected to vest. The adoption of ASU 2016-09 did not have a material impact to our consolidated results of operations, financial position or cash flows.

Goodwill Impairment – In January 2017, the FASB issued ASU No. 2017-04, Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment ("ASU 2017-04") simplifying the subsequent measurement of goodwill by eliminating the second step from the goodwill impairment test. The second step requires the measurement of a goodwill impairment by comparing the implied value of a reporting unit's goodwill and the goodwill's carrying amount. Under the amendments, the goodwill impairment will be measured as the excess of the reporting unit's carrying amount over its fair value. An impairment charge should be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. ASU 2017-04 also eliminates the requirement for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform the second step of the goodwill impairment test. Therefore, the same impairment assessment applies to all reporting units. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. As permitted, we early adopted this standard effective January 1, 2017.

Recently Issued Authoritative Guidance

Revenue Recognition – In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09"). The standard outlines a single comprehensive revenue recognition model for entities to follow in accounting for revenue from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that an entity should recognize revenue for the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to receive for those goods or services. ASU 2014-09 also includes new accounting principles related to the deferral and amortization of contract acquisition and fulfillment costs. ASU 2014-09 may be adopted by applying the provisions of the new standard on a retrospective basis to all periods presented in the financial statements or on a modified retrospective basis which would result in the recognition of a cumulative effect adjustment in the year of adoption. When issued, ASU 2014-09 was to be effective for annual periods beginning after December 15, 2016 and interim periods within those annual periods. Early adoption was not permitted.

In July 2015, the FASB deferred the effective date of ASU 2014-09 by one year to December 15, 2017 for annual reporting periods beginning after that date, or January 1, 2018, for calendar companies like Windstream. Entities are permitted to early adopt the standard, but not before the original effective date of December 15, 2016.

In 2016, the FASB issued the following updates to the revenue recognition guidance:

- ASU No. 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net) to improve the operability and understandability of the implementation guidance on principal versus agent considerations.

- ASU No. 2016-10, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing to provide more detailed guidance with respect to identifying performance obligations and accounting for licensing arrangements, including intellectual property licenses, royalties, license restrictions and renewals.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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1. Preparation of Interim Financial Statements, Continued:

- ASU No. 2016-11, Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting to rescind several SEC Staff announcements that are codified in Topic 605: Revenue Recognition, including, among other items, guidance relating to accounting for consideration given by a vendor to a customer, as well as accounting for shipping and handling fees and freight services.

- ASU No. 2016-12, Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients to provide clarification to Topic 606 on how to assess collectability, present sales tax, treat noncash consideration, and account for completed and modified contracts at the time of transition. This guidance also clarifies that an entity retrospectively applying the guidance in Topic 606 is not required to disclose the effect of the accounting change in the period of adoption.

- ASU No. 2016-20, Technical Corrections and Improvements to Topic 606: Revenue from Contracts with Customers to provide additional clarification and guidance with respect to a number of issues including impairment testing for capitalized contract costs, losses on construction and production-type contracts, and disclosures of prior-period and remaining performance obligations.

The effective date and transition requirements for each of these amendments are the same as the effective date and transition requirements of ASU 2014-09.

We will adopt this standard effective January 1, 2018 utilizing the modified retrospective basis. We have established a cross-functional team to implement the standard and have identified and are in the process of implementing changes to our systems, processes and internal controls to meet the standard's reporting and disclosure requirements. While we have not fully quantified the effects of the standard on our consolidated financial statements, we have determined that due to changes in the timing of recognition of certain installation services and discounts, promotional credits and price guarantees given to customers, we will recognize contract assets and liabilities in our consolidated balance sheets. In addition, the requirement to defer incremental contract acquisition costs, including sales commissions, and recognize such costs over the contract period or expected customer life will result in the recognition of a deferred charge within our consolidated balance sheets.

Leases – In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which will require that virtually all lease arrangements that do not meet the criteria of a short-term lease be presented on the lessee's balance sheet by recording a right-of-use asset and a lease liability equal to the present value of the related future lease payments. The income statement impacts of the leases will depend on the nature of the leasing arrangement and will be similar to existing accounting for operating and capital leases. The new standard does not substantially change the accounting for lessors. The new standard will also require additional disclosures regarding an entity's leasing arrangements and will be effective for the first interim reporting period within annual periods beginning after December 15, 2018, although early adoption is permitted. Lessees and lessors will be required to apply the new standard at the beginning of the earliest period presented in the financial statements in which they first apply the new guidance, using a modified retrospective transition method. We will adopt ASU 2016-02 effective January 1, 2019, and we are currently assessing the impact the new standard will have on our consolidated financial statements.

Financial Instruments - Credit Losses – In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments ("ASU 2016-13"). This standard introduces a new forward-looking approach, based on expected losses, to estimate credit losses on certain types of

financial instruments, including trade receivables. The estimate of expected credit losses will require entities to incorporate considerations of historical information, current information and reasonable and supportable forecasts. This new standard also expands the disclosure requirements to enable users of financial statements to understand the entity's assumptions, models and methods for estimating expected credit losses. ASU 2016-13 is effective for annual and interim reporting periods beginning after December 15, 2019, and the guidance is to be applied using a modified retrospective transition approach. Early adoption is permitted for annual and interim reporting periods beginning after December 15, 2018. We are currently assessing the timing of adoption and the impact the new standard will have on our consolidated financial statements.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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1. Preparation of Interim Financial Statements, Continued:

Statement of Cash Flows –In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”). This standard provides guidance on how certain cash receipts and cash payments should be presented and classified in the statement of cash flows, including among others, debt prepayment and extinguishment costs, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims and distributions received from equity method investees. The standard also clarifies that when cash receipts and cash payments have aspects of more than one class of cash flows and cannot be separated, classification will depend on the predominant source or use of the underlying cash flows. ASU 2016-15 is effective for annual and interim reporting periods beginning after December 15, 2017, with early adoption permitted. We will adopt this standard effective January 1, 2018. We are currently assessing the impact the new standard will have on our consolidated statement of cash flows.

Definition of a Business – In January 2017, the FASB issued ASU No. 2017-01, Business Combinations (Topic 805), Clarifying the Definition of a Business (“ASU 2017-01”). Under the new guidance an integrated set of activities must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output to be considered a business. ASU 2017-01 provides a framework to assist entities in evaluating whether both an input and a substantive process are present and removes the evaluation of whether a market participant could replace missing elements. Although outputs are not required for an integrated sets of activities to be a business, outputs generally are a key element of a business; therefore, the new guidance provides more stringent criteria for an integrated sets of activities without outputs. Furthermore, ASU 2017-01 narrows the definition of the term output so that it is consistent with how outputs are described in Topic 606. ASU 2017-01 is effective for annual periods beginning after December 15, 2017, including interim periods within those annual reporting periods. Early adoption is permitted. We are currently assessing the timing of adoption and the impact the new standard will have on our consolidated financial statements.

Presentation of Defined Benefit Retirement Costs – In March 2017, the FASB issued ASU 2017-07, Compensation-Retirement Benefits (Topic 715) Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost (“ASU 2017-07”). This standard changes the income statement presentation of defined benefit plan expense by requiring separation between operating expense (service cost component) and non-operating expense (all other components, including interest cost, amortization of prior service cost, actuarial gains and losses, curtailments and settlements). The operating expense component will be reported in the same income statement line item(s) as other employee compensation costs arising from services rendered during the period while the non-operating components will be reported in other income and expense. In addition, only the service cost component will be eligible for capitalization as part of an asset such as inventory or property, plant and equipment. Retrospective application of the change in income statement presentation is required, while the change in capitalized benefit cost is to be applied prospectively. The ASU is effective for fiscal years beginning after December 15, 2017. We are currently assessing the impact that adopting this new accounting standard will have on our consolidated financial statements.

2. Completion of Merger:

On February 27, 2017, Windstream Holdings completed its merger with EarthLink Holdings Corp. (“EarthLink”), pursuant to the terms of the Agreement and Plan of Merger (the “Merger Agreement”) dated November 5, 2016, whereby EarthLink merged into Europa Merger Sub, Inc., an wholly-owned subsidiary of Windstream Services, LLC, and survived, and immediately following, merged with Europa Merger Sub, LLC, a wholly-owned subsidiary of Windstream Services, LLC, with Merger Sub surviving and changing its name to EarthLink Holdings, LLC (the

"Merger"). EarthLink Holdings, LLC is a direct, wholly-owned subsidiary of Windstream Services and provides data, voice and managed network services to retail and wholesale business customers and nationwide Internet access and related value-added services to residential customers. In the Merger, we added approximately 700,000 customers and approximately 16,000 incremental route fiber miles, which expanded our national footprint to approximately 150,000 fiber route miles and enhanced our ability to offer customers expanded products, services and enhanced enterprise solutions. We also expect to achieve operating expense and capital expenditure synergies in integrating the acquired operations. Pursuant to the terms of the Merger Agreement, each share of EarthLink common stock was exchanged for .818 of Windstream Holdings common stock. No fractional shares were issued in the Merger, with a cash payment being made in lieu of fractional shares. Employee restricted stock units issued by EarthLink that were outstanding as of the merger date were exchanged for an equivalent number of Windstream Holdings restricted stock units based on the same exchange ratio of EarthLink common stock to Windstream Holdings common stock of .818 per share. The replacement restricted stock units remain subject to the vesting and other terms and conditions prescribed by the EarthLink equity plans that were assumed by us in the Merger. In the aggregate, Windstream Holdings issued 87.8 million shares of its common stock and 5.2 million of replacement equity awards. Windstream also assumed $435.3 million aggregate principal amount of EarthLink's long-term debt, which we refinanced, as further discussed in Note 4. The Merger qualifies as a tax-free reorganization for U.S. federal income tax purposes and is valued at approximately $1.1 billion.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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2. Completion of Merger, Continued:

We accounted for the Merger using the acquisition method of accounting and accordingly, the cost of the acquisition was allocated to the assets acquired and liabilities assumed based on their estimated fair values as of the merger date. During the second quarter of 2017, we revised our preliminary purchase price allocation to reduce total merger consideration by $4.3 million to update the portion of the fair value of replacement equity awards attributable to future vesting requirements. We also revised the estimated fair value of certain acquired tangible and intangible assets, primarily consisting of an increase of $11.6 million in property, plant and equipment and a decrease of $7.0 million to customer lists, based on updates to the information applicable to the third-party valuations of these assets. The impact of these changes on depreciation and amortization was not material to our consolidated results of operations. Based on additional information received and further analysis, we adjusted the purchase price allocation applicable to acquired net operating losses, resulting in a $108.5 million reduction in the valuation allowance associated with the net deferred tax assets acquired in the Merger. Our initial purchase price allocation had yielded a net deferred tax asset which had been fully offset by a valuation allowance. In addition, we adjusted certain contingent liabilities and other reserves based on additional information received subsequent to the Merger date. The revisions to the merger consideration and estimated fair values of assets acquired and liabilities assumed resulted in an offsetting change to the amount of goodwill recorded from the transaction and also impacted the amount of goodwill allocated to our business segments.

The allocation of the purchase price is preliminary and subject to change based on obtaining information currently not available to us, primarily related to the tax basis of assets acquired. Any changes to the initial estimates of the fair value of the acquired assets and liabilities assumed will be recorded as adjustments to those asset and liabilities with the offset charged to goodwill. Goodwill associated with the Merger was primarily attributable to the EarthLink workforce and expected synergies. As a result of past acquisitions completed by EarthLink, approximately $54.8 million of goodwill recorded in the Merger is expected to be deductible for income tax purposes.

The following table summarizes the preliminary fair values of the assets acquired and liabilities assumed for EarthLink.

(Millions)	Preliminary Allocation
Fair value of assets acquired:	
Cash and other current assets	$ 36.1
Accounts receivable	74.7
Property, plant and equipment	355.6
Goodwill	357.5
Customer lists (a)	268.0
Trade name, developed technology and software (b)	31.0
Deferred income taxes	108.5
Other assets	0.8
Total assets acquired	1,232.2
Fair value of liabilities assumed:	
Current liabilities	116.9
Long-term debt	449.1
Other liabilities	23.6
Total liabilities assumed	589.6
Common stock and replacement equity awards issued to EarthLink shareholders (c)	$ 642.6

(a) Customer lists are amortized using the sum-of-years digit methodology over a weighted average life of 5.5 years.

(b) Trade name of $8.0 million is amortized on a straight-line basis over an estimated useful life of 7 years. Internally developed technology and software of $23.0 million are amortized on a straight-line basis over an estimated useful life of 3 years.

(c) Total merger consideration of $642.6 million consisted of $631.4 million related to shares issued to EarthLink shareholders and $11.2 million related to replacement equity awards.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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2. Completion of Merger, Continued:

The preliminary fair values of the assets acquired and liabilities assumed were determined with the assistance of a third-party valuation firm using income, cost, and market approaches. The customer lists were valued based on the present value of future cash flows and the trade name was valued using the relief-from-royalty method, both of which are income approaches. Significant assumptions utilized in the income approach were based on our specific information and projections, which are not observable in the market and are thus considered Level 3 measurements as defined by authoritative guidance. The cost approach, which estimates value by determining the current cost of replacing an asset with another of equivalent economic utility, was used as appropriate for valuing internally developed technology and software and property, plant and equipment. The cost to replace a given asset reflects the estimated reproduction or replacement cost for the asset, less an allowance for loss in value due to depreciation. The fair value of the EarthLink credit facility was based on its redemption cost, while the remaining bonds were valued based on quoted market prices. Equity consideration was based on the opening price of our common stock on February 27, 2017. Consideration related to replacement restricted stock units was calculated based on the opening price of our common stock on February 27, 2017, net of the portion of the fair value attributable to future vesting requirements. The amount allocated to unearned compensation cost for awards subject to future service requirements was calculated based on the fair value of such awards at the acquisition date and will be recognized as compensation cost over the remaining future service period.

The results of EarthLink's operations are included in our consolidated results of operations beginning on February 27, 2017. For the three and six month periods ended June 30, 2017, our consolidated results of operations include revenues and sales of $225.0 million and $307.1 million and operating income of $6.8 million and $4.0 million attributable to EarthLink. We incurred $13.4 million and $66.5 million of merger and integration expenses during the three and six month periods ended June 30, 2017, respectively, related to the completion of the Merger (see Note 9).

The following unaudited pro forma consolidated results of operations of Windstream for the three and six month periods ended June 30, 2017 and 2016 assume that the Merger occurred as of January 1, 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions)	2017	2016	2017	2016
Revenues and sales	$1,491.6	$1,606.5	$3,006.8	$3,238.0
Operating income	$108.6	$153.4	$174.7	$279.4
Net loss	$(70.4)	$(1.7)	$(168.1)	$(251.7)
Loss per share	($.38)	($.01)	($.91)	($1.41)

The pro forma information presents our historical results of operations adjusted to include EarthLink, with the results prior to the merger closing date adjusted to include the pro forma effect of the elimination of transactions between Windstream and EarthLink, the adjustment to revenues and sales to change EarthLink's reporting of USF fees billed to customers and the related payments from a net basis to a gross basis to conform to Windstream's reporting of such customer billings, the adjustment to depreciation and amortization expense associated with the estimated acquired fair value of property, plant and equipment and intangible assets, the adjustment to interest expense to reflect the refinancing of EarthLink's long-term debt obligations, the impact of merger expenses related to the acquisition and the related income tax effects of the pro forma adjustments.

The pro forma results are presented for illustrative purposes only and do not reflect either the realization of potential cost savings or any additional integration costs. These pro forma results do not purport to be indicative of the results that would have been obtained if the Merger had occurred as of the date indicated, nor do the pro forma results intend

to be a projection of results that may be obtained in the future.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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3. Goodwill and Other Intangible Assets:

Goodwill represents the excess of cost over the fair value of net identifiable tangible and intangible assets acquired through various business combinations. The cost of acquired entities at the date of the acquisition is allocated to identifiable assets and liabilities, and the excess of the total purchase price over the amounts assigned to net identifiable assets has been recorded as goodwill.

Changes in the carrying amount of goodwill were as follows:

(Millions)	
Balance at December 31, 2016	$4,213.6
Acquisition completed during the period - merger with EarthLink	357.5
Balance at June 30, 2017	$4,571.1

Goodwill assigned to our four operating segments was as follows:

(Millions)	ILEC Consumer and Small Business	Wholesale	Enterprise	CLEC Consumer and Small Business	Total
Balance at December 31, 2016	$ 2,321.2	$ 1,176.4	$ 598.0	$ 118.0	$4,213.6
Acquisition completed during the period - merger with EarthLink	—	121.5	123.7	112.3	357.5
Balance at June 30, 2017	$ 2,321.2	$ 1,297.9	$ 721.7	$ 230.3	$4,571.1

Intangible assets were as follows at:

	June 30, 2017			December 31, 2016		
(Millions)	Gross Cost	Accumulated Amortization	Net Carrying Value	Gross Cost	Accumulated Amortization	Net Carrying Value
Franchise rights	$1,285.1	$ (350.4)	$ 934.7	$1,285.1	$ (328.9)	$ 956.2
Customer lists	2,059.7	(1,528.7)	531.0	1,791.7	(1,442.4)	349.3
Cable franchise rights	17.3	(8.6)	8.7	17.3	(8.0)	9.3
Trade name	8.0	(0.4)	7.6	—	—	—
Developed technology and software	23.0	(2.3)	20.7	—	—	—
Patents	10.6	(6.5)	4.1	10.6	(4.9)	5.7
Balance	$3,403.7	$ (1,896.9)	$ 1,506.8	$3,104.7	$ (1,784.2)	$ 1,320.5

Intangible asset amortization methodology and useful lives were as follows as of June 30, 2017:

Intangible Assets	Amortization Methodology	Estimated Useful Life
Franchise rights	straight-line	30 years
Customer lists	sum of years digits	5.5 - 15 years
Cable franchise rights	straight-line	15 years
Trade name	straight-line	7 years
Developed technology and software	straight-line	3 years
Patents	straight-line	3 years

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

3. Goodwill and Other Intangible Assets, Continued:

Amortization expense for intangible assets subject to amortization was $63.9 million and $112.7 million for the three and six month periods ended June 30, 2017, respectively, as compared to $46.7 million and $94.2 million for the same periods in 2016. Amortization expense for intangible assets subject to amortization was estimated to be as follows for each of the years ended June 30:

Year	(Millions)
2018	$ 227.9
2019	189.4
2020	148.3
2021	111.3
2022	79.3
Thereafter	750.6
Total	$ 1,506.8

4. Long-term Debt:

Windstream Holdings has no debt obligations. All debt, including the senior secured credit facility described below, have been incurred by Windstream Services and its subsidiaries. Windstream Holdings is neither a guarantor of nor subject to the restrictive covenants imposed by such debt.

Long-term debt was as follows at:

(Millions)	June 30, 2017	December 31, 2016
Issued by Windstream Services:		
Senior secured credit facility, Tranche B5 – variable rates, due August 8, 2019	$—	$ 572.3
Senior secured credit facility, Tranche B6 – variable rates, due March 29, 2021 (a)	1,338.0	894.8
Senior secured credit facility, Tranche B7 – variable rates, due February 17, 2024	577.1	—
Senior secured credit facility, Revolving line of credit – variable rates, due April 24, 2020	750.0	475.0
Debentures and notes, without collateral:		
2020 Notes – 7.750%, due October 15, 2020	700.0	700.0
2021 Notes – 7.750%, due October 1, 2021	809.3	809.3
2022 Notes – 7.500%, due June 1, 2022	441.2	441.2
2023 Notes – 7.500%, due April 1, 2023	343.5	343.5
2023 Notes – 6.375%, due August 1, 2023	585.7	585.7
Issued by subsidiaries of Windstream Services:		
Windstream Holdings of the Midwest, Inc. – 6.75%, due April 1, 2028 (b)	100.0	100.0
Net discount on long-term debt (c)	(13.4)	(7.2)
Unamortized debt issuance costs (c)	(52.2)	(51.0)
	5,579.2	4,863.6
Less current maturities	(19.3)	(14.9)
Total long-term debt	$5,559.9	$ 4,848.7

(a) If the maturity of the revolving line of credit is not extended prior to April 24, 2020, the maturity date of the Tranche B6 term loan will be April 24, 2020; provided further, if the 2020 Notes have not been repaid or refinanced prior to July 15, 2020 with indebtedness having a maturity date no earlier than March 29, 2021, the

maturity date of the Tranche B6 term loan will be July 15, 2020.

(b) These bonds are secured equally with the senior secured credit facility with respect to the assets of Windstream Holdings of the Midwest, Inc.

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4. Long-term Debt, Continued:

(c) The net discount balance and unamortized debt issuance costs are amortized using the interest method over the life of the related debt instrument.

Senior Secured Credit Facility - The amended credit facility provides that Windstream Services may seek to obtain incremental revolving or term loans in an unlimited amount subject to maintaining a maximum secured leverage ratio and other customary conditions, including obtaining commitments and pro forma compliance with financial maintenance covenants consisting of a maximum debt to consolidated earnings before interest, taxes, depreciation and amortization (“EBITDA”) ratio and a minimum interest coverage ratio. In addition, Windstream Services may request extensions of the maturity date under any of its existing revolving or term loan facilities.

On February 17, 2017, Windstream Services issued an aggregate principal amount of $580.0 million in borrowings under Tranche B7 of its senior secured credit facility, the proceeds of which were used to pay down amounts outstanding under Tranche B5, including accrued interest, and to pay related fees and expenses. The incremental Tranche B7 term loan matures on February 17, 2024 and was issued at a price of 99.5 percent of the principal amount of the loan.

Interest rates applicable to the Tranche B7 term loan are, at Windstream Services’ option, equal to either a base rate plus a margin of 2.25 percent per annum or LIBOR plus a margin of 3.25 percent per annum. LIBOR for the Tranche B7 term loan shall at no time be less than 0.75 percent. The Tranche B7 term loan is subject to quarterly amortization payments in an aggregate amount equal to 0.25 percent of the initial principal amount of such term loans, with the remaining balance payable at maturity. At the time of repayment, unamortized debt issuance and discount related to Tranche B5 totaled $6.3 million, of which $1.2 million were included in the loss on debt extinguishment, while the remaining $5.1 million continue to be deferred and amortized to interest expense over the remaining life of Tranche B7 in accordance with debt modification accounting.

On the date of closing of the merger with EarthLink, Windstream Services amended its existing senior secured credit agreement to provide for the issuance of an aggregate principal amount of $450.0 million in incremental borrowings under Tranche B6, the proceeds of which were used to repay amounts outstanding under EarthLink’s credit facility and to redeem EarthLink’s outstanding 8.875 percent Senior Notes due 2019 and 7.375 percent Senior Secured Notes due 2020. The incremental loans were issued at a price of 99.0 percent of the principal amount of the loan. The incremental loans will be repayable at any time, subject to soft call protection for the first six months following incurrence.

During 2016, Windstream Services had executed incremental amendments to its existing senior secured credit facility to provide for the issuance of an aggregate principal amount $900.0 million term loan under Tranche B6 due March 29, 2021, the proceeds of which were used to repurchase $441.1 million of outstanding 7.875 percent notes due November 1, 2017 (the “2017 Notes”) pursuant to a tender offer and to repay other debt obligations of Windstream Services along with related fees and expenses. Interest on all incremental loans under Tranche B6 accrue at LIBOR plus a margin of 4.00 percent per annum, with LIBOR subject to a 0.75 percent floor. The incremental loans are subject to quarterly amortization in an aggregate amount of approximately 0.25 percent of the initial principal amount of the loans, with the remaining balance payable on March 29, 2021.

Revolving line of credit - Under the amended senior secured credit facility, Windstream Services may obtain revolving loans and may issue up to $30.0 million of letters of credit, which upon issuance reduce the amount available for other extensions of credit. Accordingly, the total amount outstanding under the letters of credit and the

indebtedness incurred under the revolving line of credit may not exceed $1,250.0 million. Borrowings under the revolving line of credit may be used for permitted acquisitions, working capital and other general corporate purposes of Windstream Services and its subsidiaries. Windstream Services will pay a commitment fee on the unused portion of the commitments under the revolving credit facility that will range from 0.40 percent to 0.50 percent per annum, depending on the debt to consolidated EBITDA ratio of Windstream Services and its subsidiaries. Revolving loans made under the credit facility are not subject to interim amortization and such loans are not required to be repaid prior to April 24, 2020, other than to the extent the outstanding borrowings exceed the aggregate commitments under the revolving credit facility. Interest rates applicable to loans under the revolving line of credit are, at Windstream Services' option, equal to either a base rate plus a margin ranging from 0.25 percent to 1.00 percent per annum or LIBOR plus a margin ranging from 1.25 percent to 2.00 percent per annum, based on the debt to consolidated EBITDA ratio of Windstream Services and its subsidiaries. The maturity date of the revolving line of credit is April 24, 2020.

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4. Long-term Debt, Continued:

During the first six months of 2017, Windstream Services borrowed $513.0 million under the revolving line of credit in its senior secured credit facility and retired $238.0 million of these borrowings through June 30, 2017. Considering letters of credit of $25.4 million, the amount available for borrowing under the revolving line of credit was $474.6 million at June 30, 2017.

During the first six months of 2017, the variable interest rate on the revolving line of credit ranged from 2.65 percent to 5.25 percent, and the weighted average rate on amounts outstanding was 2.95 percent during the period. Comparatively, the variable interest rate ranged from 2.44 percent to 4.50 percent during the first six months of 2016, with a weighted average rate on amounts outstanding during the period of 2.50 percent.

Debentures and Notes Repaid in 2016
Tender Offer for 2017 Notes - On March 29, 2016, Windstream Services repurchased $441.1 million aggregate principal amount of the 2017 Notes for total consideration of $477.5 million, plus accrued interest, pursuant to a cash tender offer. Under the tender offer, Windstream Services paid total consideration of $1,082.50 per $1,000 principal amount of the 2017 Notes, which included a $30 early tender payment, plus accrued and unpaid interest. At the time of the repurchases, there was $4.6 million in unamortized net discount and debt issuance costs related to the repurchased notes. Proceeds from the issuance of the Tranche B6 term loan were used to fund the repurchase of the 2017 Notes under the tender offer.

Partial Repurchase of Senior Notes - Pursuant to the debt repurchase program authorized by Windstream Services' board of directors, during the first six months of 2016, Windstream Services repurchased in the open market $394.6 million aggregate principal amount of its senior unsecured notes consisting of the following:

- $93.5 million aggregate principal amount of 2017 Notes, at a repurchase price of $97.8 million, including accrued and unpaid interest;

- $97.9 million aggregate principal amount of 7.750 percent senior unsecured notes due October 1, 2021, (the "2021 Notes"), at a repurchase price of $81.3 million, including accrued and unpaid interest;

- $38.8 million aggregate principal amount of 7.500 percent senior unsecured notes due June 1, 2022, (the "2022 Notes"), at a repurchase price of $30.5 million, including accrued and unpaid interest; and

- $119.9 million aggregate principal amount of 7.500 percent senior unsecured notes due April 1, 2023 and $44.5 million aggregate principal amount of 6.375 percent senior unsecured notes due August 1, 2023 (collectively the "2023 Notes"), at a repurchase price of $98.5 million and $36.9 million, including accrued and unpaid interest, respectively.

At the time of repurchase, there was $8.8 million in unamortized net discount and debt issuance costs related to the repurchased notes. The repurchases were funded utilizing available borrowings under the amended revolving line of credit.

The repurchases under the tender offer and the debt repurchase program were accounted for under the extinguishment method of accounting. Windstream Services recognized a net gain on the early extinguishment of these debt obligations, as presented in the table below.

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4. Long-term Debt, Continued:

Net Gain (Loss) on Early Extinguishment of Debt

The net gain (loss) on early extinguishment of debt was as follows:

(Millions)	Three Months Ended June 30, 2017	2016	Six Months Ended June 30, 2017	2016
EarthLink 2019 and 2020 Notes:				
Premium on early redemption	$—	$—	$(18.3)	$—
Unamortized premium recorded in the Merger	—	—	16.3	—
Loss on early extinguishment of EarthLink 2019 and 2020 Notes	—	—	(2.0)	—
Senior secured credit facility:				
Unamortized discount on original issuance	—	—	(0.3)	—
Unamortized debt issuance costs on original issuance	—	—	(0.9)	—
Loss on early extinguishment of senior secured credit facility	—	—	(1.2)	—
2017 Notes:				
Premium on repurchases	—	—	—	(40.6)
Third-party fees for repurchases	—	(0.2)	—	(2.4)
Unamortized discount on original issuance	—	—	—	(2.0)
Unamortized debt issuance costs on original issuance	—	—	—	(3.7)
Loss on early extinguishment of 2017 Notes	—	(0.2)	—	(48.7)
Partial repurchases of 2021, 2022 and 2023 Notes:				
Discount on repurchases	—	40.3	—	53.9
Unamortized premium on original issuance	—	0.5	—	0.8
Unamortized debt issuance costs on original issuance	—	(3.1)	—	(3.9)
Gain on early extinguishment from partial repurchases of 2021, 2022 and 2023 Notes	—	37.7	—	50.8
Net gain (loss) on early extinguishment of debt	$—	$37.5	$(3.2)	$2.1

Maturities for long-term debt outstanding as of June 30, 2017, excluding $13.4 million of unamortized net discount and $52.2 million of unamortized debt issuance costs, were as follows:

Twelve month period ended:	(Millions)
June 30, 2018	$ 19.3
June 30, 2019	19.3
June 30, 2020	769.3
June 30, 2021	2,003.4
June 30, 2022	1,256.3
Thereafter	1,577.2
Total	$ 5,644.8

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

4. Long-term Debt, Continued:

Interest Expense

Interest expense was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions)	2017	2016	2017	2016
Interest expense - long-term debt	$88.4	$89.6	$174.3	$181.1
Interest expense - long-term lease obligations:				
Telecommunications network assets	121.7	125.4	244.5	252.3
Real estate contributed to pension plan	1.6	1.6	3.1	3.1
Impact of interest rate swaps	3.2	2.9	6.0	5.7
Interest on capital leases and other	1.3	1.0	2.4	1.6
Less capitalized interest expense	(1.8)	(3.1)	(4.1)	(6.7)
Total interest expense	$214.4	$217.4	$426.2	$437.1

Debt Compliance

The terms of Windstream Services' credit facility and indentures include customary covenants that, among other things, require maintenance of certain financial ratios and restrict Windstream Services' ability to incur additional indebtedness. These financial ratios include a maximum leverage ratio of 4.5 to 1.0 and a minimum interest coverage ratio of 2.75 to 1.0. In addition, the covenants include restrictions on dividend and certain other types of payments. As of June 30, 2017, Windstream Services was in compliance with all of these covenants.

In addition, certain of Windstream Services' debt agreements contain various covenants and restrictions specific to the subsidiary that is the legal counterparty to the agreement. Under Windstream Services' long-term debt agreements, acceleration of principal payments would occur upon payment default, violation of debt covenants not cured within 30 days, a change in control including a person or group obtaining 50 percent or more ownership interest in Windstream Services, or breach of certain other conditions set forth in the borrowing agreements. Windstream Services and its subsidiaries were in compliance with these covenants as of June 30, 2017.

5. Derivatives:

Windstream Services enters into interest rate swap agreements to mitigate the interest rate risk inherent in its variable rate senior secured credit facility. Derivative instruments are accounted for in accordance with authoritative guidance for recognition, measurement and disclosures about derivative instruments and hedging activities, including when a derivative or other financial instrument can be designated as a hedge. This guidance requires recognition of all derivative instruments at fair value, and accounting for the changes in fair value depends on whether the derivative has been designated as, qualifies as and is effective as a hedge. Changes in fair value of the effective portions of cash flow hedges are recorded as a component of other comprehensive (loss) income in the current period. Any ineffective portion of the hedges is recognized in earnings in the current period.

As of December 31, 2016, Windstream Services was party to three pay fixed, receive variable interest rate swap agreements to serve as cash flow hedges of the interest rate risk inherent in its senior secured credit facility. The swaps have a notional value of $675.0 million and mature on October 17, 2021. The average fixed interest rate paid is 2.984

percent and includes a component which serves to settle the liability existing on Windstream Services swaps at the time of the transaction. Windstream Services also was a party to an additional pay fixed, receive variable interest rate swap agreement with a bank counterparty with a notional value of $200.0 million, fixed interest rate paid of 1.1275 percent and a maturity date of October 17, 2021. The variable rate received on these four swaps is based on one-month LIBOR and resets on the seventeenth day of each month. On February 27, 2017, Windstream Services entered into two new pay fixed, receive variable interest rate swap agreements with bank counterparties with a total notional value of $500.0 million and maturing on October 17, 2021. The fixed rate paid on the new swaps is 1.8812 percent. Similar to Windstream Services' other four swaps, the variable rate received on the new swaps is the one-month LIBOR and resets on the seventeenth day of each month. Windstream Services has designated each of its six swaps as cash flow hedges of the interest rate risk inherent in borrowings outstanding under its senior secured credit facility due to changes in the LIBOR benchmark interest rate.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

5. Derivatives, Continued:

All of the swaps are hedging probable variable cash flows which extend up to one year beyond the maturity of certain components of Windstream Services' variable rate debt. Consistent with past practice, Windstream Services expects to extend or otherwise replace these components of its debt with variable rate debt. The three renegotiated swaps are off-market swaps, meaning they contain an embedded financing element, which the swap counterparties recover through an incremental charge in the fixed rate over what would be charged for an at-market swap. As such, a portion of the cash payment on the swaps represents the rate that Windstream Services would pay on a hypothetical at-market interest rate swap and is recognized in interest expense. The remaining portion represents the repayment of the embedded financing element and reduces the initial swap liability.

As a result of refinancing transactions completed in 2013, 2015 and 2016, Windstream Services de-designated certain interest rate swaps and froze the accumulated net gains and losses in accumulated other comprehensive income related to those swaps. The frozen balance is amortized from accumulated other comprehensive income to interest expense over the remaining life of the original swaps.

All derivative instruments are recognized at fair value in the accompanying consolidated balance sheets as either assets or liabilities, depending on the rights or obligations under the related contracts.

Set forth below is information related to interest rate swap agreements:

(Millions, except for percentages)	June 30, 2017	December 31, 2016
Designated portion, measured at fair value:		
Other assets	$7.5	$ 6.3
Other current liabilities	$13.1	$ 13.4
Other non-current liabilities	$19.9	$ 21.9
Accumulated other comprehensive income	$20.4	$ 22.3
De-designated portion, unamortized value:		
Accumulated other comprehensive income	$(7.8)	$ (10.7)
Weighted average fixed rate paid	1.10 %	1.82 %
Variable rate received	1.21 %	0.74 %

Derivatives are assessed for effectiveness each quarter and any ineffectiveness is recognized in other income (expense), net in our consolidated statements of operations. There was $(0.1) million of ineffectiveness recognized on the cash flow hedges for both the three and six month periods ended June 30, 2017. Comparatively, ineffectiveness recognized on the cash flow hedges was $(0.6) million and $(1.1) million for the three and six month periods ended June 30 2016, respectively.

All or a portion of the change in fair value of Windstream Services' interest rate swap agreements recorded in accumulated other comprehensive income may be recognized in earnings in certain situations. If Windstream Services extinguishes all of its variable rate debt, or a portion of its variable rate debt such that the variable rate interest received on the swaps exceeds the variable rate interest paid on its debt, all or a portion of the change in fair value of the swaps may be recognized in earnings. In addition, the change in fair value of the swaps may be recognized in earnings if Windstream Services determines it is no longer probable that it will have future variable rate cash flows to hedge against or if a swap agreement is terminated prior to maturity. Windstream Services has assessed the counterparty risk and determined that no substantial risk of default exists as of June 30, 2017. Each counterparty is a bank with a current credit rating at or above A, as determined by Moody's Investors Service, Standard & Poor's

Corporation and Fitch Ratings.

Windstream Services expects to recognize net losses of $3.7 million, net of taxes, in interest expense in the next twelve months related to the unamortized value of the de-designated portion of interest rate swap agreements and the interest settlements for those interest swap agreements at June 30, 2017. Payments on the swaps are presented in the financing activities section of the accompanying consolidated statements of cash flows due to the embedded financing element discussed above.

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5. Derivatives, Continued:

Changes in derivative instruments were as follows for the six month periods ended June 30:

(Millions)	2017			2016		
Changes in fair value of effective portion, net of tax (a)	$	(1.2	)	$	(7.1	)
Amortization of net unrealized losses on de-designated interest rate swaps, net of tax (a)	$	1.8		$	1.4	

(a) Included as a component of other comprehensive (loss) income and will be reclassified into earnings as the hedged transaction affects earnings.

The agreements with each of the derivative counterparties contain cross-default provisions, whereby if Windstream Services were to default on certain indebtedness, it could also be declared in default on its derivative obligations and may be required to net settle any outstanding derivative liability positions with its counterparties at the swap termination value of $33.5 million including accrued interest and excluding the credit valuation adjustment to measure non-performance risk. In addition, certain of the agreements with the counterparties contain provisions where if a specified event or condition, such as a merger, occurs that materially changes Windstream Services' creditworthiness in an adverse manner, Windstream Services may be required to fully collateralize its derivative obligations. At June 30, 2017, Windstream Services had not posted any collateral related to its interest rate swap agreements.

Balance Sheet Offsetting

Windstream Services is party to master netting arrangements, which are designed to reduce credit risk by permitting net settlement of transactions with counterparties. For financial statement presentation purposes, Windstream Services does not offset assets and liabilities under these arrangements.

The following tables presents the assets and liabilities subject to an enforceable master netting arrangement as of June 30, 2017 and December 31, 2016. Information pertaining to derivative assets was as follows:

			Gross Amounts Not Offset in the Consolidated Balance Sheets		
(Millions)	Gross Amount of Recognized Assets	Net Amount of Assets presented in the Consolidated Balance Sheets	Financial Instruments	Cash Collateral Received	Net Amount
June 30, 2017:					
Interest rate swaps	$ 7.5	$ 7.5	$ (1.2)	$ —	$ 6.3

December 31, 2016:					
Interest rate swaps	$ 6.3	$ 6.3	$ —	$ —	$ 6.3

Information pertaining to derivative liabilities was as follows:

(Millions)	Gross Amount of Recognized Liabilities	Net Amount of Liabilities Presented in the Consolidated Balance Sheets	Gross Amounts Not Offset in the Consolidated Balance Sheets		Net Amount
			Financial Instruments	Cash Collateral Received	
June 30, 2017:					
Interest rate swaps	$ 33.0	$ 33.0	$ (1.2)	$ —	$ 31.8
December 31, 2016:					
Interest rate swaps	$ 35.3	$ 35.3	$ —	$ —	$ 35.3

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

6. Fair Value Measurements:

Fair value of financial and non-financial assets and liabilities is defined as an exit price, representing the amount that would be received to sell an asset or transfer a liability in an orderly transaction between market participants. Authoritative guidance defines the following three tier hierarchy for assessing the inputs used in fair value measurements:

Level 1 – Quoted prices in active markets for identical assets or liabilities
Level 2 – Observable inputs other than quoted prices in active markets for identical assets or liabilities
Level 3 – Unobservable inputs

The highest priority is given to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurement) and the lowest priority is given to unobservable inputs (level 3 measurement). Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the determination of fair value of assets and liabilities and their placement within the fair value hierarchy levels.

Our non-financial assets and liabilities, including property, plant and equipment, goodwill, intangible assets and asset retirement obligations, are measured at fair value on a non-recurring basis. No event occurred during the six-month period ended June 30, 2017 requiring our non-financial assets and liabilities to be subsequently recognized at fair value. Our financial instruments consist primarily of cash and cash equivalents, accounts receivable, accounts payable, long-term debt and interest rate swaps. The carrying amount of cash, accounts receivable and accounts payable was estimated by management to approximate fair value due to the relatively short period of time to maturity for those instruments. Cash equivalents, long-term debt and interest rate swaps are measured at fair value on a recurring basis. Cash equivalents were not significant as of June 30, 2017 or December 31, 2016.

The fair values of interest rate swaps and long-term debt were determined using the following inputs at:

(Millions)	June 30, 2017	December 31, 2016
Recorded at Fair Value in the Financial Statements:		
Derivatives - Interest rate swap assets - Level 2	$7.5	$ 6.3
Derivatives - Interest rate swap liabilities - Level 2	$33.0	$ 35.3
Not Recorded at Fair Value in the Financial Statements: (a)		
Long-term debt, including current maturities - Level 2	$5,414.8	$ 4,884.4

(a) Recognized at carrying value of $5,631.4 million and $4,914.6 million in long-term debt, including current maturities, and excluding unamortized debt issuance costs, in the accompanying consolidated balance sheets as of June 30, 2017 and December 31, 2016, respectively.

The fair values of interest rate swaps are determined based on the present value of expected future cash flows using observable, quoted LIBOR swap rates for the full term of the swaps and also incorporate credit valuation adjustments to appropriately reflect both Windstream Services' own non-performance risk and non-performance risk of the respective counterparties. As of June 30, 2017 and December 31, 2016, the fair values of the interest rate swaps were reduced by $2.8 million and $1.7 million, respectively, to reflect non-performance risk.

In calculating the fair value of Windstream Services' long-term debt, the fair value of the debentures and notes was calculated based on quoted market prices of the specific issuances in an active market when available. The fair value

of the other debt obligations was estimated based on appropriate market interest rates applied to the debt instruments. In calculating the fair value of the Windstream Holdings of the Midwest, Inc. notes, an appropriate market price of similar instruments in an active market considering credit quality, nonperformance risk and maturity of the instrument was used.

We do not have any assets or liabilities measured for purposes of the fair value hierarchy at fair value using significant unobservable inputs (Level 3). We recognize transfers between levels of the fair value hierarchy as of the end of the reporting period. There were no transfers within the fair value hierarchy during the six-month period ended June 30, 2017.

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7. Employee Benefit Plans and Postretirement Benefits:

We maintain a non-contributory qualified defined benefit pension plan. Future benefit accruals for all eligible nonbargaining employees covered by the pension plan have ceased. We also maintain supplemental executive retirement plans that provide unfunded, non-qualified supplemental retirement benefits to a select group of management employees. Additionally, we provide postretirement healthcare and life insurance benefits for eligible employees. Employees share in, and we fund, the costs of these plans as benefits are paid.

The components of pension benefit (income) expense, including provision for executive retirement agreements, were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions)	2017	2016	2017	2016
Benefits earned during the period	$2.0	$2.0	$4.1	$4.2
Interest cost on benefit obligation	11.5	13.9	23.1	27.7
Net actuarial (gain) loss	(2.3)	2.4	(2.3)	2.4
Amortization of prior service credit	(0.1)	(0.1)	(0.2)	(0.2)
Expected return on plan assets	(13.6)	(16.2)	(27.2)	(32.4)
Net periodic benefit (income) expense	$(2.5)	$2.0	$(2.5)	$1.7

The expected employer contributions to the qualified pension plan to meet our 2017 annual funding requirements are $27.0 million. On January 12, 2017, we made our required quarterly employer contribution of $8.0 million in cash to the qualified pension plan. We intend to fund the remaining 2017 contributions using cash, our common stock, or a combination thereof. On March 2, 2017, we filed an effective shelf registration statement on Form S-3 (the “Registration Statement”) to offer and sell various securities from time to time. Under the Registration Statement, we established an at-the-market common stock offering program (the “ATM Program”) to sell shares of our common stock. We intend to utilize the ATM Program to facilitate contributions of cash to the qualified pension plan, if the price we can obtain for our common stock is no less than $6.00 per share. During the six months ended June 30, 2017, we issued and sold 1.3 million shares of common stock under the ATM Program and received proceeds of approximately $9.6 million, net of commissions. At June 30, 2017, subject to the terms and conditions of the ATM Program, we may sell an additional $15.2 million aggregate offering price of shares of common stock under the ATM Program. On April 14, 2017 and July 14, 2017, we made in cash our required quarterly contributions of $8.9 million and $1.5 million, respectively, using primarily proceeds from the ATM Program. The amount and timing of future contributions to the qualified pension plan are dependent upon a myriad of factors including future investment performance, changes in future discount rates and changes in the demographics of the population participating in the plan. We also expect to make cash contributions in 2017 totaling $0.9 million to fund the expected benefit payments of our unfunded supplemental executive retirement pension plans.

The components of postretirement benefits expense (income) were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions)	2017	2016	2017	2016
Interest cost on benefit obligation	$0.2	$0.3	$0.5	$0.6

Amortization of net actuarial loss	0.1	—	0.1	0.1
Amortization of prior service credit	(0.1)	—	(0.2)	(0.4)
Plan curtailment	—	—	—	(5.5)
Net periodic benefit expense (income)	$0.2	$0.3	$0.4	$(5.2)

During the first quarter of 2016, we made changes to our postretirement medical plan, eliminating medical and prescription drug subsidies primarily for certain active participants effective March 14, 2016. As a result, we remeasured the plan and recognized curtailment gains totaling $5.5 million, which was recognized in cost of services and selling, general and administrative expenses, with the offsetting effect recorded as a reduction in accumulated other comprehensive income.

We contributed $1.4 million to the postretirement plan during the six-month period ended June 30, 2017, and expect to contribute an additional $0.5 million for postretirement benefits throughout the remainder of 2017, excluding amounts that will be funded by participant contributions to the plan.

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7. Employee Benefit Plans and Postretirement Benefits, Continued:

We also sponsor an employee savings plan under section 401(k) of the Internal Revenue Code, which covers substantially all salaried employees and certain bargaining unit employees. Windstream matches on an annual basis up to a maximum of 4.0 percent of employee pre-tax contributions to the plan for employees contributing up to 5.0 percent of their eligible pre-tax compensation. We recorded expenses of $4.7 million and $11.5 million in the three and six month periods ended June 30, 2017, respectively, as compared to $4.2 million and $10.7 million for the same periods in 2016 related to our matching contribution under the employee savings plan, which was included in cost of services and selling, general and administrative expenses in our consolidated statements of operations. Expense related to our 2017 matching contribution expected to be made in Windstream Holdings common stock is included in share-based compensation expense in the accompanying consolidated statements of cash flow. In March 2017, we contributed 3.1 million shares of our common stock with a fair value of $22.7 million, as determined by the plan trustee, and $0.6 million in cash to the plan for the 2016 annual matching contribution. Additionally, we contributed 3.2 million shares of our common stock to the plan for the 2015 annual matching contribution during the six-month period ended June 30, 2016. At the time of this contribution, the shares had a fair value of approximately $24.0 million as determined by the plan trustee.

8. Share-Based Compensation Plans:

Under the Amended and Restated 2006 Equity Incentive Plan (the "Incentive Plan"), we may issue a maximum of 24.3 million equity stock awards in the form of restricted stock, restricted stock units, stock appreciation rights or stock options. As of June 30, 2017, the Incentive Plan had remaining capacity of approximately 4.4 million awards. As of June 30, 2017, we had additional remaining capacity of approximately 6.2 million awards from a similar equity incentive plan assumed in the merger with EarthLink.

Our Board of Directors approves grants of restricted stock and restricted stock units to officers, executives, non-employee directors and certain management employees. These grants include the standard annual grants to these employee and director groups as a key component of their annual incentive compensation plan and one-time grants. Grants may include time-based and performance-based awards. Time-based awards granted to employees vest over a service period of two or three years. Each recipient of the performance-based restricted stock units may vest in a number of shares from zero to 150.0 percent of their award based on attainment of certain operating targets, some of which are indexed to the performance of Standard & Poor's 500 Stock Index, over a three-year period.

The 2017 annual and three-year operating targets for these performance based restricted stock units were approved by the Board of Directors in February 2017 and May 2017. All performance targets for replacement awards granted to EarthLink employees were met prior to the merger date. For equity awards that contain only service conditions for vesting, we calculate the fair value of the award based on Windstream Holdings' closing price on the grant date determined in accordance with the applicable authoritative guidance.

The vesting periods and grant date fair value for restricted stock and restricted stock units issued, including the EarthLink replacement awards, were as follows for the six-month period ended June 30, 2017:

(Number of shares in thousands)	
Service-based restricted stock and restricted units:	
Vest variably over remaining service period, up to three years	2,858.7
Vest ratably over a three-year service period	1,201.4
Vest three years from date of grant, service based	33.8
Vest one year from date of grant, service based - granted to non-employee directors	207.2

Total granted	4,301.1
Grant date fair value (Dollars in millions)	$ 30.6
Performance restricted units:	
Vest variably over remaining required service period, up to three years	2,370.9
Vest contingently at the end of the respective performance period	1,258.6
Total granted	3,629.5
Grant date fair value (Dollars in millions)	$ 26.1

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

8. Share-Based Compensation Plans, Continued:

Service-based restricted stock and restricted unit activity for the six-month period ended June 30, 2017 was as follows:

	(Thousands) Underlying Number of Shares	Per Share Weighted Average Fair Value
Non-vested at December 31, 2016	3,283.8	$ 10.27
Replacement grants related to merger with EarthLink	2,858.7	$ 7.19
Granted	1,442.4	$ 9.12
Vested	(2,345.6)	$ 9.61
Forfeited	(475.9)	$ 8.07
Non-vested at June 30, 2017	4,763.4	$ 7.97

Performance restricted stock unit activity for the six-month period ended June 30, 2017 was as follows:

	(Thousands) Underlying Number of Shares	Per Share Weighted Average Fair Value
Non-vested at December 31, 2016	1,206.3	$ 5.64
Replacement grants related to merger with EarthLink	2,370.9	$ 7.19
Granted	1,258.6	$ 7.22
Vested	(1,590.6)	$ 7.32
Forfeited	(214.2)	$ 5.97
Non-vested at June 30, 2017	3,031.0	$ 6.60

At June 30, 2017, unrecognized compensation expense for restricted stock and restricted stock units totaled $35.1 million and is expected to be recognized over the weighted average vesting period of 1.8 years. Unrecognized compensation expense is included in additional paid-in capital in the accompanying consolidated balance sheets and statements of shareholders’ and member equity. The total fair value of shares vested was $34.2 million for the six-month period ended June 30, 2017, as compared to $21.2 million for the same period in 2016. Share-based compensation expense for restricted stock and restricted stock units was $10.9 million and $20.9 million for the three and six month periods ended June 30, 2017, respectively, as compared to $4.7 million and $11.3 million for the same periods in 2016.

In addition to including amounts related to restricted stock and restricted units, share-based compensation expense presented in the accompanying consolidated statements of cash flow also includes amounts related to certain executive and management incentive compensation plans and the matching contribution to the employee savings plan for which payments to eligible participants are expected to be made in Windstream Holdings common stock.

A summary of share-based compensation expense was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions)	2017	2016	2017	2016

Restricted stock and restricted units and stock options	$10.9	$4.7	$20.9	$11.3
Employee savings plan (See Note 7)	4.7	4.2	11.5	10.7
Management incentive compensation plans	—	—	—	0.6
Share-based compensation expense	$15.6	$8.9	$32.4	$22.6

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

9. Merger, Integration and Other Costs and Restructuring Charges:

We incur costs to complete a merger or acquisition and integrate its operations into our business, which are presented as merger, integration and other costs in our consolidated results of operations. These costs include transaction costs, such as accounting, legal, consulting and broker fees; severance and related costs; IT and network conversion; rebranding; and contract termination fees. During 2017, we incurred investment banking fees, legal, accounting and other consulting fees and severance and employee benefit costs related to the merger with EarthLink. During the fourth quarter of 2015, we began a network optimization project designed to consolidate traffic onto network facilities operated by us and reduce the usage of other carriers' networks in our acquired CLEC markets. In undertaking this initiative, we incurred costs to migrate traffic to lower cost circuits and to terminate existing contracts prior to their expiration. We will complete this project in 2017. Costs related to the network optimization project and our merger with EarthLink account for the merger, integration and other costs incurred in 2017.

Restructuring charges are primarily incurred as a result of evaluations of our operating structure. Among other things, these evaluations explore opportunities to provide greater flexibility in managing and financing existing and future strategic operations, for task automation and the balancing of our workforce based on the current needs of our customers. Severance, lease exit costs and other related charges are included in restructuring charges.

In the first half of 2017, we completed reductions in our workforce eliminating approximately 375 positions in our ILEC small business and enterprise segments as well as in our engineering, finance and information technology workgroups to more efficiently manage our operations. In completing these workforce reductions, we incurred severance and other employee benefit costs of $10.5 million. Restructuring charges in the first six months of 2016 principally consisted of $8.9 million of severance and other employee-related costs incurred in connection with completing several small workforce reductions.

A summary of the merger, integration and other costs and restructuring charges recorded was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions)	2017	2016	2017	2016
Merger, integration and other costs:				
Information technology conversion costs	$0.6	$—	$1.5	$—
Costs related to merger with EarthLink (a)	13.4	—	66.5	—
Network optimization and contract termination costs	1.6	2.4	4.9	6.6
Consulting and other costs	0.8	0.2	0.8	1.0
Total merger, integration and other costs	16.4	2.6	73.7	7.6
Restructuring charges	3.5	5.9	10.9	10.3
Total merger, integration and other costs and restructuring charges	$19.9	$8.5	$84.6	$17.9

(a) Includes investment banking, legal, accounting and other consulting fees of $22.8 million, severance and employee benefit costs for EarthLink employees terminated after the Merger of $29.5 million, share-based compensation expense of $9.8 million attributable to the accelerated vesting of replacement equity awards for terminated EarthLink employees and other miscellaneous expenses of $4.4 million.

After giving consideration to tax benefits on deductible items, merger, integration and other costs and restructuring charges increased our reported net loss $13.1 million and $58.0 million for the three and six month periods ended June 30, 2017, respectively, and $11.0 million for the six month period ended June 30, 2016. Merger, integration and other cots and restructuring charges decreased net income $5.2 million for the three month period ended June 30, 2016.

The following is a summary of the activity related to the liabilities associated with merger, integration and other costs and restructuring charges at June 30:

(Millions)	2017
Balance, beginning of period	$ 5.8
Merger, integration and other costs and restructuring charges	84.6
Cash outlays during the period	(77.7)
Balance, end of period	$ 12.7

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9. Merger, Integration and Other Costs and Restructuring Charges, Continued:

As of June 30, 2017, unpaid merger, integration and other costs and restructuring liabilities consisted of $3.0 million associated with the restructuring initiatives and $9.7 million related to merger and integration activities. Payments of these liabilities will be funded through operating cash flows.

10. Other-Than-Temporary Impairment Loss on Investment in Uniti Common Stock:

On April 24, 2015, we completed the spin-off of certain telecommunications network assets, including our fiber and copper networks and other real estate, to Uniti Group, Inc. (“Uniti”) (formerly Communications Sales & Leasing, Inc.). As of the spin-off date, we retained a passive ownership interest in approximately 19.6 percent of the common stock of Uniti. Shares of Uniti retained by us following the spin-off were classified as available-for-sale and recorded at fair value with unrealized gains and losses reported in accumulated other comprehensive income. No deferred income taxes were recorded with respect to the unrealized gains and losses due to the tax-free qualification of the spin-off.

During the first quarter of 2016, we recorded an other-than-temporary impairment loss of $181.9 million for the difference between the fair value of the Uniti common stock as of March 31, 2016 and our cost basis, which had been based on the market value of the shares on the date of spin-off. We recorded the other-than-temporarily impairment due to the duration in which the Uniti shares had traded at a market price below our initial cost basis. Following the recognition of the other-than-temporary impairment loss, the cost basis of the Uniti shares was adjusted to equal the March 31, 2016 market value of $653.8 million. Subsequent changes in the market value of the Uniti shares were recorded in accumulated other comprehensive income.

11. Net Gain on Disposal of Investment in Uniti Common Stock:

In June 2016, Windstream Services disposed of all of its shares of Uniti common stock through the completion of two debt-for-equity exchanges, pursuant to which Windstream Services transferred the Uniti shares to its bank creditors in exchange for the retirement of $672.0 million of borrowings outstanding under its revolving line of credit and to satisfy transaction-related expenses. Net of expenses, Windstream Services recognized a net gain on disposal of $17.3 million. Unrealized gains related to the Uniti common stock at the time of consummating the debt-for-equity exchanges were reclassified from accumulated other comprehensive income and included in the determination of the net gain on disposal.

12. Accumulated Other Comprehensive Income:

Accumulated other comprehensive income balances, net of tax, were as follows:

(Millions)	June 30, 2017	December 31, 2016
Pension and postretirement plans	$ (0.5)	$ (1.2)
Unrealized net gains on interest rate swaps:		
Designated portion	12.5	13.7
De-designated portion	(4.8)	(6.6)
Accumulated other comprehensive income	$ 7.2	$ 5.9

Changes in accumulated other comprehensive income balances, net of tax, were as follows:

(Millions)	Pension and	Total

	Net Gains on Interest Rate Swaps	Postretirement Plans	
Balance at December 31, 2016	$ 7.1	$ (1.2)	$ 5.9
Other comprehensive income before reclassifications	(1.2)	0.9	(0.3)
Amounts reclassified from other accumulated comprehensive income (a)	1.8	(0.2)	1.6
Balance at June 30, 2017	$ 7.7	$ (0.5)	$ 7.2

(a) See separate table below for details about these reclassifications.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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12. Accumulated Other Comprehensive Income, Continued:

Reclassifications out of accumulated other comprehensive income were as follows:

Details about Accumulated Other Comprehensive Income Components	(Millions) Amount Reclassified from Accumulated Other Comprehensive Income				Affected Line Item in the Consolidated Statements of Operations
	Three Months Ended June 30,		Six Months Ended June 30,		
	2017	2016	2017	2016	
Available-for-sale securities:					
Gain on disposal recognized in the period	$—	$(51.5)	$—	$(51.5)	Net gain on disposal of investment in Uniti common stock
Other-than-temporary impairment loss recognized in the period	—	—	—	181.9	Other-than-temporary impairment loss on investment in Uniti common stock
	—	(51.5)	—	130.4	Net (loss) income
Interest rate swaps:					
Amortization of net unrealized losses on de-designated interest rate swaps	1.4	1.0	2.9	2.2	Interest expense
	1.4	1.0	2.9	2.2	Loss before income taxes
	(0.5)	(0.3)	(1.1)	(0.8)	Income tax benefit
	0.9	0.7	1.8	1.4	Net (loss) income
Pension and postretirement plans:					
Plan curtailment	—	—	—	(5.5)	(a)
Amortization of net actuarial loss	0.1	—	0.1	0.1	(a)
Amortization of prior service credits	(0.2)	(0.1)	(0.4)	(0.6)	(a)
	(0.1)	(0.1)	(0.3)	(6.0)	Loss before income taxes
	—	0.1	0.1	2.4	Income tax benefit
	(0.1)	—	(0.2)	(3.6)	Net (loss) income
Total reclassifications for the period, net of tax	$0.8	$(50.8)	$1.6	$128.2	Net (loss) income

(a) These accumulated other comprehensive income components are included in the computation of net periodic benefit expense (income) (see Note 7).

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

13. Income Taxes:

The significant components of the net deferred income tax (asset) liability were as follows:

(Millions)	June 30, 2017	December 31, 2016
Property, plant and equipment	$1,377.3	$ 1,395.8
Goodwill and other intangible assets	1,317.2	1,265.6
Operating loss and credit carryforward	(887.0)	(528.8)
Postretirement and other employee benefits	(134.0)	(142.4)
Deferred compensation	(4.1)	(4.0)
Bad debt	(20.3)	(19.4)
Long-term lease obligations	(1,902.4)	(1,932.7)
Deferred debt costs	8.7	8.9
Restricted stock	(17.4)	(9.4)
Other, net	(41.0)	(28.6)
	(303.0)	5.0
Valuation allowance	249.5	146.5
Deferred income taxes, net	$(53.5)	$ 151.5
Deferred tax assets	$(3,043.0)	$ (2,695.9)
Deferred tax liabilities	2,989.5	2,847.4
Deferred income taxes, net	$(53.5)	$ 151.5

At June 30, 2017 and December 31, 2016, we had gross federal net operating loss carryforwards of approximately $1,966.9 million and $1,094.2 million, respectively, which expire in varying amounts from 2023 through 2037. The loss carryforwards at June 30, 2017 were primarily losses acquired in conjunction with our prior acquisitions and the acquisition of EarthLink on February 27, 2017. The 2017 increase is primarily associated with the amount generated for the year and the acquisition of EarthLink.

At June 30, 2017 and December 31, 2016, we had net state net operating loss carryforwards of approximately $118.6 million and $87.2 million, respectively, which expire annually in varying amounts from 2017 through 2037. The loss carryforwards at June 30, 2017 were primarily losses acquired in conjunction with our prior acquisitions and the acquisition of EarthLink. The 2017 increase is primarily associated with the acquisition of EarthLink. Federal and state tax rules limit the deductibility of loss carryforwards in years following an ownership change. As a result of these limitations or the expected lack of sufficient future taxable income, we believe that it is more likely than not that the benefit from certain federal and state loss carryforwards will not be realized prior to their expiration. In 2015, Windstream's board of directors adopted a shareholder rights plan designed to protect our net operating loss carryforwards from the effect of limitations imposed by federal and state tax rules following an ownership change. This plan was designed to deter an ownership change (as defined in IRC Section 382) from occurring, and therefore protect our ability to utilize our federal and state net operating loss carryforwards in the future. The plan is not meant to be an anti-takeover measure and our board of directors has established a procedure to consider requests to exempt the acquisition of Windstream common stock from the rights plan, if such acquisition would not limit or impair the availability of our net loss carryforwards.

We establish valuation allowances when necessary to reduce deferred tax assets to amounts expected to be realized. Therefore, as of June 30, 2017 and December 31, 2016, we recorded valuation allowances of approximately $243.3 million and $140.3 million, respectively, related to federal and state loss carryforwards which are expected to expire before they are utilized. The 2017 increase in the valuation allowance is related to the acquisition of federal and state

net operating losses from EarthLink and was recorded with an offset through goodwill.

The amount of federal tax credit carryforward at June 30, 2017 and December 31, 2016 was approximately $63.7 million and $48.7 million, respectively, which expire in varying amounts from 2031 through 2036. The 2017 increase is primarily associated with the acquisition of EarthLink. The amount of state tax credit carryforward was approximately $22.7 million at both June 30, 2017 and December 31, 2016, which expire in varying amounts from 2017 through 2027. Due to the expected lack of sufficient future taxable income, we believe that it is more likely than not that the benefit from some of the state tax credit carryforwards will not be realized prior to their expiration. Therefore, we recorded valuation allowances of approximately $6.2 million (net of federal benefit) to reduce deferred tax assets to amounts expected to be realized at both June 30, 2017 and December 31, 2016.

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14. (Loss) Earnings per Share:

We compute basic earnings (loss) per share by dividing net income (loss) applicable to common shares by the weighted average number of common shares outstanding during each period. Our non-vested restricted shares containing a non-forfeitable right to receive dividends on a one-to-one per share ratio to common shares are considered participating securities, and the impact is included in the computation of earnings (loss) per share pursuant to the two-class method. Calculations of earnings (loss) per share under the two-class method exclude from the numerator any dividends paid or owed on participating securities and any undistributed earnings considered to be attributable to participating securities. The related participating securities are similarly excluded from the denominator.

Diluted earnings (loss) per share is computed by dividing net income (loss) applicable to common shares by the weighted average number of common shares adjusted to include the effect of potentially dilutive securities. Potentially dilutive securities include incremental shares issuable upon exercise of outstanding stock options and warrants. Diluted earnings (loss) per share excludes all potentially dilutive securities if their effect is anti-dilutive.

We also issue performance-based restricted stock units as part of our share-based compensation plan. Certain of these restricted stock units contain a forfeitable right to receive dividends. Because dividends attributable to these shares are forfeited if the vesting provisions are not met, they are considered non-participating restricted shares and are not dilutive under the two-class method until the performance conditions have been satisfied. As of June 30, 2017, the performance conditions for the outstanding restricted stock units have not yet been satisfied. Restricted stock units, stock options and warrants granted in conjunction with past acquisitions are included in the computation of dilutive earnings (loss) per share using the treasury stock method.

A reconciliation of net (loss) income and number of shares used in computing basic and diluted (loss) earnings per share was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions, except per share amounts)	2017	2016	2017	2016
Basic and diluted (loss) earnings per share:				
Numerator:				
Net (loss) income	$(68.1)	$1.5	$(179.4)	$(230.4)
Income allocable to participating securities	(0.7)	(0.6)	(1.3)	(1.1)
Net (loss) income attributable to common shares	$(68.8)	$0.9	$(180.7)	$(231.5)
Denominator:				
Basic and diluted shares outstanding				
Weighted average shares outstanding	190.7	96.4	160.2	98.1
Weighted average participating securities	(3.1)	(3.6)	(3.3)	(4.9)
Weighted average basic and diluted shares outstanding	187.6	92.8	156.9	93.2
Basic and diluted (loss) earnings per share:				
Net (loss) income	($.37)	$.01	($1.15)	($2.48)

We have excluded from the computation of diluted shares the effect of restricted stock units and options to purchase shares of our common stock because their inclusion would have an anti-dilutive effect due to our reported net loss for

the three and six month periods ended June 30, 2017 and the six month period ended June 30, 2016. Stock options totaling 0.4 million shares were also excluded for the three month period ended June 30, 2016 because the exercise prices were greater than the average market price of our common stock. We had 4.7 million restricted stock units and 0.2 million stock options outstanding as of June 30, 2017, compared to 1.4 million restricted stock units and 0.4 million stock options outstanding at June 30, 2016.

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15. Segment Information:

Our business unit organizational structure is focused on our core customer relationships. Enterprise customers consist of those relationships that have the propensity now or in the future to generate at least $1,500 or more in monthly recurring revenue. Business customers not meeting this criterion are classified as small business. In classifying our business customers, we consider the maximum potential revenue to be generated from the customer relationship for both our existing customer base and any new customers in determining which business unit can best support the customer. Accordingly, over time, we may prospectively change the classification of a particular business customer between enterprise and small business. Our consumer and small business customer base is further disaggregated between those customers located in service areas in which we are the incumbent local exchange carrier ("ILEC") and provide services over network facilities operated by us and those customers located in service areas in which we are a competitive local exchange carrier ("CLEC") and provide services over network facilities primarily leased from other carriers. Under our current organizational structure, we have combined our ILEC Consumer and Small Business operations into one segment and we have combined into a separate segment our CLEC Consumer and Small Business operations due to similarities with respect to product and service offerings, marketing strategies and customer service delivery. Following the merger with EarthLink, we operate and report these four customer-based segments:

- ILEC Consumer and Small Business - We manage as one business our residential and small business operations in those markets in which we are the ILEC due to the similarities with respect to service offerings, marketing strategies and customer service delivery. Products and services offered to customers include traditional local and long-distance voice services and high-speed Internet services, which are delivered primarily over network facilities operated by us. We offer consumer video services primarily through a relationship with Dish Network LLC and we also own and operate cable television franchises in some of our service areas. We offer Kinetic, a complete video entertainment offering in our Lincoln, Nebraska; Lexington, Kentucky; Sugar Land, Texas markets, as well as several communities in North Carolina.

Residential customers can bundle voice, high-speed Internet and video services, to provide one convenient billing solution and receive bundle discounts. Small Business - ILEC services offer a wide range of advanced Internet, voice, and web conferencing products. These services are equipped to deliver high-speed Internet with competitive speeds, value added services to enhance business productivity and options to bundle services for a global business solution to meet our small business customer needs.

- Wholesale - Our wholesale operations are focused on providing products and services to other communications services providers. Our service offerings leverage Windstream's extensive fiber network to provide wave transport services, carrier Ethernet services, fiber-to-tower connections to support backhaul services to wireless carriers, and high speed Internet access. We also offer traditional services including special access services and Time Division Multiplexing ("TDM") private line transport. The combination of these services allow wholesale customers to provide voice and data services to their customers through the use of our network or in combination with their own networks.

- Enterprise - Products and services offered by our enterprise operations include integrated voice and data services, which deliver voice and broadband services over a single Internet connection, multi-site networking services which provide a fast and private connection between business locations, as well as a variety of other data services, including cloud computing and collocation and managed services as an alternative to traditional information technology infrastructure.

- CLEC Consumer and Small Business - Products and services offered to customers include integrated voice and data services, advanced data and traditional voice and long-distance services, as well as value added services including

online backup, managed web design and web hosting, and various e-mail services.

We evaluate performance of the segments based on segment income, which is computed as segment revenues and sales less segment operating expenses. As further discussed below, certain operating revenues and expenses are not assigned to our segments. During the second quarter of 2017, we realigned certain engineering teams focused on specific initiatives to enhance our broadband capabilities and network expansion and have allocated the related labor costs to the appropriate segment. Previously, these labor costs had not been assigned to our segments. We also reclassified certain product sales and the related cost of products sold from our Enterprise segment to CLEC Consumer and Small Business segment to better align these sales to the customer base purchasing these products. In addition, we revised our methodology for determining segment income to include within the segment operating results a reduction for certain engineering and other costs attributable to the construction of property, plant and equipment, including capitalized labor. Previously, internal costs associated with capitalizable activities were included in segment costs and expenses, while the associated benefits for capitalizing these costs were not allocated to the segments and were included within other unassigned operating expenses in reconciling total segment income to total consolidated net (loss) income. We believe these changes more accurately present the operating results of each of our business segments. Prior period segment information has been revised to reflect these changes for all periods presented. The changes had no impact on our consolidated results of operations.

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15. Segment Information, Continued:

Segment revenues are based upon each customer's classification to an individual segment and include all services provided to that customer. Certain operating revenues are derived from activities that are centrally-managed by us and, accordingly, these revenues are not included in any of our four segments presented below. These other operating revenues include revenue from federal and state universal service funds, CAF Phase II support, and funds received from federal access recovery mechanisms. We also generate other service revenues from providing switched access services, which include usage-based revenues from long-distance companies and other carriers for access to our network to complete long-distance calls, as well as reciprocal compensation received from wireless and other local connecting carriers for the use of network facilities. Other operating revenues also include certain surcharges assessed to our customers, including billings for our required contributions to federal and state USF programs and product sales to contractors.

Segment expenses include specific expenses incurred as a direct result of providing services and products to segment customers; selling, general and administrative expenses that are directly associated with specific segment customers or activities; and certain allocated expenses which include network expenses, facilities expenses and other expenses, such as vehicle and real estate-related expenses. We do not assign depreciation and amortization expense, merger, integration and other costs, restructuring charges, share-based compensation and pension costs to our segments, because these expenses are centrally managed and are not monitored by or reported to the chief operating decision maker ("CODM") by segment. Similarly, certain regulatory fees, cost of products sold to contractors, and centrally-managed administrative functions, such as accounting and finance, information technology, network management, legal and human resources, are not assigned to our segments. Interest expense and net loss on early extinguishment of debt have also been excluded from segment operating results because we manage our financing activities on a total company basis and have not assigned any long-term debt obligations to the segments. Amounts related to our investment in Uniti common stock consisting of dividend income, net gain on disposal and other-than-temporary impairment loss, as well as other (expense) income, net, and income tax benefit are not monitored as a part of our segment operations and, therefore, these items also have been excluded from our segment operating results.

Asset information by segment is not monitored or reported to the CODM and therefore has not been presented. All of our customers are located in the United States and we do not have any single customer that provides more than 10 percent of our total consolidated revenues and sales.

The following table summarizes our segment results:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions)	2017	2016	2017	2016
ILEC Consumer and Small Business:				
Revenues and sales	$387.2	$395.2	$778.2	$792.4
Costs and expenses	174.8	174.6	349.8	348.0
Segment income	212.4	220.6	428.4	444.4
Wholesale:				
Revenues	175.9	159.9	333.4	323.1
Costs and expenses	59.5	43.9	107.4	87.4
Segment income	116.4	116.0	226.0	235.7
Enterprise:				

Revenues and sales	574.9	505.8	1,100.4	1,015.3
Costs and expenses	472.1	418.2	907.1	848.7
Segment income	102.8	87.6	193.3	166.6
CLEC Consumer and Small Business:				
Revenues	193.1	128.8	333.4	261.1
Costs and expenses	121.0	87.5	211.2	178.4
Segment income	72.1	41.3	122.2	82.7
Total segment revenues and sales	1,331.1	1,189.7	2,545.4	2,391.9
Total segment costs and expenses	827.4	724.2	1,575.5	1,462.5
Total segment income	$503.7	$465.5	$969.9	