

# Notes to Consolidated Financial Statements

## 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Nature of Operations

Telephone and Data Systems, Inc. ("TDS") is a diversified telecommunications company providing high-quality telecommunications services to approximately 6.1 million wireless telephone customers and wireline telephone equivalent access lines in 36 states at December 31, 2004. TDS conducts substantially all of its wireless telephone operations through its 82.0%-owned subsidiary, United States Cellular Corporation ("U.S. Cellular") and its incumbent local exchange carrier and competitive local exchange carrier wireline telephone operations through its wholly owned subsidiary, TDS Telecommunications Corporation ("TDS Telecom").

See Note 25 – Business Segment Information for summary financial information on each business segment.

### Principles of Consolidation

The accounting policies of TDS conform to accounting principles generally accepted in the United States of America ("U.S. GAAP"). The consolidated financial statements include the accounts of TDS, its majority-owned subsidiaries since acquisition, the wireless partnerships in which it has a majority general partnership interest and any entity where TDS has a variable interest that will absorb a majority of the entity's expected gains or losses, or both. All material intercompany items have been eliminated.

TDS adopted Financial Accounting Standards Board ("FASB") Interpretation No. 46R ("FIN 46R"), "Consolidation of Variable Interest Entities," in January 2004. The adoption of FIN 46R did not have a material impact on TDS's financial position or results of operations.

### Business Combinations

TDS uses the purchase method of accounting for business combinations. TDS includes as investments in subsidiaries the value of the consideration given and all direct and incremental costs relating to acquisitions. All costs relating to unsuccessful negotiations for acquisitions are charged to expense.

### Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect (a) the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and (b) the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### Reclassifications

Certain amounts reported in prior years have been reclassified to conform to current period presentation. The reclassifications had no impact on previously reported net income and stockholders' equity.

### Cash and Cash Equivalents

Cash and cash equivalents include cash and those short-term, highly liquid investments with original maturities of three months or less.

Outstanding checks totaled \$19.3 million and \$22.3 million at December 31, 2004 and 2003, respectively, and are classified as accounts payable in the consolidated Balance Sheets.

### Accounts Receivable and Allowance for Doubtful Accounts

U.S. Cellular's accounts receivable primarily consist of amounts owed by customers for both service provided and equipment sales, by agents for equipment sales, by other wireless carriers whose customers have used U.S. Cellular's wireless systems and by unaffiliated third-party partnerships or corporations pursuant to equity distribution declarations.

TDS Telecom's accounts receivable primarily consist of amounts owed by customers for services provided, by connecting companies for carrying interstate and intrastate long-distance traffic on its network, and by interstate and intrastate revenue pools that distribute access charges.

The allowance for doubtful accounts is the best estimate of the amount of probable credit losses in the existing accounts receivable. The allowance is based on historical write-off experience. Account receivable balances are reviewed on either an aggregate basis or individual basis for collectibility depending on the type of receivable. When it is probable the account balance will not be collected, the account balance is charged off against the allowance for the doubtful accounts. TDS does not have any off-balance sheet credit exposure related to its customers.

The changes in the allowance for doubtful accounts during the years ended December 31, 2004, 2003 and 2002 were as follows:

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Beginning Balance	\$ 25,327	\$ 40,475	\$ 13,657
Additions, net of recoveries	86,938	65,379	84,897
Deductions	(87,322)	(80,527)	(58,079)
Ending Balance	\$ 24,943	\$ 25,327	\$ 40,475

### Materials and Supplies

U.S. Cellular's inventory, primarily handsets and accessories, is stated at the lower of cost or market with cost determined using the first-in, first-out method. TDS Telecom's materials and supplies are stated at average cost.

### Marketable Equity Securities

Marketable equity securities are classified as available-for-sale, and are stated at fair market value. Net unrealized holding gains and losses are included in accumulated other comprehensive income. Realized gains and losses are determined on the basis of specific identification.

The market values of marketable equity securities may fall below the accounting cost basis of such securities. If management determines the decline in value to be other than temporary, the unrealized loss included in accumulated other comprehensive income is recognized and recorded as a non-operating loss in the Statement of Operations.

Factors that management considers in determining whether a decrease in the market value of its securities is an other-than-temporary decline include if there has been a significant change in the financial condition, operational structure or near-term prospects of the issuer; how long and how much the security has been below

carrying value; and whether TDS has the intent and ability to retain its investment in the issuer's securities to allow the market value to return to the accounting cost basis.

TDS utilizes derivative financial instruments to reduce market risks due to fluctuations in market prices of marketable equity securities. At December 31, 2004 and 2003, TDS had variable prepaid forward contracts ("forward contracts") maturing in 2007 and 2008 in connection with substantially all TDS's marketable equity security portfolio, hedging the market price risk with respect to the contracted securities. The downside risk is hedged at or above the accounting cost basis thereby eliminating the risk of an other-than-temporary loss being recorded on these contracted securities.

### Derivative Instruments

TDS utilizes derivative financial instruments to reduce marketable equity security market value risk. TDS does not hold or issue derivative financial instruments for trading purposes. TDS recognizes all derivatives as either assets or liabilities on the Balance Sheet and measures those instruments at fair value. Changes in fair value of those instruments are reported in the Statements of Operations or accumulated other comprehensive income depending on the use of the derivative and whether it qualifies for hedge accounting. The accounting for gains and losses associated with changes in the fair value of the derivative and the effect on the consolidated financial statements depends on the derivative's hedge designation and whether the hedge is anticipated to be highly effective in achieving offsetting changes in the fair value of the hedged item or cash flows of the asset hedged.

### Licenses

Licenses consist of costs incurred in acquiring Federal Communications Commission ("FCC") licenses to provide wireless service. These costs include amounts paid to license applicants and owners of interests in entities awarded licenses and all direct and incremental costs relating to acquiring the licenses. Licenses are intangible assets with indefinite useful lives and are not amortized.

TDS has determined that licenses are intangible assets with indefinite useful lives, based on the following factors:

- Radio spectrum is not a depleting asset.
- The ability to use radio spectrum is not limited to any one technology.
- U.S. Cellular and its consolidated subsidiaries are licensed to use radio spectrum through the FCC licensing process, which enables licensees to utilize specified portions of the spectrum for the provision of wireless service.
- U.S. Cellular and its consolidated subsidiaries are required to renew their FCC licenses every ten years. To date, all of U.S. Cellular's license renewal applications, filed for unique licenses in every year from 1994 to the present, have been granted by the FCC. Generally, license renewal applications filed by licensees otherwise in compliance with FCC regulations are routinely granted. If, however, a license renewal application is challenged, either by a competing applicant for the license or by a petition to deny the renewal application,

the license will be renewed if the licensee can demonstrate its entitlement to a "renewal expectancy." Licensees are entitled to such an expectancy if they can demonstrate to the FCC that they have provided "substantial service" during their license term and have "substantially complied" with FCC rules and policies. U.S. Cellular believes that it could demonstrate its entitlement to a renewal expectancy in any of its markets in the unlikely event any of its license renewal applications were challenged, and therefore believes that it is probable that its future license renewal applications will be granted.

### License Rights

In accordance with an exchange agreement with AT&T Wireless, U.S. Cellular has deferred the assignment and development of certain licenses for a period of up to five years from the closing date, August 1, 2003. The 21 licenses that have not yet been assigned to U.S. Cellular, with a recorded value of \$42.0 million, are included in license rights on the Balance Sheet.

### Goodwill

TDS has goodwill as a result of the acquisition of licenses and wireless markets, and the acquisition of operating telephone companies. U.S. Cellular's goodwill reflects the portion of the purchase price of acquisitions of interest in operating wireless markets that was not assigned to the other acquired assets, including licenses. TDS Telecom's goodwill reflects the costs in excess of the underlying fair value of the net tangible and intangible assets of acquired telephone companies. No deferred taxes have been provided on goodwill.

### Impairment of Intangible Assets

Licenses and goodwill must be reviewed for impairment annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired. TDS performs the annual impairment review on licenses and goodwill during the second quarter. There can be no assurance that upon review at a later date material impairment charges will not be required.

The intangible asset impairment test consists of comparing the fair value of the intangible asset to the carrying amount of the intangible asset. If the carrying amount exceeds the fair value, an impairment loss is recognized for the difference. The goodwill impairment test is a two-step process. The first step compares the fair value of the reporting unit to its carrying value. If the carrying amount exceeds the fair value, the second step of the test is performed to measure the amount of impairment loss, if any. The second step compares the implied fair value of reporting unit goodwill with the carrying amount of that goodwill. To calculate the implied fair value of goodwill, an enterprise allocates the fair value of the reporting unit to all of the assets and liabilities of that reporting unit (including any unrecognized intangible assets) as if the reporting unit had been acquired in a business combination and the fair value was the price paid to acquire the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to the assets and liabilities of the reporting unit is the implied fair value of goodwill. If the carrying amount exceeds the implied fair value, an impairment loss is recognized for that difference.

The fair value of an intangible asset and reporting unit goodwill is the amount at which that asset or reporting unit could be bought or sold in a current transaction between willing parties. Therefore, quoted market prices in active markets are the best evidence of fair value and should be used when available. If quoted market prices are not available, the estimate of fair value is based on the best information available, including prices for similar assets and the use of other valuation techniques. Other valuation techniques include present value analysis, multiples of earnings or revenue or a similar performance measure. The use of these techniques involve assumptions by management about factors that are highly uncertain including future cash flows, the appropriate discount rate, and other inputs. Different assumptions for these inputs or valuation methodologies could create materially different results.

U.S. Cellular tests goodwill for impairment at the level of reporting referred to as a reporting unit. U.S. Cellular has identified six reporting units pursuant to paragraph 30 of Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets." The six reporting units represent six geographic groupings of FCC licenses, constituting six geographic service areas. U.S. Cellular combines its FCC licenses into six units of accounting for purposes of testing the licenses for impairment pursuant to Emerging Issues Task Force Issue 02-7, "Unit of Accounting for Testing Impairment of Indefinite-Lived Intangible Assets" ("EITF 02-7"), and SFAS No. 142, using the same geographic groupings as its reporting units. The divestitures of markets in 2004 resulted in the elimination of one of the six reporting units.

U.S. Cellular prepared valuations of each of the reporting units for purposes of goodwill impairment testing. A discounted cash flow approach was used to value each of the reporting units, using value drivers and risks specific to each individual geographic region. The cash flow estimates incorporate assumptions that market participants would use in their estimates of fair value. Key assumptions made in this process were the selection of a discount rate, estimated future cash flow levels, projected capital expenditures, and selection of terminal value multiples.

U.S. Cellular also prepared valuations of similar groupings of FCC licenses (units of accounting pursuant to EITF 02-7) using an excess earnings methodology, through the use of a discounted cash flow approach. This excess earnings methodology estimates the fair value of the intangible assets (FCC license units of accounting) by measuring the future cash flows of the license groups, reduced by charges for contributory assets such as working capital, trademarks, existing subscribers, fixed assets, assembled workforce and goodwill.

TDS Telecom has recorded goodwill primarily as a result of the acquisition of operating telephone companies. TDS Telecom has assigned goodwill to its incumbent local exchange carrier reporting unit and its competitive local exchange carrier reporting units. The incumbent local exchange carrier reporting unit was valued using a multiple of cash flow valuation technique.

TDS Telecom's competitive local exchange carrier has two reporting units for purposes of impairment testing as defined by SFAS No. 142, the larger reporting unit was valued using a market approach and the smaller reporting unit was valued using an income approach. The market approach compares the reporting unit to similar companies whose securities are actively traded. Ratios or multiples of value relative to certain significant financial measures, such as revenue and earnings are developed based upon the comparable companies. The valuation multiples are applied to the appropriate financial measures of the reporting unit to indicate its value. The income approach uses a discounted cash flow analysis based on value drivers and risks specific to its reporting unit. The cash flow estimates incorporate assumptions that market participants would use in their estimates of fair value. Key assumptions made in this process were the selection of a discount rate, estimated future cash flow levels, projected capital expenditures, and determination of terminal value.

#### **Investments in Unconsolidated Entities**

Investments in unconsolidated entities consists of investments where TDS holds a less than 50% non-controlling ownership interest. TDS follows the equity method of accounting, which recognizes TDS's proportionate share of the income and losses accruing to it under the terms of its partnership or shareholder agreements, where TDS's ownership interest equals or exceeds 20% for corporations and 3% to 5% for partnerships and limited liability companies. An estimate of TDS's proportionate share of income is recorded each quarter with such estimate being adjusted to the actual share of income upon receipt of financial statements from the unconsolidated entity. The cost method of accounting is followed for certain minority interests where TDS's ownership interest is less than 20% for corporations and 3% to 5% for partnerships and limited liability companies, or where TDS does not have the ability to exercise significant influence.

#### **Property, Plant and Equipment**

##### ***U.S. Cellular***

U.S. Cellular's property, plant and equipment is stated at the original cost of construction including capitalized costs of certain taxes, payroll-related expenses and estimated costs to remove the assets.

Renewals and betterments of units of property are recorded as additions to plant in service. The original cost of depreciable property retired (along with the related accumulated depreciation) is removed from plant in service and, together with removal cost less any salvage realized, is charged to depreciation expense. Repairs and renewals of minor units of property are charged to system operations expense.

Costs of developing new information systems are capitalized in accordance with Statement of Position 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use," ("SOP 98-1") and amortized over a three- or seven-year period, starting when each new system is placed in service.

### **TDS Telecom**

#### Incumbent Local Exchange Carrier Operations

TDS Telecom's incumbent local exchange carrier property, plant and equipment is stated at the original cost of construction including the capitalized costs of certain taxes, payroll-related expenses, and an allowance for funds used during construction.

Renewals and betterments of units of property are recorded as additions to telephone plant in service. The original cost of depreciable property retired is removed from plant in service and, together with removal cost less any salvage realized, is charged to accumulated depreciation. No gain or loss is recognized on ordinary retirements of depreciable telephone property. Repairs and renewals of minor units of property are charged to plant operations expense.

Costs of developing new information systems are capitalized and amortized starting when each new system is placed in service.

TDS's incumbent local exchange carrier operations follow accounting for regulated enterprises prescribed by SFAS No. 71,

"Accounting for the Effects of Certain Types of Regulation."

Management periodically reviews the criteria for applying these provisions to determine whether continuing application of SFAS No. 71 is appropriate. Management believes that such criteria are still being met and therefore has no current plans to change its method of accounting.

#### Competitive Local Exchange Carrier Operations

TDS Telecom's competitive local exchange carrier property, plant and equipment is stated at the original cost of construction including capitalized costs of certain taxes and payroll-related expenses.

Renewals and betterments of units of property are recorded as additions to plant in service. The original cost of depreciable property retired (along with the related accumulated depreciation) is removed from plant in service and, together with removal cost less any salvage realized, is charged to depreciation expense. Repairs and renewals of minor units of property are charged to maintenance expense.

Costs of developing new information systems are capitalized and amortized starting when each new system is placed in service.

### **Depreciation**

U.S. Cellular provides for depreciation using the straight-line method over the estimated useful lives of the assets.

U.S. Cellular depreciates its leasehold improvement assets associated with leased properties over periods ranging from three to ten years, which approximates the shorter of the assets' economic lives or the specific lease terms, as defined in SFAS No. 13, "Accounting for Leases," as amended.

TDS Telecom's incumbent local exchange carrier operations provide for depreciation on a group basis according to depreciable rates approved by state public utility commissions. TDS Telecom's competitive local exchange carrier operations provide for depreciation using the straight-line method over the estimated useful lives of the assets.

### **Asset Impairment**

TDS reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be fully recoverable. The tangible asset impairment test is a two-step process. The first step compares the carrying value of the assets with the estimated undiscounted cash flows over the remaining asset life. If the carrying value of the assets is greater than the undiscounted cash flows, the second step of the test is performed to measure the amount of impairment loss. The second step compares the estimated fair value of the assets to the carrying value of the assets. An impairment loss is recognized for the difference between the fair value of the assets (less cost to sell) and the carrying value of the assets.

The fair value of a tangible asset is the amount at which that asset could be bought or sold in a current transaction between willing parties. Therefore, quoted market prices in active markets are the best evidence of fair value and should be used when available. If quoted market prices are not available, the estimate of fair value is based on the best information available, including prices for similar assets and the use of other valuation techniques. A present value analysis of cash flow scenarios is often the best available valuation technique with which to estimate the fair value of the long-lived asset. The use of this technique involves assumptions by management about factors that are highly uncertain including future cash flows, the appropriate discount rate, and other inputs. Different assumptions for these inputs or valuation methodologies could create materially different results.

TDS Telecom's competitive local exchange carrier incurred a loss on impairment of long-lived assets in 2004. TDS Telecom has two asset groups for purposes of impairment testing. TDS Telecom valued the larger asset group using a market approach and the smaller asset group using an income approach. The market approach compares the asset group to similar companies whose securities are actively traded. Ratios or multiples of value relative to certain significant financial measures, such as revenue and earnings are developed based upon the comparable companies. The valuation multiples are applied to the appropriate financial measures of the asset group to indicate its value. The income approach uses a discounted cash flow analysis based on value drivers and risks specific to its asset group. The cash flow estimates incorporate assumptions that market participants would use in their estimates of fair value. Key assumptions made in this process were the selection of a discount rate, estimated future cash flow levels, projected capital expenditures, and determination of terminal value.

### **Assets and Liabilities of Operations Held For Sale**

TDS accounts for the disposal of long-lived assets in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." When long-lived assets meet the held for sale criteria set forth in SFAS No. 144, the Balance Sheet reflects the assets and liabilities of the properties to be disposed of as assets and liabilities of operations held for sale. The assets and liabilities of operations held for sale are presented separately in the asset and liability sections of the Balance Sheet. The revenues and expenses of the properties to be disposed of are included in operations until the transaction is completed.



### Asset Retirement Obligations

SFAS No. 143, "Accounting for Asset Retirement Obligations," was issued in June 2001, and became effective for TDS beginning January 1, 2003. SFAS No. 143 requires entities to record the fair value of a liability for legal obligations associated with an asset retirement in the period in which the obligations are incurred. When the liability is initially recorded, the entity capitalizes the cost of the asset retirement obligation by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the obligations, any differences between the cost to retire an asset and the liability recorded is recognized in the Statement of Operations as a gain or loss.

U.S. Cellular is subject to asset retirement obligations associated primarily with its cell sites, retail sites and office locations. Asset retirement obligations generally include obligations to remediate leased land on which U.S. Cellular's cell sites and switching offices are located. U.S. Cellular is also generally required to return leased retail store premises and office space to their pre-existing conditions.

The change in asset retirement obligation during 2004 and 2003 was as follows:

Year Ended December 31,	2004	2003
(Dollars in thousands)		
Beginning balance	\$64,501	\$54,438
Additional liabilities accrued	5,426	5,641
Disposition of assets	(2,065)	—
Accretion expense	4,672	4,422
Ending balance	\$72,534	\$64,501

TDS Telecom's incumbent local exchange carriers' rates are regulated by the respective state public utility commissions and the FCC and therefore, reflect the effects of the rate-making actions of these regulatory bodies in the financial statements of the TDS incumbent local exchange carriers. The incumbent local exchange carriers have recorded an asset retirement obligation in accordance with the requirements of SFAS No. 143 and a regulatory liability for the costs of removal that state public utility commissions have required to be recorded for regulatory accounting purposes which are in excess of the amounts required to be recorded in accordance with SFAS No. 143. These amounts combined make up the asset retirement obligation for the incumbent local exchange carriers.

The change in asset retirement obligation and regulatory obligation during 2004 and 2003 was as follows:

Year Ended December 31,	2004	2003
(Dollars in thousands)		
Beginning balance	\$60,000	\$55,300
Additional liabilities incurred	6,057	5,600
Costs of removal	(1,057)	(900)
Ending balance	\$65,000	\$60,000

The regulatory liability included in asset retirement obligation at December 31, 2004 and 2003 was \$31.1 million and \$28.2 million, respectively. The asset retirement obligation calculated in accordance with the provisions of SFAS No. 143 at December 31, 2004 and 2003 was \$33.9 million and \$31.8 million, respectively.

TDS Telecom's competitive local telephone carriers adopted SFAS No. 143 effective January 1, 2003. TDS Telecom determined that its competitive local telephone carriers do not have a material legal obligation to remove long-lived asset described by SFAS No. 143.

### Revenue Recognition

Revenues from wireless operations primarily consist of charges for access, airtime, roaming and value-added services provided for U.S. Cellular's retail customers and to end users through third-party resellers; charges to carriers whose customers use U.S. Cellular's systems when roaming; charges for long-distance calls made on U.S. Cellular's systems; amounts received from the universal service fund in states where U.S. Cellular has been designated an Eligible Telecommunications Carrier; end user equipment sales; and sales of accessories. Revenues are recognized as services are rendered. Unbilled revenues, resulting from wireless service provided from the billing cycle date to the end of each month and from other wireless carriers' customers using U.S. Cellular's systems for the last half of each month, are estimated and recorded.

Equipment sales represent a separate earnings process. Revenues from equipment and accessory sales are recognized upon delivery to the customer. In order to provide better control over handset quality, U.S. Cellular sells handsets to agents at a price approximately equal to cost. In most cases, the agents receive rebates from U.S. Cellular at the time the agents sign up new customers or retain current customers. U.S. Cellular accounts for the sale of equipment to agents in accordance with Emerging Issues Task Force ("EITF") Issue 01-09, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)." This standard requires that equipment sales revenue be reduced by the anticipated rebates to be paid to the agents at the time the agent purchases the handsets rather than at the time the agent signs up a new customer or retains a current customer. Similarly, U.S. Cellular offers certain rebates to customers related to handset purchases; in accordance with EITF Issue 01-09, the equipment sales revenue from a handset sale which includes such a rebate is recorded net of the rebate anticipated to be applied to the handset sale.

Activation fees charged with the sale of service only are deferred and recognized over the average customer service period.

Under EITF Issue 00-21, "Accounting for Multiple Element Arrangements," activation fees charged with the sale of equipment and service are allocated to the equipment and service based upon the relative fair values of each item. Due to the subsidy provided on customer handsets, this generally results in the recognition of the activation fee as additional handset revenue at the time of sale.

Revenue from incumbent local exchange carriers primarily consists of charges for the provision of local telephone exchange service; compensation for carrying interstate and intrastate long-distance traffic on TDS Telecom's local telephone networks; and charges for (i) leasing, selling, installing and maintaining customer premise equipment; (ii) providing billing and collection services; (iii) providing Internet services; (iv) reselling long-distance services; and (v) selling digital broadcast satellite receivers. Revenues are recognized as services are rendered.

TDS's incumbent local exchange carriers participate in revenue pools with other telephone companies for interstate revenue and for certain intrastate revenue. Such pools are funded by toll revenue and/or access charges within state jurisdictions and by access charges in the interstate market. Revenues earned through the various pooling processes are initially recorded based on TDS Telecom's estimates.

Revenue from competitive local exchange carriers primarily consists of charges for the provision of local telephone exchange service; compensation for carrying interstate and intrastate long-distance traffic on TDS Telecom's local telephone networks; and charges for providing Internet services and reselling long-distance services. Revenues are recognized as services are rendered.

#### Cumulative Effect of Accounting Changes

Effective January 1, 2003, TDS adopted SFAS No. 143 and recorded the initial liability for legal obligations associated with an asset retirement. The cumulative effect of the implementation of this accounting standard on periods prior to 2003 was recorded in the first quarter of 2003, decreasing net income by \$11.8 million, net of income taxes of \$9.7 million and minority interest of \$3.0 million or \$0.20 per diluted share.

The following pro forma amounts show the effect of the retroactive application of the change in accounting principle for the adoption of SFAS No. 143:

Year Ended December 31,	2003	2002
(Dollars in thousands, except per share amounts)		
Actual		
Net income (loss)	\$46,608	\$(994,772)
Basic earnings (loss) per share	0.80	(16.97)
Diluted earnings (loss) per share	\$ 0.79	\$ (16.97)
Pro forma		
Net income (loss)	\$58,397	\$(997,321)
Basic earnings (loss) per share	1.00	(17.01)
Diluted earnings (loss) per share	\$ 0.99	\$ (17.01)
(Dollars in thousands)		
December 31, 2002		
Pro forma—Balance Sheet data		
Asset retirement obligation		\$ 109,738

Effective January 1, 2002, TDS adopted SFAS No. 142 and determined that wireless licenses have indefinite lives. Upon initial adoption, TDS reviewed its investments in licenses and determined there was an impairment loss on certain licenses. The cumulative effect of the initial impairment upon the adoption of SFAS No. 142 reduced net income in 2002 by \$10.4 million, net of income taxes of \$8.2 million and minority interest of \$2.3 million, or \$0.18 per diluted share.

Effective January 1, 2002, U.S. Cellular changed its method of accounting for commission expenses related to customer activations and began deferring expense recognition of a portion of commission expenses in the amount of deferred activation fee revenues. TDS believes this change is a preferable method of accounting for such costs primarily due to the fact that the new method of accounting provides for better matching of revenue from customer activations to direct incremental costs associated with these activations within each reporting period. The cumulative effect of this accounting change on periods prior to 2002 was recorded in 2002 increasing net income by \$3.4 million, net of income taxes of \$3.0 million and minority interest of \$1.2 million, or \$0.06 per diluted share.

#### Advertising Costs

TDS expenses advertising costs as incurred. Advertising expense totaled \$171.4 million, \$140.9 million and \$105.3 million in 2004, 2003 and 2002, respectively.

#### Income Taxes

TDS files a consolidated federal income tax return. Deferred taxes are computed using the liability method, whereby deferred tax assets are recognized for deductible temporary differences and operating loss carryforwards, and deferred tax liabilities are recognized for taxable temporary differences. Both deferred tax assets and liabilities are measured using the tax rates anticipated to be in effect when the temporary differences reverse. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax basis. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. Deferred tax assets are reduced by a valuation allowance when it is more likely than not that some portion or all of the deferred tax assets will not be realized.

#### Stock-Based Compensation

TDS accounts for stock options and employee stock purchase plans under Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," as allowed by SFAS No. 123, "Accounting for Stock-Based Compensation," using the intrinsic value method.

No compensation costs were recognized for the stock option and employee stock purchase plans in 2004 and 2002. In 2003, TDS recorded compensation expense of \$0.3 million on 53,000 options granted in 2003. No compensation costs were recognized for the remaining 615,000 options granted in 2003. Had compensation cost for all stock option and employee stock purchase plans been determined consistent with SFAS No. 123, TDS's net income available to common and earnings per share would have been reduced to the following pro forma amounts:

Year Ended December 31,	2004	2003	2002
(Dollars in thousands, except per share amounts)			
Net Income (Loss)			
Available to Common			
As reported	\$48,801	\$ 46,191	\$ (995,199)
Pro forma expense	(20,555)	(14,886)	(11,503)
Pro forma	28,246	31,305	(1,006,702)
Basic Earnings per Share from			
Net income (loss) available to common			
As reported	0.85	0.80	(16.97)
Pro forma expense	(0.36)	(0.26)	(0.20)
Pro forma	0.49	0.54	(17.17)
Diluted Earnings per Share from			
Net income (loss) available to common			
As reported	0.84	0.79	(16.97)
Pro forma expense	(0.36)	(0.26)	(0.20)
Pro Forma	\$ 0.48	\$ 0.53	\$ (17.17)

### Operating Leases

TDS, U.S. Cellular and TDS Telecom are parties to various lease agreements for office space, retail sites, cell sites and equipment that are accounted for as operating leases. Certain leases have renewal options and/or fixed rental increases. Renewal options that are reasonably assured are included in determining the lease term.

During 2004, TDS revised its accounting for certain operating leases that contain fixed rental increases to recognize lease revenue and expense on a straight-line basis over the lease term in accordance with SFAS No. 13, as amended, and related pronouncements. Pursuant to its revised accounting for such leases, TDS recorded out-of-period adjustments to operating revenues and operating expenses during 2004. The adjustments were not considered material to the current year or to any prior years' earnings, earnings trends or individual financial statement line items. The adjustments were recorded in 2004, and no prior periods were adjusted. The impact of the out-of-period adjustments on the affected line items in the Statement of Operations for the year ended December 31, 2004 is as follows:

Year Ended December 31, 2004	TDS Telecom			
(Dollars in thousands, except earnings per share)	U.S. Cellular	ILEC	CLEC	All Other
Increase (decrease)				
Operating revenues	\$ 821	\$ 69	\$ —	\$ —
Cost of services and products	2,334	50	—	—
Selling, general and administrative expense	1,606	223	454	—
Total operating expenses	3,940	273	454	—
Operating income	(3,119)	(204)	(454)	—
Other income (expense) net				(1,589)
Income before income taxes and minority interest				(5,366)
Net income				\$(2,880)
Basic earnings per share				\$ (0.05)
Diluted earnings per share				\$ (0.05)

### Recent Accounting Pronouncements

#### Share-Based Payment

SFAS No. 123 (revised 2004), "Share-Based Payment," was issued in December 2004 and becomes effective for TDS in the third quarter of 2005. The statement requires that compensation cost resulting from all share-based payment transactions be recognized in the financial statements. TDS has reviewed the provisions of this statement and expects to record compensation expense for certain share-based payment transactions, primarily related to stock options, in the Statement of Operations upon adoption of this standard. See the "Stock-Based Compensation" disclosure above for a pro forma impact on net income and earnings per share.

## 2 INCOME TAXES

Income tax provisions charged to income (loss) from continuing operations before minority interest, discontinued operations and cumulative effect of accounting changes are summarized as follows:

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Current			
Federal	\$ 290	\$ 8,881	\$ 1,273
State	16,056	20,243	2,365
Foreign	—	—	7,068
Deferred			
Federal	51,409	29,844	(491,616)
State	10,896	(8,618)	(96,090)
Total income tax expense (benefit) from continuing operations	\$78,651	\$50,350	\$(577,000)

A reconciliation of TDS's income tax expense (benefit) from continuing operations computed at the statutory rate to the reported income tax expense (benefit) from continuing operations, and the statutory federal income tax expense (benefit) rate to TDS's effective income tax expense (benefit) rate from continuing operations, is as follows:

Year Ended December 31,	2004		2003		2002	
	Amount	Rate	Amount	Rate	Amount	Rate
(Dollars in millions)						
Statutory federal income tax expense (benefit)	\$52.3	35.0%	\$45.8	35.0%	\$(544.5)	(35.0)%
State income taxes, net of federal benefit	17.4	11.6	1.9	1.5	(57.2)	(3.7)
Minority share of income not included in consolidated tax return	(0.4)	(0.2)	(4.3)	(3.3)	(4.3)	(0.3)
Gains (losses) on investments and assets held for sale	22.7	15.2	3.9	3.0	12.6	0.8
Resolution of prior period tax issues	(10.0)	(6.7)	1.8	1.4	11.5	0.7
Foreign tax	—	—	—	—	4.6	0.3
Net research tax credit	(6.0)	(4.0)	—	—	—	—
Other differences, net	2.7	1.8	1.3	0.9	0.3	0.1
Total income tax expense (benefit)	\$78.7	52.7%	\$50.4	38.5%	\$(577.0)	(37.1)%

Income from continuing operations for each of the three years ended December 31, 2004, includes gains and losses (reported in the captions gain (loss) on investments and (gain) loss on assets held for sale, loss on impairment of intangible assets and loss on impairment of long-lived assets in the Statement of Operations) that significantly affected income (loss) from continuing operations before income taxes and minority interest. The effective income tax rate excluding such gains and losses was 32.7%, 38.6%, and 43.1% for the years ended December 31, 2004, 2003, and 2002, respectively.

The 2004 effective tax rate on operations excluding losses and gains is lower than 2003 due to favorable settlements of several tax issues in 2004. During 2004, the Internal Revenue Service ("IRS") substantially completed its audit of TDS's federal income tax returns for the years 1997 through 2001 and TDS's claims for research tax credits for the years 1995 through 2001. Primarily based on the results of the audit, TDS reduced its accrual for audit contingencies by \$10.0 million (6.7%) in 2004. Also in 2004, based upon the results of the federal income tax audit, TDS recorded a \$6.0 million (4.0%) benefit for the research tax credits.

Income tax provisions charged to net income (loss) are summarized as follows:

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Current			
Federal	\$ 290	\$ 8,861	\$ 1,273
State	16,056	20,029	2,365
Foreign	—	—	7,068
Deferred			
Federal	54,897	21,035	(495,999)
State	11,084	(10,436)	(97,021)
Total income tax expense (benefit)	\$82,327	\$ 39,489	\$(582,314)

Included in income tax expense charged to net income (loss) were deferred income tax benefits on cumulative effect of accounting change of \$9.7 million in 2003 and \$5.3 million in 2002.

Income from discontinued operations was decreased by deferred income tax expense of \$3.7 million in 2004 and loss from discontinued operations was decreased by an income tax benefit of \$1.2 million in 2003.

TDS's current net deferred tax assets totaled \$36.0 million and \$19.4 million as of December 31, 2004 and 2003, respectively. The net current deferred tax asset primarily represents the deferred tax effects of federal net operating loss ("NOL") carryforwards expected to be utilized in 2005 and the allowance for doubtful accounts on customer receivables.

The temporary differences that gave rise to the noncurrent deferred tax assets and liabilities are as follows:

December 31,	2004	2003
(Dollars in thousands)		
Deferred Tax Asset		
Net operating loss carryforwards	\$ 91,767	\$ 82,054
Derivative instruments	481,687	286,247
Other	9,699	—
	583,153	368,301
Less valuation allowance	(85,328)	(67,209)
Total Deferred Tax Asset	497,825	301,092
Deferred Tax Liability		
Marketable equity securities	1,271,637	1,044,230
Property, plant and equipment	362,735	312,232
Partnership investments	107,048	24,627
Licenses	223,054	203,989
Other	—	1,038
Total Deferred Tax Liability	1,964,474	1,586,116
Net Deferred Income Tax Liability	\$1,466,649	\$1,285,024

At December 31, 2004, TDS and certain subsidiaries had \$1,102 million of state NOL carryforwards (generating a \$85.9 million deferred tax asset) available to offset future taxable income primarily of the individual subsidiaries that generated the losses. The state NOL carryforwards expire between 2005 and 2024. Certain subsidiaries that are not included in the federal consolidated income tax return,



but file separate federal tax returns, had federal NOL carryforwards (generating a \$5.9 million deferred tax asset) available to offset future taxable income. The federal NOL carryforwards expire between 2005 and 2024. A valuation allowance was established for a portion of the state NOL carryforwards and the federal NOL carryforwards since it is more than likely that a portion of such carryforwards will expire before they can be utilized.

TDS is routinely subject to examination of its income tax returns by the IRS and other tax authorities. TDS periodically assesses the likelihood of adjustments to its tax liabilities resulting from these examinations to determine the adequacy of its provision for income taxes, including related interest. TDS's management judgment is required in assessing the eventual outcome of these examinations. Changes to such assessments affect the calculation of TDS's income tax expense. As a result of the substantial completion of federal and state tax audits, TDS has reclassified \$38 million from other deferred liabilities and credits to accrued taxes in the current liabilities section of the Balance Sheet.

### 3 EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income (loss) available to common by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using net income available to common and weighted average 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 the potential conversion of preferred stock to common shares.

The amounts used in computing earnings per share from continuing operations and the effect on income and the weighted average number of Common and Series A Common Shares of dilutive potential common stock are as follows:

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Basic Earnings per Share			
Income (loss) from continuing operations	\$42,642	\$ 60,006	\$(987,737)
Preferred dividend requirement	(203)	(417)	(427)
Income (loss) from continuing operations available to common	42,439	59,589	(988,164)
Discontinued operations	6,362	(1,609)	—
Cumulative effect of accounting change	—	(11,789)	(7,035)
Net income (loss) available to common used in basic earnings per share	\$48,801	\$ 46,191	\$(995,199)

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Diluted Earnings per Share			
Income (loss) from continuing operations available to common used in basic earnings per share	\$42,439	\$ 59,589	\$(988,164)
Minority income adjustment <sup>(1)</sup>	(504)	(335)	—
Income (loss) from continuing operations available to common	41,935	59,254	(988,164)
Discontinued operations	6,362	(1,609)	—
Cumulative effect of accounting change	—	(11,789)	(7,035)
Net income (loss) available to common used in diluted earnings per share	\$48,297	\$ 45,856	\$(995,199)

(1) The minority income adjustment reflects the additional minority share of U.S. Cellular's income computed as if all of U.S. Cellular's dilutive issuable securities were outstanding.

Year Ended December 31,	2004	2003	2002
(Shares in thousands)			
Weighted average number of Common Shares used in basic earnings per share			
	57,296	57,721	58,644
Effect of dilutive securities			
Common Shares outstanding if Preferred Shares converted <sup>(1)</sup>	—	—	—
Stock options <sup>(2)</sup>	271	154	—
Weighted average number of Common Shares used in diluted earnings per share	57,567	57,875	58,644

(1) Preferred Shares convertible into 75,373 Common Shares in 2004, 210,269 Common Shares in 2003 and 231,013 Common Shares in 2002 were not included in computing diluted earnings per share because their effects were anti-dilutive.

(2) Stock options convertible into 682,122 Common Shares in 2004, 1,277,834 Common Shares in 2003 and 1,792,639 Common Shares in 2002 were not included in computing diluted earnings per share because their effects were anti-dilutive.

Year Ended December 31,	2004	2003	2002
Basic Earnings per Share			
Continuing operations	\$0.74	\$ 1.03	\$(16.85)
Discontinued operations	0.11	(0.03)	—
Cumulative effect of accounting change	—	(0.20)	(0.12)
	\$0.85	\$ 0.80	\$(16.97)
Diluted Earnings per Share			
Continuing operations	\$0.73	\$ 1.02	\$(16.85)
Discontinued operations	0.11	(0.03)	—
Cumulative effect of accounting change	—	(0.20)	(0.12)
	\$0.84	\$ 0.79	\$(16.97)

**4 MARKETABLE EQUITY SECURITIES**

Information regarding TDS's marketable equity securities is summarized as follows:

December 31,	2004	2003
(Dollars in thousands)		
Deutsche Telekom AG		
131,461,861 ordinary shares	\$2,960,521	\$2,403,123
Vodafone Group Plc		
12,945,915 American Depositary Receipts	354,459	324,166
VeriSign, Inc.		
2,361,333 common shares	79,341	38,490
Rural Cellular Corporation		
719,396 equivalent common shares	4,482	5,719
Other	1	912
Aggregate fair value	3,398,804	2,772,410
Accounting cost basis	1,543,677	1,543,932
Gross unrealized holding gains	1,855,127	1,228,478
Equity method unrealized gains	261	126
Income tax expense	(724,257)	(479,683)
Minority share of unrealized holding (gains)	(13,385)	(10,801)
Unrealized gains on marketable equity securities, net of tax and minority share	1,117,746	738,120
Derivatives, net of tax and minority share	(744,241)	(441,300)
Accumulated other comprehensive income	\$ 373,505	\$ 296,820

TDS and its subsidiaries hold a substantial amount of marketable equity securities that are publicly traded and can have volatile movements in share prices. TDS and its subsidiaries do not make direct investments in publicly traded companies and all of these interests were acquired as a result of sales, trades or reorganizations of other assets.

The investment in Deutsche Telekom AG ("Deutsche Telekom") resulted from TDS's disposition of its over 80%-owned personal communication services operating subsidiary, Aerial Communications, Inc., to VoiceStream Wireless Corporation ("VoiceStream") in exchange for stock of VoiceStream, which was then acquired by Deutsche Telekom in exchange for Deutsche Telekom stock. The investment in Vodafone Group Plc ("Vodafone") resulted from certain dispositions of non-strategic wireless investments to or settlements with AirTouch Communications Inc. ("AirTouch"), in exchange for stock of AirTouch, which was then acquired by Vodafone whereby TDS and its subsidiaries received American Depositary Receipts representing Vodafone stock. The investment in VeriSign, Inc. ("VeriSign") is the result of the acquisition by VeriSign of Illuminet, Inc., a telecommunication entity in which several TDS subsidiaries held interests. The investment in Rural Cellular Corporation ("Rural Cellular") is the result of a consolidation of several wireless partnerships in which TDS subsidiaries held interests in Rural Cellular, and the distribution of Rural Cellular stock in exchange for these interests.

The market values of the marketable equity securities may fall below the accounting cost basis of such securities. If TDS determines the decline in value of the marketable equity securities to

be other than temporary, the unrealized loss included in accumulated other comprehensive income is recognized and recorded as a loss in the Statement of Operations.

TDS and its subsidiaries have entered into a number of forward contracts related to the marketable equity securities that they hold. The risk management objective of the forward contracts is to hedge the value of the marketable equity securities from losses due to decreases in the market prices of the securities while retaining a share of gains from increases in the market prices of such securities. The downside risk is hedged at or above the accounting cost basis thereby eliminating the risk of an other-than-temporary loss on these contracted securities.

**5 LICENSES AND GOODWILL**

Changes in licenses and goodwill are primarily the result of impairments and acquisitions and divestitures of wireless markets and telephone companies by TDS. See Note 12 – Acquisitions, Divestitures and Exchanges for the details on the changes in licenses and goodwill.

In conjunction with the implementation of SFAS No. 142, "Goodwill and Other Intangible Assets" on January 1, 2002, TDS recorded an impairment loss of \$20.9 million, before income tax benefits of \$8.2 million and minority interest of \$2.3 million as a cumulative effect of an accounting change on licenses for the excess carrying value of the licenses over the fair value. In 2003, TDS recorded an additional impairment loss of \$49.6 million on licenses in two reporting units and a \$3.5 million loss on impairment of its investment in a non-operating license. An additional \$1.8 million impairment loss was recorded in 2004 on the Daytona Beach, Florida license, which was sold in December 2004. See Note 1 – Summary of Significant Accounting Policies under the heading "Impairment of Intangible Assets" for a detailed discussion of the license impairment test.

A schedule of license activity follows:

December 31,	2004	2003
(Dollars in thousands)		
Balance, beginning of year	\$1,231,363	\$1,247,197
Acquisitions <sup>(1)</sup>	5,629	178,609
Divestitures	(8,426)	(76,905)
Allocation to assets of operations held for sale	—	(63,569)
Impairment loss	(1,830)	(53,095)
Other	2,065	(874)
Balance, end of year <sup>(1)</sup>	\$1,228,801	\$1,231,363

(1) Includes \$42.0 million of license rights from the AT&T Wireless transactions in 2003.

In response to petitions filed by the Regional Bell Operating Company for increases in rates for certain wholesale services that it provides to competitive local exchange carriers, the state public service commissions of Illinois, Wisconsin and Michigan have issued orders that will adversely affect the cost of providing some services for TDS Telecom's competitive local exchange carrier operations in those states, primarily services to residential customers

and certain small business customers. The pricing data for the major markets of TDS Telecom's competitive local exchange carrier became available in the fourth quarter of 2004. These pricing changes, as well as other regulatory changes and competitive pressures in 2004, triggered an impairment review by TDS Telecom of its competitive local exchange carrier operations' tangible and intangible assets. As a result of the impairment review, TDS Telecom concluded that goodwill associated with the competitive local exchange carrier operations was impaired and recorded a loss on impairment of intangible assets of \$29.4 million in the Statement of Operations.

TDS Telecom's carrying value for the competitive local exchange carrier operations exceeded the fair value of such operations, thus requiring the second step of the goodwill test. Pursuant to the second step of the goodwill test, TDS Telecom allocated the fair value of the competitive local exchange carrier operations to all of the assets, including unrecognized intangible assets, (e.g., the value of the customer list and trade names) and liabilities of such operations. As a result of this allocation, there was no implied goodwill. Therefore, the carrying amount of goodwill was charged to expense. See Note 1 – Summary of Significant Accounting Policies under the heading "Impairment of Intangible Assets" for a detailed discussion of the goodwill impairment test.

In 2003, TDS recorded a goodwill impairment loss of \$5.0 million, included in gain (loss) on investments in the Statement of Operations on a wireless market investment held by TDS Telecom.

A schedule of goodwill activity follows:

December 31,	2004	2003
(Dollars in thousands)		
Consolidated Beginning Balance	<b>\$887,937</b>	\$967,566
U.S. Cellular		
Balance, beginning of year	<b>430,256</b>	504,744
Acquisitions	<b>4,225</b>	7,516
Divestitures	<b>(8,257)</b>	(69,961)
Allocation to assets of operations held for sale	—	(7,565)
Other	<b>(306)</b>	(4,478)
Balance, end of year	<b>425,918</b>	430,256
TDS Telecom–ILEC		
Balance, beginning of year	<b>397,341</b>	397,482
Other	—	(141)
Balance, end of year	<b>397,341</b>	397,341
TDS Telecom–CLEC		
Balance, beginning of year	<b>29,440</b>	29,440
Impairment loss	<b>(29,440)</b>	—
Balance, end of year	—	29,440
Other		
Balance, beginning of year	<b>30,900</b>	35,900
Divestitures	<b>(30,900)</b>	—
Impairment loss	—	(5,000)
Balance, end of year	—	30,900
Net Change	<b>(64,678)</b>	(79,629)
Consolidated Ending Balance	<b>\$823,259</b>	\$887,937

## 6 CUSTOMER LISTS

Customer lists, intangible assets from the acquisition of wireless properties, are being amortized based on average customer retention periods using the declining balance method. The acquisition of certain minority interests in 2004 added \$12.9 million to the gross balance of customer lists. Amortization expense was \$12.4 million, \$15.6 million and \$6.6 million for the years ended December 31, 2004, 2003 and 2002, respectively. Amortization expense related to customer list assets recorded as of December 31, 2004 for the years 2005 through 2009 is expected to be \$8.2 million, \$5.4 million, \$3.6 million, \$2.4 million and \$1.6 million, respectively.

## 7 INVESTMENTS IN UNCONSOLIDATED ENTITIES

Investments in unconsolidated entities consist of amounts invested in wireless and wireline entities in which TDS holds a minority interest. These investments are accounted for using either the equity or cost method, as shown in the following table:

December 31,	2004	2003
(Dollars in thousands)		
Equity method investments:		
Capital contributions, loans and advances	<b>\$ 26,593</b>	\$ 38,005
Goodwill	<b>18,594</b>	23,821
Cumulative share of income	<b>411,335</b>	391,008
Cumulative share of distributions	<b>(262,223)</b>	(252,492)
	<b>194,299</b>	200,342
Cost method investments:		
Capital contributions, net of partnership contributions and impairments	<b>3,920</b>	5,565
Goodwill	<b>8,544</b>	8,978
	<b>12,464</b>	14,543
Total investments in unconsolidated entities	<b>\$ 206,763</b>	\$ 214,885

TDS follows the equity method of accounting for minority interests where TDS's ownership interest is 20% or greater for corporations or greater than 3% to 5% for partnerships and limited liability companies. This method recognizes, on a current basis, TDS's proportionate share of the income and losses accruing to it under the terms of the respective partnership and shareholder agreements. Income and losses from the entities are reflected in the Statement of Operations on a pretax basis as investment income. Investment income totaled \$69.6 million, \$53.2 million and \$43.7 million in 2004, 2003 and 2002, respectively. TDS follows the cost method of accounting for its investments where TDS's ownership interest is less than 20% for corporations or 3% to 5% for partnerships and limited liability companies, or where TDS does not have the ability to exercise significant influence.

Investments in unconsolidated entities include goodwill and costs in excess of the underlying book value of certain investments. At December 31, 2004, \$179.7 million represented the investment in underlying equity and \$27.1 million represented goodwill. At December 31, 2003, \$182.1 million represented the investment in underlying equity and \$32.8 million represented goodwill.

With the adoption of FIN 46R in January 2004, one wireless market that was included in investment in unconsolidated entities as of the end of 2003 was included in consolidated operations. This market was subsequently sold to ALLTEL on November 30, 2004 along with other wireless properties. In the ALLTEL transaction, TDS sold six minority interests that had been included in investment in unconsolidated entities. The transaction reduced goodwill \$5.5 million and the investment in underlying equity by \$17.3 million. See Note 12 – Acquisitions, Divestitures and Exchanges for more information related to this transaction.

Also during 2004, TDS reduced the carrying value of one of its cost method investments by \$0.5 million. The change was included in gain (loss) on investment on the Statement of Operations.

During 2003, TDS reduced the carrying value of one of its cost method investments by \$1.7 million. This charge was included in gain (loss) on investments on the Statement of Operations.

Los Angeles SMSA Limited Partnership meets certain tests, pursuant to Rule 3-09 of SEC Regulation S-X, contributing \$43.4 million, \$30.2 million and \$19.7 million in investment income in 2004, 2003 and 2002, respectively. TDS's more significant investments in unconsolidated entities consist of the following:

December 31,	Percentage Ownership	
	2004	2003
Los Angeles SMSA Limited Partnership	5.5%	5.5%
Raleigh-Durham MSA Limited Partnership <sup>(1)</sup>	—	8.0%
Midwest Wireless Communications, LLC	15.2%	15.2%
North Carolina RSA 1 Partnership	50.0%	50.0%
Oklahoma City SMSA Limited Partnership	14.6%	14.6%

(1) As a result of the agreement with ALLTEL, as described more fully in Note 12 – Acquisitions, Divestitures and Exchanges, TDS's investment in this partnership was sold to ALLTEL on November 30, 2004.

Based primarily on data furnished to TDS by third parties, the following summarizes the combined assets, liabilities and equity, and the combined results of operations of the entities for which TDS's investments are accounted for by the equity method.

December 31,	2004	2003
(Dollars in thousands)		
Assets		
Current	\$ 290,000	\$ 252,000
Due from affiliates	591,000	522,000
Property and other	1,676,000	1,674,000
	<b>\$2,557,000</b>	<b>\$2,448,000</b>
Liabilities and Equity		
Current liabilities	\$ 207,000	\$ 185,000
Deferred credits	5,000	86,000
Long-term debt	97,000	33,000
Long-term capital lease obligations	23,000	—
Partners' capital and stockholders' equity	2,225,000	2,144,000
	<b>\$2,557,000</b>	<b>\$2,448,000</b>

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Results of Operations			
Revenues	\$3,035,000	\$2,509,000	\$2,184,000
Costs and expenses	2,113,000	1,854,000	1,699,000
Operating income	922,000	655,000	485,000
Other income (expense)	28,000	5,000	14,000
Net income	<b>\$ 950,000</b>	<b>\$ 660,000</b>	<b>\$ 499,000</b>

## 8 NOTES RECEIVABLE

Included in notes receivable is a loan of \$55.1 million to Airadigm Communications, Inc. ("Airadigm"), related to the funding of Airadigm's operations. The value of the note was directly related to the values of certain assets and contractual rights of Airadigm. As a result of changes in business strategies and other events, in 2002, management reviewed the Airadigm business plan and reviewed the fair market value of the wireless markets and concluded that the notes receivable were impaired. TDS recorded valuation allowances against the Airadigm notes receivable, reducing the carrying value by \$55.1 million to zero, and charged \$1.1 million of capitalized cost to expense.

## 9 PROPERTY, PLANT AND EQUIPMENT

U.S. Cellular's property, plant and equipment consists of the following:

December 31,	2004	2003
(Dollars in thousands)		
Cell site-related equipment	\$2,003,842	\$1,777,251
Land, buildings and leasehold improvements	782,262	621,070
Switching-related equipment	617,650	460,165
Office furniture and equipment	225,180	203,139
Systems development	220,472	212,043
Other operating equipment	153,940	127,542
Work in process	127,206	252,010
	<b>4,130,552</b>	<b>3,653,220</b>
Accumulated depreciation	1,690,833	1,381,966
	<b>\$2,439,719</b>	<b>\$2,271,254</b>

During 2004, U.S. Cellular adjusted the useful lives of Time Division Multiple Access ("TDMA") radio equipment, switch software and antenna equipment. TDMA radio equipment lives were adjusted to be fully depreciated by the end of 2008, which is the latest date the wireless industry will be required by law to support analog service. U.S. Cellular currently uses TDMA radio equipment to support analog service, and expects to have its digital radio network fully migrated to Code Division Multiple Access ("CDMA") 1XRTT or some future generation of CDMA technology by that time. The useful lives for certain switch software were reduced to one year from three years and antenna equipment lives were reduced from eight years to seven years in order to better align the useful lives with the actual length of time the assets are expected to be in use. These changes increased depreciation by \$14.9 million in 2004. The changes in useful lives reduced net income by \$7.4 million, or \$0.13 per share in 2004.



In 2004, certain U.S. Cellular TDMA digital radio equipment consigned to a third party for future sale was taken out of service and was written down by \$17.2 million prior to its consignment, increasing depreciation expense by that amount. This writedown was necessary to reduce the book value of the assets sold or to be sold to the proceeds received or expected to be received from their disposition.

In preparation for the implementation of a fixed asset management and tracking software system, including a bar code asset identification system, U.S. Cellular conducted a physical inventory review of its cell site fixed assets in 2004. As a result of the review, U.S. Cellular charged \$11.9 million to depreciation expense for the write-off of certain assets in 2004.

Useful lives generally range from six to twenty-five years for cell site-related equipment; twenty years for buildings; three to ten years, which approximates the shorter of the assets' economic lives or the specific lease terms, for leasehold improvements; one to eight years for switching-related equipment; three to five years for office furniture and equipment; three to seven years for systems development; and five to twenty-five years for other operating equipment. Depreciation expense totaled \$450.0 million, \$374.8 million and \$312.0 million in 2004, 2003 and 2002, respectively. Amortization expense on system development costs totaled \$30.3 million, \$34.0 million and \$28.8 million in 2004, 2003 and 2002, respectively.

TDS Telecom's property, plant and equipment consists of the following:

December 31,	2004	2003
(Dollars in thousands)		
<b>Incumbent Local Exchange Operations</b>		
Cable and wire	\$1,057,387	\$1,052,964
Central office equipment	625,111	606,894
Office furniture and equipment	111,825	109,844
Systems development	125,244	110,359
Land and buildings	82,738	82,799
Other equipment	65,928	64,502
Work in process	20,905	37,344
	<b>2,089,138</b>	<b>2,064,706</b>
Accumulated depreciation	<b>1,242,160</b>	<b>1,173,429</b>
	<b>846,978</b>	<b>891,277</b>
<b>Competitive Local Exchange Operations</b>		
Cable and wire	55,080	74,082
Central office equipment	138,405	165,849
Office furniture and equipment	23,565	37,126
Systems development	11,446	11,296
Land and buildings	382	475
Other equipment	5,084	5,107
Work in process	4,709	3,458
	<b>238,671</b>	<b>297,393</b>
Accumulated depreciation	<b>139,887</b>	<b>108,938</b>
	<b>98,784</b>	<b>188,455</b>
<b>Total</b>	<b>\$ 945,762</b>	<b>\$1,079,732</b>

Useful lives of incumbent local exchange property generally range from fifteen to twenty years for cable and wire, five to twelve years for central office equipment, five to ten years for office furniture and equipment, five to seven years for systems development and ten to fifteen years for other equipment. Buildings are depreciated over thirty years. The provision for depreciation as a percentage of depreciable property was 6.6% in 2004, 6.6% in 2003 and 6.2% in 2002. Depreciation expense totaled \$129.7 million, \$127.7 million and \$128.0 million in 2004, 2003 and 2002, respectively.

Useful lives of competitive local exchange property generally range from fifteen to twenty years for cable and wire, eight to twelve years for central office equipment, five to ten years for office furniture and equipment, five to seven years for systems development and ten to fifteen years for other equipment. Buildings are depreciated over thirty years. The provision for depreciation as a percentage of depreciable property was 12.0% in 2004, 9.0% in 2003 and 12.7% in 2002. Depreciation expense totaled \$33.9 million, \$31.2 million and \$28.9 million in 2004, 2003 and 2002, respectively.

As discussed in Note 5 – Licenses and Goodwill, regulatory changes and competitive pressures in 2004 triggered an impairment review by TDS Telecom of its competitive local exchange carrier operations' tangible assets. As a result of the impairment review, TDS Telecom concluded that the long-lived tangible assets of its competitive local exchange carrier operations were impaired and recorded a loss on impairment of tangible assets of \$87.9 million in the Statement of Operations.

TDS reviewed the long-lived assets for possible impairment based on an estimate of related undiscounted cash flows over the remaining asset lives. TDS concluded that the undiscounted cash flows attributable to the fixed assets were less than the carrying values of the fixed assets, thus requiring the second step of the long-lived asset impairment test. Pursuant to the second step of the long-lived asset impairment test, TDS Telecom calculated the fair value of the fixed assets. The loss recognized is the difference between the fair value and the carrying value of the fixed assets. See Note 1 – Summary of Significant Accounting Policies under the heading "Impairment of Tangible Assets" for a detailed discussion of the long-lived asset impairment test.

TDS recorded a write-down of plant assets totaling \$0.4 million in the incumbent local exchange operations and a write-down of \$4.6 million in the competitive local exchange operations in 2003, of which \$3.3 million related to plant assets.

#### 10 OPERATIONS HELD FOR SALE

There were no operations held for sale as of December 31, 2004.

On November 26, 2003, U.S. Cellular announced that it had entered into a definitive agreement to sell its southern Texas wireless markets to AT&T Wireless Services, Inc. ("AT&T Wireless"), now a subsidiary of Cingular Wireless LLC, for \$96.5 million in cash. The U.S. Cellular markets sold to AT&T Wireless included 25 MHz metropolitan statistical area and rural service area licenses representing 1.3 million population equivalents, approximately 150 cell sites and 76,000 customers. The closing of the sale occurred on February 18, 2004.

The sale was accounted for in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." The Balance Sheet as of December 31, 2003 reflected assets and liabilities of the wireless properties to be sold as assets and liabilities of operations held for sale. The revenues and expenses of the markets were included in operations until the completion of the sale.

The following table summarizes the recorded value of the assets and liabilities of operations held for sale as of December 31, 2003:

Year Ended December 31,	2003
(Dollars in thousands)	
Current assets	\$ 5,363
Property, plant and equipment, net	45,710
Licenses	63,569
Goodwill	7,565
Other assets	316
Loss on assets held for sale	(22,000)
Assets of operations held for sale	<u>\$100,523</u>
Current liabilities	\$ 2,189
Non-current liabilities	238
Liabilities of operations held for sale	<u>\$ 2,427</u>

In 2003, U.S. Cellular recorded a loss of \$22.0 million as a loss on assets held for sale (included in operating expenses) representing the difference between the carrying value of the markets to be sold to AT&T Wireless and the cash received in the transaction. In 2004, this amount was reduced by \$0.7 million to finalize the loss upon closing of the transaction, for an aggregate loss of \$21.3 million.

## 11 SUPPLEMENTAL CASH FLOW DISCLOSURES

Following are supplemental cash flow disclosures for interest and income taxes paid and certain noncash transactions.

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Interest paid	\$176,912	\$143,159	\$112,062
Income taxes paid			
(refund received)	(10,512)	(53,112)	77,443
Common Shares issued for			
conversion of Preferred Shares	—	2,940	122
Notes issued for			
the Chicago acquisition	\$ —	\$ —	\$175,000

## 12 ACQUISITIONS, DIVESTITURES AND EXCHANGES

TDS assesses its holdings on an ongoing basis in order to maximize the benefits derived from its operations. TDS also reviews attractive opportunities to acquire additional telecommunications companies and wireless spectrum that it believes will add value to the business.

### 2004 Activity

On December 20, 2004, U.S. Cellular completed the sale of its Daytona Beach Florida 20 megahertz C block personal communications service license to MetroPCS California/Florida Inc. ("MetroPCS") for \$8.5 million. TDS recorded impairment losses of \$1.8 million in 2004 and \$3.5 million in 2003 in gain (loss) on

investments included within investment and other income (expense) on the Statement of Operations related to the Daytona license. Also included in gain (loss) on investments in 2004 was a loss of \$0.3 million associated with buying out the former partner of the Daytona investment.

On November 30, 2004, TDS and U.S. Cellular completed the sale to ALLTEL of certain wireless properties. TDS and U.S. Cellular subsidiaries sold three consolidated properties and six minority interests to ALLTEL for \$142.9 million in cash, including repayment of debt and working capital that is subject to adjustment. TDS recorded a pre-tax gain of \$49.6 million related to the ALLTEL transaction representing the excess of the cash received over the net book value of the assets and liabilities sold. The portion of the gain related to the two consolidated markets included in operations of \$10.1 million, was recorded in (gain) loss on assets held for sale in the Statement of Operations. The remaining portion of the gains of \$39.5 million was recorded in gain (loss) on investments included within investment and other income (expense) of the Statement of Operations. TDS has included the results of operations of the markets sold to ALLTEL in the Statement of Operations through November 30, 2004.

The following table summarizes the recorded value of the assets and liabilities transferred to ALLTEL.

November 30, 2004	
(Dollars in thousands)	
Current assets	\$ (11,897)
Property, plant and equipment	(33,223)
Licenses transferred	(258)
Goodwill	(39,157)
Investment in unconsolidated entities	(22,782)
Other assets and liabilities	647
Current liabilities	3,417
Minority interest divested	9,924
Gain recorded on transfer	(49,568)
Cash (received)	<u>\$(142,897)</u>

On February 18, 2004, U.S. Cellular completed the sale of certain of its wireless properties in southern Texas to AT&T Wireless for \$96.5 million in cash, including a working capital adjustment. The U.S. Cellular properties sold to AT&T Wireless included wireless assets and customers in six markets. An aggregate loss of \$21.3 million (including a \$22.0 million estimate of the loss on assets of operations held for sale in the fourth quarter of 2003 and a \$0.7 million reduction of the loss in 2004) was recorded as a (gain) loss on assets of operations held for sale (included in operating expenses), representing the difference between the carrying value of the markets sold to AT&T Wireless and the cash received in the transaction. On December 31, 2003, U.S. Cellular reflected the assets and liabilities to be transferred to AT&T Wireless as assets and liabilities held for sale in accordance with SFAS No. 144. U.S. Cellular has included the results of operations of the markets sold to AT&T Wireless in the Statement of Operations through February 17, 2004.

The following table summarizes the recorded value of the southern Texas assets and liabilities sold to AT&T Wireless.

February 18, 2004

(Dollars in thousands)

Current assets	\$ (4,342)
Property, plant and equipment	(46,592)
Wireless licenses transferred	(63,237)
Goodwill	(7,565)
Other assets and liabilities	1,483
Current liabilities	2,455
Loss recorded on transfer	21,275
Cash (received)	<u>\$(96,523)</u>

In addition, in 2004 U.S. Cellular purchased certain minority interests in several wireless markets in which it already owned a controlling interest for \$40.8 million in cash and \$2.0 million to be paid in 2005. These acquisitions increased licenses, goodwill and customer lists by \$5.6 million, \$4.2 million and \$12.9 million, respectively.

In aggregate, the 2004 acquisitions, divestitures and exchanges decreased licenses by \$2.8 million and goodwill by \$34.9 million. Licenses and goodwill associated with the southern Texas transaction with AT&T Wireless that closed in 2004 were included in assets of operations held for sale in 2003.

### 2003 Activity

During 2003, U.S. Cellular completed an exchange with AT&T Wireless along with the acquisition of two minority interests.

On August 1, 2003, U.S. Cellular completed the transfer of properties to AT&T Wireless and the assignments to it by AT&T Wireless of a portion of the licenses covered by the agreement with AT&T Wireless. On the initial closing date, U.S. Cellular also received approximately \$34.0 million in cash and minority interests in six markets in which it currently owns a controlling interest. Also on the initial closing date, U.S. Cellular transferred wireless assets and customers in 10 markets in Florida and Georgia to AT&T Wireless. The assignment and development of certain licenses has been deferred by U.S. Cellular for a period of up to five years from the closing date, in accordance with the agreement. U.S. Cellular will take possession of the licenses in staggered closings over that five-year period to comply with service requirements of the Federal Communications Commission. The acquisition of the licenses in the exchange was accounted for as a purchase by U.S. Cellular and the transfer of the properties by U.S. Cellular to AT&T Wireless was accounted for as a sale. TDS capitalized \$2.8 million of costs associated with the AT&T Wireless transaction.

The 15 licenses that have been transferred to U.S. Cellular as of December 31, 2003, with a recorded value of \$136.6 million, are included in licenses on the Balance Sheet. The 21 licenses that have not yet been assigned to U.S. Cellular, with a recorded value of \$42.0 million, are included in license rights on the Balance Sheet. TDS has included the results of operations in the Florida and Georgia markets in the Statement of Operations until the date of the transfer, August 1, 2003.

Prior to the close of the AT&T Wireless exchange, U.S. Cellular allocated \$70.0 million of goodwill related to the properties transferred to AT&T Wireless to assets of operations held for sale in accordance with SFAS No. 142. A loss of \$23.9 million was recorded as a loss on assets held for sale (included in operating expenses) representing the difference between the book value of the markets transferred to AT&T Wireless and the fair value of the assets received or to be received in this transaction.

The following table summarizes the estimated fair values of the AT&T Wireless licenses received and the recorded value of the Florida and Georgia assets and liabilities transferred to AT&T Wireless from U.S. Cellular.

August 1, 2003

(Dollars in thousands)

Current assets	\$ (12,785)
Property, plant and equipment	(88,314)
Licenses transferred	(76,905)
Licenses received	136,571
License rights	42,037
Goodwill	(69,961)
Minority interests acquired	3,000
Other assets and liabilities	(717)
Current liabilities	9,213
Loss recorded on transfer	23,908
Cash received	<u>\$ (33,953)</u>

In addition, in 2003, U.S. Cellular acquired the minority interest in two entities which held licenses for \$2.3 million.

In aggregate, the 2003 acquisitions, divestitures and exchanges increased licenses by \$59.7 million and license rights by \$42.0 million and reduced U.S. Cellular goodwill by \$62.4 million.

### 2002 Activity

On August 7, 2002, U.S. Cellular completed the acquisition of the assets and certain liabilities of Chicago 20 MHz, LLC, now known as United States Cellular Operating Company of Chicago, LLC ("USCOC of Chicago" or the "Chicago market") from PrimeCo Wireless Communications LLC ("PrimeCo"). USCOC of Chicago operates a wireless system in the Chicago major trading area. USCOC of Chicago is the holder of certain FCC licenses, including a 20 megahertz personal communications service license in the Chicago major trading area (excluding Kenosha County, Wisconsin) covering 13.2 million population equivalents.

U.S. Cellular financed the purchase price (\$617.8 million) using \$327.3 million of revolving lines of credit, \$175.0 million in 30-year notes issued to PrimeCo, a \$105.0 million loan from TDS and a \$10.5 million accrued payable. TDS has included the USCOC of Chicago results of operations in the Statement of Operations subsequent to the purchase date.

The tangible fixed assets were valued at net book value. The personal communications service licenses were valued at \$163.5 million. The customer list was assigned a value of \$43.4 million and is being amortized based on a 30-month average customer retention period using the declining balance method.

Total goodwill attributed to the Chicago market acquisition aggregated \$168.4 million. In January 2003, U.S. Cellular repurchased the \$45.2 million 9% Series A notes that remained outstanding at December 31, 2002, at 90% of face value. The \$4.5 million gain on retirement of the 9% Series A notes was credited to goodwill, reducing the aggregate goodwill attributed to the Chicago market acquisition to \$163.9 million. Such goodwill is deductible for tax purposes and will be amortized over 15 years.

The following table summarizes the estimated fair values of the PrimeCo assets acquired and liabilities assumed at the date of acquisition.

	August 7, 2002
(Dollars in thousands)	
Current assets, excluding \$6,984 cash acquired	\$ 34,081
Property, plant and equipment	235,953
Other assets	815
Customer list	43,400
Licenses	163,500
Goodwill	168,436
Total assets acquired	646,185
Current liabilities	(22,518)
Non-current liabilities	(1,300)
Total liabilities acquired	(23,818)
Net assets purchased	622,367
Notes issued to PrimeCo	(175,000)
Accrued but unpaid items	(15,500)
Cash required	\$ 431,867

In addition, TDS acquired two incumbent local telephone companies, three additional personal communications service licenses and additional minority interests in majority-owned markets during 2002. In conjunction with these acquisitions, the following assets were acquired and liabilities assumed. The goodwill acquired in these acquisitions is not deductible for tax purposes.

	2002
(Dollars in thousands)	
Current assets, excluding \$3,366 cash acquired	\$ 6,454
Property, plant and equipment	24,640
Licenses	18,010
Goodwill—U.S. Cellular	3,827
Goodwill—TDS Telecom	64,231
Other assets	2,068
Current liabilities	(5,450)
Long-term debt	(9,767)
Deferred credits	(3,080)
Other liabilities	(1,627)
Cash required	\$99,306

In aggregate, the 2002 acquisitions increased licenses by \$181.5 million, U.S. Cellular goodwill by \$172.3 million and TDS Telecom's incumbent local exchange carrier goodwill by \$64.2 million.

### Pro Forma Operations

Assuming the exchanges and acquisitions accounted for as purchases during the period January 1, 2003 to December 31, 2004, had taken place on January 1, 2003; and the acquisitions during the period January 1, 2002 to December 31, 2002, had taken place on January 1, 2002, unaudited pro forma results of operations would have been as follows:

Year Ended December 31,	2004	2003	2002
(Unaudited, dollars in thousands, except per share amounts)			
Operating revenues	\$3,694,744	\$3,302,878	\$ 3,124,563
Interest expense			
(including cost to finance acquisitions)	198,706	171,391	141,673
Income (loss) from continuing operations	31,376	53,585	(1,015,194)
Net income (loss)	37,738	40,188	(1,022,229)
Earnings per share—basic	0.66	0.69	(17.44)
Earnings per share—diluted	\$ 0.64	\$ 0.68	\$ (17.44)

### 13 GAIN (LOSS) ON INVESTMENTS

The following table summarizes the components of gain (loss) on investments included in investment and other income (expense) in the Statement of Operations:

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Gain on sale of investment interests	\$39,487	\$ —	\$ —
Impairment of unconsolidated interests	(2,633)	(10,200)	(32,716)
Marketable equity securities other-than-temporary losses	—	—	(1,757,471)
Notes receivable impairment	—	—	(93,978)
Other	—	—	(4,226)
	\$36,854	\$(10,200)	\$(1,888,391)

In 2004, TDS recorded a gain of \$39.5 million related to the ALLTEL transaction representing the excess of the cash received over the net book value of the minority investments sold.

TDS recorded impairment losses of \$1.8 million in 2004 and \$3.5 million in 2003 related to the Daytona license that was sold to MetroPCS in December 2004. Also included in gain (loss) on investments in 2004 was a \$0.3 million loss associated with buying out the former partner of the Daytona investment.

Also in 2004, TDS recorded a \$0.5 million impairment loss on an investment in a telephone company accounted for using the cost method.



In 2003, U.S. Cellular reduced the carrying value of one of its cost method investments by \$1.7 million to its underlying equity value based on a cash flow analysis.

TDS Telecom recorded an impairment loss of \$5.0 million in 2003 on a wireless market investment held by it in conjunction with its annual license and goodwill impairment testing.

In 2002, management determined that a decline in the value of marketable equity securities relative to their respective accounting cost basis was other than temporary and charged an aggregate \$1,757.5 million loss to the Statement of Operations and reduced the accounting cost basis of such marketable equity securities by a corresponding amount.

TDS had certain notes receivable from Airadigm and Kington Management Corporation ("Kington"). During 2002, management concluded that the notes receivable were impaired, and accordingly, recorded a \$54.8 million valuation allowance and an additional \$0.3 million expense included in other income (expense), net, to reduce the Airadigm note receivable carrying value to zero, charged \$1.1 million of capitalized costs to expense and reduced the Kington note receivable carrying value by \$38.1 million to net realizable value.

TDS recorded additional losses in 2002 of \$25.4 million related to the withdrawal from a partnership in which it had owned an investment interest, \$7.3 million to the write-down of a wireless investment to fair value and \$4.2 million to the reduction in value of a land purchase option.

#### 14 NOTES PAYABLE

TDS has used short-term debt to finance acquisitions, for general corporate purposes and to repurchase common shares. Proceeds from the sale of long-term debt from time to time have been used to reduce such short-term debt. Proceeds from the sale of non-strategic wireless and other investments from time to time have also been used to reduce short-term debt.

TDS had a \$600 million revolving credit facility with a group of banks at December 31, 2004, and had \$3.4 million of letters of credit outstanding against the revolving credit facility, leaving \$596.6 million available for use. On December 9, 2004, TDS entered into an agreement to amend the terms and conditions of this facility. The primary changes to the terms and conditions are that (i) the maturity date has been extended to December 2009 and (ii) the material adverse change condition has been removed with respect to drawdowns. Borrowings bear interest at the London InterBank Offered Rate ("LIBOR") plus a contractual spread based on TDS's credit rating. At December 31, 2004, the contractual spread was 30 basis points (the one-month LIBOR rate was 2.4% at December 31, 2004). The margin percentage increases by 10 basis points if more than 50% of the facility is outstanding. TDS may select borrowing periods of either seven days or one, two, three or six months. Under certain circumstances, with less than

two days' notice of intent to borrow, interest on borrowings is the prime rate less 50 basis points (the prime rate was 5.25% at December 31, 2004). TDS currently pays facility and administration fees at an aggregate annual rate of 0.11% of the total \$600 million facility. These fees totaled \$0.7 million for the years ended December 31, 2004, 2003 and 2002.

TDS also had \$75 million in direct bank lines of credit at December 31, 2004, all of which were unused. The terms of the direct bank lines of credit provide for borrowings at negotiated rates up to the prime rate (5.25% at December 31, 2004).

On December 19, 2003, U.S. Cellular amended its \$325 million revolving credit facility with a group of banks to increase the size of the facility to \$700 million. At December 31, 2004, U.S. Cellular's \$700 million revolving credit facility had \$30.0 million of borrowings and \$0.2 million of letters of credit outstanding against it leaving \$669.8 million available for use. On December 9, 2004, U.S. Cellular entered into an agreement to amend the terms and conditions of this facility. The primary changes to the terms and conditions are that (i) the maturity date has been extended to December 2009; (ii) the facility fee and certain interest rates payable on loans have been reduced; (iii) a utilization fee has been added for each day that facility usage exceeds 50% of the total facility; and (iv) the material adverse change condition has been removed with respect to drawdowns. Borrowings bear interest at the LIBOR rate plus a contractual spread based on U.S. Cellular's credit rating. At December 31, 2004, the contractual spread was 30 basis points (the one-month LIBOR rate was 2.4% at December 31, 2004). U.S. Cellular may select borrowing periods of either seven days or one, two, three or six months. Under certain circumstances, with less than two days' notice of intent to borrow, interest on borrowings is the prime rate less 50 basis points (the prime rate was 5.25% at December 31, 2004). U.S. Cellular currently pays facility and administration fees at an aggregate annual rate of 0.11% of the total facility. These fees totaled \$1.5 million in 2004, \$0.7 million in 2003 and \$0.5 million in 2002.

Until December 23, 2003, U.S. Cellular had a \$500 million revolving credit facility with a group of banks. This credit facility was terminated on December 23, 2003 in connection with the amendment of U.S. Cellular's \$325 million credit facility to \$700 million. The terms of the revolving credit facility provided for borrowings with interest at the LIBOR rate plus a margin percentage based on U.S. Cellular's credit rating. Interest and principal were due the last day of the borrowing period, as selected by U.S. Cellular, of either seven days or one, two, three or six months. U.S. Cellular paid facility and administration fees at an aggregate annual rate of 0.10% of the total \$500 million facility. These fees totaled \$0.5 million for the years ended December 31, 2003 and 2002.

Information concerning notes payable is shown in the table that follows:

Year Ended December 31,	2004	2003
(Dollars in thousands)		
Balance at end of year	\$ 30,000	\$ —
Weighted average interest rate at end of year	4.8%	—%
Maximum amount outstanding during the year	\$100,000	\$627,892
Average amount outstanding during the year <sup>(1)</sup>	\$ 47,917	\$491,960
Weighted average interest rate during the year <sup>(1)</sup>	2.1%	1.5%

(1) The average was computed based on month-end balances.

The financial covenants associated with TDS's and U.S. Cellular's lines of credit require that each company maintain certain debt-to-capital and interest coverage ratios. In addition, the financial covenants associated with revolving credit facilities and lines of credit of certain subsidiaries require that these subsidiaries maintain certain debt-to-capital and interest coverage ratios. The covenants of U.S. Cellular's revolving credit facility prescribe certain terms associated with intercompany loans from TDS or TDS subsidiaries to U.S. Cellular or U.S. Cellular subsidiaries.

TDS's and U.S. Cellular's interest costs on its revolving credit facilities would increase if their credit ratings from either Standard & Poor's or Moody's were lowered. However, their credit facilities would not cease to be available solely as a result of a decline in their credit ratings. A downgrade in TDS's or U.S. Cellular's credit ratings could adversely affect their ability to renew existing, or obtain access to new, credit facilities in the future. Standard & Poor's currently rates both TDS and U.S. Cellular at A- with a Negative Outlook. Moody's currently rates both Baa1 with a Negative Outlook.

The maturity dates of certain of TDS's and U.S. Cellular's credit facilities would accelerate in the event of a change in control.

The continued availability of the revolving credit facilities requires TDS and U.S. Cellular to comply with certain negative and affirmative covenants, maintain certain financial ratios and represent certain matters at the time of each borrowing. On April 19, 2004 and December 22, 2004, TDS and U.S. Cellular announced that they would restate certain financial statements. The restatements resulted in defaults under the revolving credit agreements. TDS and U.S. Cellular were not in violation of any covenants that require TDS and U.S. Cellular to maintain certain financial ratios. TDS and U.S. Cellular did not fail to make any scheduled payments under such revolving credit agreements. TDS and U.S. Cellular received waivers from the lenders associated with the credit agreements under which the lenders agreed to waive any defaults that may have occurred as a result of the restatements. As of December 31, 2004, TDS and U.S. Cellular are in compliance with all covenants and other requirements set forth in their revolving credit agreements.

## 15 LONG-TERM DEBT

Long-term debt is as follows:

December 31,	2004	2003
(Dollars in thousands)		
Telephone and Data Systems, Inc. (Parent)		
7.6% Series A notes, due in 2041	\$ 500,000	\$ 500,000
Medium-term notes, averaging 9.8%, 9.25% to 10.0% due 2021-2025	52,200	52,200
7.0% senior notes, maturing in 2006	200,000	200,000
Purchase contracts, averaging 6.0%, due through 2021	1,097	1,097
Total Parent	753,297	753,297
Subsidiaries		
U.S. Cellular		
6% zero coupon convertible debentures (Liquid Yield Options Notes), maturing in 2015	—	310,749
Unamortized discount	—	(153,090)
	—	157,659
6.7% senior notes maturing in 2033	544,000	444,000
Unamortized discount	(13,070)	(7,171)
	530,930	436,829
7.5% senior notes, maturing in 2034	330,000	—
7.25% senior notes, maturing in 2007	—	250,000
8.75% senior notes, maturing in 2032	130,000	130,000
Other, 9.0% due in 2009	10,000	13,000
TDS Telecom		
Rural Utilities Service, Rural Telephone Bank and Federal Financing Bank		
Mortgage notes, various rates averaging 5.7% in 2004 and 5.9% in 2003, due through 2035	234,147	251,697
Other long-term notes, various rates averaging 6.5% in 2004 and 6.8% in 2003, due through 2006	9,891	12,326
Other Subsidiaries		
Long-term notes and leases, 4.7% to 5.7%, due through 2009	15,121	13,817
Total Subsidiaries	1,260,089	1,265,328
Total Long-term debt	2,013,386	2,018,625
Less: Current portion of long-term debt	38,787	23,712
Total Long-term debt, excluding current portion	\$1,974,599	\$1,994,913

### Telephone and Data Systems, Inc. (Parent)

The unsecured 7.6% Series A notes are due in 2041. Interest is payable quarterly. The notes are redeemable by TDS beginning December 2006 at 100% of the principal amount plus accrued and unpaid interest.

The unsecured medium-term notes mature at various times from 2021 to 2025. Interest is payable semi-annually. The medium-term notes may be redeemed by TDS at par value plus accrued but unpaid interest. As of December 31, 2004, medium-term notes aggregating \$17.2 million and \$35.0 million have initial redemption dates in 2005 and 2006, respectively. On December 15, 2004, TDS issued notice of its intent to redeem the \$17.2 million of medium-term notes in 2005. This amount has been reclassified to current portion of long-term debt on the Balance Sheet as of December 31, 2004. TDS redeemed these notes on January 18, 2005 and February 10, 2005 at a price equal to the principal amount plus accrued interest to the redemption date. TDS redeemed medium-term notes aggregating \$70.5 million in 2003. A loss of \$0.8 million was recorded on the repurchase and retirement of \$5.0 million of medium-term notes in 2003. The remaining medium-term notes were redeemed at par value in 2003.

The unsecured 7.0% senior notes are due August 2006. Interest is payable semi-annually. The notes are redeemable at any time at the option of TDS, at a redemption price equal to the greater of (a) 100% of the principal amount of such notes, plus accrued but unpaid interest, or (b) the sum of the present values of the remaining scheduled payments of principal and interest thereon discounted to the redemption date on a semi-annual basis at the Treasury Rate plus 0.25%.

#### **Subsidiaries – U.S. Cellular**

In June 2004, U.S. Cellular issued \$330 million in aggregate principal amount of unsecured 7.5% senior notes due June 15, 2034. Interest on the notes is payable quarterly. U.S. Cellular may redeem the notes, in whole or in part, at any time on and after June 17, 2009, at redemption price equal to 100% of the principal amount redeemed plus accrued and unpaid interest to the redemption date. The net proceeds from this offering, after deducting underwriting discounts, were approximately \$319.6 million.

Also, in June 2004, U.S. Cellular issued \$100 million in aggregate principal amount of unsecured 6.7% senior notes due December 15, 2033, priced to yield 7.21% to maturity. The net proceeds from this offering, after deducting underwriting discounts, were approximately \$92.9 million. This was a further issuance of U.S. Cellular's 6.7% senior notes that were issued in December 2003, in the aggregate principal amount of \$444 million.

The total net proceeds from the 7.5% and 6.7% senior note offerings completed in June 2004, after deducting underwriting discounts, were approximately \$412.5 million. Of this amount, \$163.3 million was used to redeem U.S. Cellular's Liquid Yield Option Notes, in July 2004, at accreted value. The balance of the net proceeds, together with borrowings under the revolving credit agreement, were used to redeem all \$250 million of U.S. Cellular's 7.25% senior notes on August 16, 2004. No gain or loss was recognized as a result of such redemptions. However, U.S. Cellular wrote off \$3.6 million of deferred debt expenses related to the redemption of long-term debt to other income (expense), net in the Statement of Operations in 2004.

In December 2003, U.S. Cellular sold \$444 million of 6.7% senior notes due December 15, 2033, priced to yield 6.83% to maturity. Interest is paid semi-annually. U.S. Cellular may redeem the notes, in whole or in part, at any time prior to maturity at a redemption price equal to the greater of (a) 100% of the principal amount of such notes, plus accrued but unpaid interest, or (b) the sum of the present values of the remaining scheduled payments of principal and interest thereon discounted to the redemption date on a semi-annual basis at the Treasury Rate plus 0.30%. The proceeds were used to repay outstanding short-term debt.

In November 2002, U.S. Cellular sold \$130 million of unsecured 8.75% senior notes due in November 2032. Interest is paid quarterly. U.S. Cellular may redeem the notes beginning in 2007 at the principal amount plus accrued interest.

U.S. Cellular's \$250 million, unsecured 7.25% senior notes were due 2007 and interest was payable semi-annually. U.S. Cellular redeemed the notes in August 2004 at the principal amount plus accrued interest.

On July 26, 2004, U.S. Cellular redeemed its Liquid Yield Option Notes at accreted value. The unsecured 6% yield to maturity zero coupon convertible redeemable notes were due in 2015. Each Liquid Yield Option Note was convertible at the option of the holder at any time at a conversion rate of 9.475 U.S. Cellular Common Shares per \$1,000 of note. Upon notice of conversion, U.S. Cellular had the option to deliver its Common Shares or cash equal to the market value of the Common Shares. U.S. Cellular had the option to redeem the Liquid Yield Option Notes for cash at the issue price plus accrued original issue discount through the date of redemption. Holders had the right to exercise their conversion option prior to the redemption date. There were no Liquid Yield Option Notes redeemed in 2003 and 2002.

#### **Subsidiaries – TDS Telecom**

TDS Telecom's Rural Utilities Service, Rural Telephone Bank and Federal Financing Bank mortgage notes issued under certain loan agreements with the Rural Utilities Service, Rural Telephone Bank and Federal Financing Bank, agencies of the United States of America, are to be repaid in equal monthly or quarterly installments covering principal and interest beginning six months to three years after dates of issue and expiring through 2035. Substantially all telephone plant of the incumbent local exchange companies is pledged under Rural Utilities Service and Rural Telephone Bank mortgage notes and various other obligations of the telephone subsidiaries.

#### **Consolidated**

The annual requirements for principal payments on long-term debt, excluding amounts due on the forward contracts, are approximately \$38.8 million, \$222.9 million, \$22.6 million, \$22.5 million and \$31.2 million for the years 2005 through 2009, respectively.

The covenants associated with TDS's long-term debt obligations, among other things, restrict TDS's ability, subject to certain exclusions, to incur additional liens; enter into sale and lease-back transactions; and sell, consolidate or merge assets. As of December 31, 2004, TDS was in compliance with all of the covenants of its debt obligations.

In addition, the covenants associated with long-term debt obligations of certain subsidiaries of TDS, among other things, restrict these subsidiaries' ability, subject to certain exclusions, to incur additional liens; enter into sale and leaseback transactions; sell, consolidate or merge assets, and pay dividends. As of December 31, 2004, TDS's subsidiaries were in compliance with all of the covenants of their debt obligations.

#### Forward Contracts

TDS maintains a portfolio of available-for-sale marketable equity securities, the majority of which are the result of sales or trades of non-strategic assets. During 2002, subsidiaries of TDS entered into forward contracts with counterparties in connection with its Deutsche Telekom, Vodafone and VeriSign marketable equity securities with proceeds aggregating \$1,631.8 million. The principal amount of the forward contracts was accounted for as a loan. The collar portions of the forward contracts are accounted for as derivative instruments. The following table summarizes certain facts surrounding the contracted securities, pledged as collateral for the forward contracts.

December 31,		2004	2003
Security	Shares	Loan Amount	
(Dollars in thousands)			
Deutsche Telekom	131,461,861	\$1,532,257	\$1,532,257
Unamortized debt discount		(62,192)	(78,177)
		1,470,065	1,454,080
Vodafone	12,945,915	201,038	201,038
VeriSign	2,361,333	20,819	20,819
Unamortized debt discount		(2,278)	(3,175)
		18,541	17,644
		\$1,689,644	\$1,672,762

The Deutsche Telekom forward contracts mature from May 2007 to August 2008. Contracts aggregating \$1,094.3 million require quarterly interest payments at the LIBOR rate plus 50 basis points (the three-month LIBOR rate was 2.56% at December 31, 2004). Contracts aggregating \$438.0 million are structured as zero coupon obligations with a weighted average effective interest rate of 4.4% per year. No interest payments are required for the zero coupon obligations during the contract period.

The Vodafone forward contracts mature in May and November 2007. The Vodafone forward contracts require quarterly interest payments at the LIBOR rate plus 50 basis points (the three-month LIBOR rate was 2.56% at December 31, 2004).

The VeriSign forward contract matures in May 2007 and is structured as a zero coupon obligation with an effective interest rate of 5.0% per year. TDS is not required to make interest payments during the contract period.

Forward contracts aggregating \$738.7 million and \$1,015.4 million mature in 2007 and 2008, respectively.

The risk management objective of the forward contracts is to hedge the value of the marketable equity securities from losses due to decreases in the market prices of the securities ("downside limit") while retaining a share of gains from increases in the market prices of such securities ("upside potential"). The downside limit is hedged at or above the accounting cost basis thereby eliminating the risk of an other-than-temporary loss being recorded on these contracted securities.

Under the terms of the forward contracts, subsidiaries of TDS and U.S. Cellular will continue to own the contracted shares and will receive dividends paid on such contracted shares, if any. The forward contracts mature from May 2007 to August 2008 and, at TDS's and U.S. Cellular's option, may be settled in shares of the respective security or in cash, pursuant to formulas that "collar" the price of the shares. The collars effectively limit downside risk and upside potential on the contracted shares. The collars are typically adjusted for any changes in dividends on the contracted shares. If the dividend increases, the collar's upside potential is typically reduced. If the dividend decreases, the collar's upside potential is typically increased. If TDS and U.S. Cellular elect to settle in shares, they will be required to deliver the number of shares of the contracted security determined pursuant to the formula. If shares are delivered in the settlement of the forward contract, TDS and U.S. Cellular would incur a current tax liability at the time of delivery based on the difference between the tax basis of the marketable equity securities delivered and the net amount realized through maturity. If TDS and U.S. Cellular elect to settle in cash, they will be required to pay an amount in cash equal to the fair market value of the number of shares determined pursuant to the formula. TDS and U.S. Cellular have provided guarantees to the counterparties which provide assurance that all principal and interest amounts are paid by its consolidated subsidiaries upon settlement of the contracts.

TDS and U.S. Cellular are required to comply with certain covenants under the forward contracts. On April 19, 2004 and December 22, 2004, TDS and U.S. Cellular announced that they expected to restate certain financial statements. The restatements resulted in defaults under certain of the forward contracts. TDS and U.S. Cellular were not in violation of any covenants that require TDS and U.S. Cellular to maintain certain financial ratios. TDS and U.S. Cellular did not fail to make any scheduled payments under such forward contracts. TDS and U.S. Cellular received waivers from the counterparty to such forward contracts under which the counterparty agreed to waive any defaults that may have occurred as a result of the restatement. As of December 31, 2004, TDS and U.S. Cellular are in compliance with all covenants and other requirements set forth in the forward contracts.



## 16 FINANCIAL INSTRUMENTS AND DERIVATIVES

### Financial Instruments

Financial instruments are as follows:

December 31,	2004		2003	
	Book Value	Fair Value	Book Value	Fair Value
(Dollars in thousands)				
Cash and cash equivalents	\$1,168,581	\$1,168,581	\$ 937,651	\$ 937,651
Current portion of long-term debt	38,787	38,787	23,712	23,712
Notes payable	30,000	30,000	—	—
Long-term debt	1,974,599	1,983,826	1,994,913	2,090,446
Forward contracts	1,689,644	1,691,101	1,672,762	1,679,450
Preferred shares	\$ 3,864	\$ 3,249	\$ 3,864	\$ 3,151

The carrying amounts of cash and cash equivalents, the current portion of long-term debt and notes payable approximate fair value due to the short-term nature of these financial instruments. The fair value of TDS's long-term debt was estimated using market prices for the 7.6% Series A notes, the 7.0% senior notes, the 6.7% senior notes, the 7.5% senior notes, the 8.75% senior notes and the 6% zero coupon convertible debentures, and discounted cash flow analysis for the remaining debt. The carrying amounts of the variable rate forward contracts approximates fair value due to the repricing of the instruments on a quarterly basis. The fair value of the zero coupon forward contracts was determined using discounted cash flow analysis.

### Derivatives

During 2002, subsidiaries of TDS entered into forward contracts in connection with its Deutsche Telekom, Vodafone and VeriSign marketable equity securities. The principal amount of the forward contracts is accounted for as a loan. The collar portions of the forward contracts are accounted for as derivative instruments. The following table summarizes the shares contracted and the downside limit and upside potential.

December 31, 2004		Downside Limit (Floor)	Upside Potential (Ceiling)
Security	Shares		
VeriSign	2,361,333	\$ 8.82	\$11.46
Vodafone	12,945,915	\$15.07–\$16.07	\$20.01–\$22.60
Deutsche Telekom	131,461,861	\$10.74–\$12.41	\$14.21–\$17.17

The forward contracts for the forecasted transactions and hedged items are designated as cash flow or fair value hedges and recorded as assets or liabilities on the balance sheet at their fair value. The fair value of the derivative instruments is determined using the Black-Scholes model.

The Deutsche Telekom and Vodafone forward contracts are designated as cash flow hedges, where changes in the forward contract's fair value are recognized in accumulated other comprehensive income until they are recognized in earnings when the forward contract is settled. If the delivery of the contracted shares does not occur, or it becomes probable that it will not occur, the gain or loss on the related cash flow hedge is recognized in earnings at that

time. No components of the forward contracts are excluded in the measurement of hedge effectiveness. The critical terms of the forward contracts are the same as the underlying forecasted transactions; therefore, changes in the fair value of the forward contracts are anticipated to be effective in offsetting changes in the expected cash flows from the forecasted transactions. No gains or losses related to ineffectiveness of cash flow hedges were recognized in earnings for the years ended December 31, 2004 and 2003.

With regard to the forward contracts on the Vodafone shares and the Deutsche Telekom shares, transactions being accounted for as cash flow hedges, management has evaluated the expected timing of the hedged forecasted transactions to deliver the underlying shares to settle the forward contracts, and believes that these forecasted transactions are probable of occurring in the periods specified in the related hedge documentation or within an additional two-month period of time thereafter.

The VeriSign forward contract is designated as a fair value hedge, where effectiveness of the hedge is assessed based upon the intrinsic value of the underlying options. The intrinsic value of the forward contract is defined as the difference between the applicable option strike price and the market value of the contracted shares on the balance sheet date. Changes in the intrinsic value of the options are expected to be perfectly effective at offsetting changes in the fair value of the hedged item. Changes in the intrinsic value of the options are recognized in accumulated other comprehensive income until they are recognized in earnings when the forward contract is settled. Changes in the time value of the options are excluded from the effectiveness assessment and are recognized in earnings each period. Changes in the time value of the options aggregating a \$2.2 million gain and \$3.5 million loss for the years ended December 31, 2004 and 2003, respectively, were included in the Statement of Operations caption other income (expense).

TDS reported a derivative liability of \$1,210.5 million and \$712.3 million at December 31, 2004 and 2003, respectively. These amounts are included in the Balance Sheet caption deferred liabilities and credits.

## 17 MINORITY INTEREST IN SUBSIDIARIES

The following table summarizes the minority shareholders' and partners' interests in the equity of consolidated subsidiaries.

December 31,	2004	2003
(Dollars in thousands)		
U.S. Cellular		
Public shareholders	\$466,624	\$439,838
Subsidiaries' partners and shareholders	32,682	51,430
	499,306	491,268
Other minority interests	—	11,434
	\$499,306	\$502,702

The Board of Directors of U.S. Cellular from time to time has authorized the repurchase of U.S. Cellular Common Shares not owned by TDS. U.S. Cellular's primary repurchase program expired in December 2003. U.S. Cellular may use repurchased shares to fund acquisitions, for the conversion of debt and for other corporate purposes. U.S. Cellular repurchased no shares during 2003.

The Board of Directors of U.S. Cellular has also authorized the repurchase of a limited amount of its common shares on a quarterly basis, primarily for use in the employee benefit plans. In 2004 U.S. Cellular repurchased 91,700 U.S. Cellular Common Shares under this authorization for an aggregate purchase price of \$3.9 million representing an average per share price of \$42.62 including commissions. U.S. Cellular repurchased no shares in 2003.

Under SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity," certain minority interests in consolidated entities with finite lives may meet the standard's definition of a mandatorily redeemable financial instrument and thus require reclassification as liabilities and remeasurement at the estimated amount of cash that would be due and payable to settle such minority interests under the applicable entity's organization agreement assuming an orderly liquidation of the finite-lived entity, net of estimated liquidation costs (the "settlement value"). TDS's consolidated financial statements include such minority interests that meet the standard's definition of mandatorily redeemable financial instruments. These mandatorily redeemable minority interests represent interests held by third parties in consolidated partnerships and limited liability companies ("LLCs"), where the terms of the underlying partnership or LLC agreement provide for a defined termination date at which time the assets of the subsidiary are to be sold, the liabilities are to be extinguished and the remaining net proceeds are to be distributed to the minority interest holders and TDS in accordance with the respective partnership and LLC agreements. The termination dates of TDS's mandatorily redeemable minority interests range from 2042 to 2100.

The settlement value of TDS's mandatorily redeemable minority interests was estimated to be \$108.9 million at December 31, 2004 and \$86.7 million at December 31, 2003. This represents the estimated amount of cash that would be due and payable to settle minority interests assuming an orderly liquidation of the finite-lived consolidated partnerships and LLCs on December 31, 2004 and 2003, net of estimated liquidation costs. This amount is being disclosed pursuant to the requirements of FASB Staff Position ("FSP") No. FAS 150-3, "Effective Date, Disclosures, and Transition for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests under FASB Statement No. 150 "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." TDS has no current plans or intentions to liquidate any of the related partnerships or LLCs prior to their scheduled termination dates. The corresponding carrying value of the minority interests in finite-lived consolidated partnerships and LLCs at December 31, 2004 and 2003 was

\$30.6 million and \$26.8 million, respectively, and is included in the Balance Sheet caption minority interest in subsidiaries. The excess of the aggregate settlement value over the aggregate carrying value of the mandatorily redeemable minority interests of \$78.3 million and \$59.9 million, respectively, was primarily due to the unrecognized appreciation of the minority-interest holders' share of the underlying net assets in the consolidated partnerships and LLCs. Neither the minority-interest holders' share, nor TDS's share, of the appreciation of the underlying net assets of these subsidiaries is reflected in the consolidated financial statements under GAAP. The estimate of settlement value was based on certain factors and assumptions. Change in those factors and assumptions could result in a materially larger or smaller settlement amount.

## 18 PREFERRED SHARES

The holders of outstanding Preferred Shares are entitled to one vote per share. TDS had 38,645 Preferred Shares (\$100 per share stated value) authorized, issued and outstanding at December 31, 2004 and 2003, 30,000 of which are redeemable at the option of TDS at \$100 per share plus accrued and unpaid dividends beginning in 2007. At December 31, 2004 and 2003, 30,000 Preferred Shares were convertible into 54,540 TDS Common Shares, at the option of the holder. Preferred Shares totaling 8,228 are redeemable at the option of TDS for 4.35 U.S. Cellular common shares or equivalent value in cash or TDS Common Shares. The remaining Preferred Shares are not redeemable. The average dividend rate was \$5.23 per share in 2004 and 2003.

The following is a schedule of Preferred Shares activity.

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Balance, beginning of year	\$3,864	\$ 6,954	\$7,442
Less:			
Conversion of preferred	—	(2,940)	(122)
Redemption of preferred	—	(150)	(366)
Balance, end of year	\$3,864	\$ 3,864	\$6,954

## 19 COMMON STOCKHOLDERS' EQUITY

### Common Stock

The holders of Common Shares are entitled to one vote per share. The holders of Series A Common Shares are entitled to ten votes per share. Series A Common Shares are convertible, on a share for share basis, into Common Shares. TDS has reserved 6,421,000 Common Shares at December 31, 2004, for possible issuance upon such conversion. See Note 24 – Subsequent Events for discussion of the potential increase in Special Common Shares authorized and the potential use of Special Common Shares.

The following table summarizes the number of Common and Series A Common Shares outstanding.

	Common Shares	Treasury Shares	Net Common Shares Outstanding	Series A Common Shares
(Shares in thousands)				
Balance				
December 31, 2001	55,659	(3,868)	51,791	6,778
Conversion of Series A Common Shares	189	—	189	(189)
Dividend reinvestment, incentive and compensation plans	8	65	73	13
Other	13	4	17	—
Conversion of Preferred Shares	6	—	6	—
Balance				
December 31, 2002	55,875	(3,799)	52,076	6,602
Repurchase of Common Shares	—	(1,961)	(1,961)	—
Conversion of Series A Common Shares	187	—	187	(187)
Dividend reinvestment, incentive and compensation plans	66	65	131	25
Other	—	7	7	—
Conversion of Preferred Shares	154	—	154	—
Balance				
December 31, 2003	56,282	(5,688)	50,594	6,440
Repurchase of Common Shares	—	(215)	(215)	—
Conversion of Series A Common Shares	37	—	37	(37)
Dividend reinvestment, incentive and compensation plans	58	537	595	17
Other	—	4	4	1
Conversion of Preferred Shares	—	—	—	—
Balance				
December 31, 2004	56,377	(5,362)	51,015	6,421

### Common Share Repurchase Program

The Board of Directors of TDS from time to time has authorized the repurchase of TDS Common Shares. In February 2003, the Board of Directors authorized the repurchase of up to 3.0 million TDS Common Shares through February 2006. As of December 31, 2004, TDS has repurchased 2,175,700 Common Shares under this authorization, leaving 824,300 shares available for repurchase under the authorization. Share repurchases may be made from time to time on the open market or at negotiated prices in private transactions. TDS may use repurchased shares to fund acquisitions and for other corporate purposes.

In 2004, TDS repurchased 214,800 Common Shares for an aggregate purchase price of \$14.9 million, representing an average per share price of \$69.15 including commissions. In 2003, TDS repurchased 1,960,900 Common Shares for an aggregate purchase price of \$92.4 million, representing an average per share price of \$47.10 including commissions. No shares were repurchased in 2002. TDS reissued 541,000 Common Shares in 2004, 72,000 in 2003 and 69,000 in 2002 primarily for incentive and compensation plans.

### Accumulated Other Comprehensive Income

The cumulative balance of unrealized gains (losses) on securities and derivative instruments and related income tax effects included in accumulated other comprehensive income are as follows:

Year Ended December 31,	2004	2003
(Dollars in thousands)		
<b>Marketable Equity Securities</b>		
Balance, beginning of year	\$ 738,120	\$ 241,288
Add (deduct):		
Unrealized gains on marketable equity securities	626,609	829,083
Income tax (expense)	(244,558)	(323,828)
	382,051	505,255
Equity method unrealized gains (losses)	135	(489)
Minority share of unrealized (gains) losses	(2,584)	(8,019)
Net unrealized gains	379,602	496,747
Recognized losses on marketable equity securities	40	168
Income tax (benefit)	(16)	(62)
	24	106
Minority share of recognized (losses)	—	(21)
Net recognized losses from marketable equity securities included in net income	24	85
Net change in unrealized gains (losses) on marketable equity securities in comprehensive income	379,626	496,832
Balance, end of year	\$1,117,746	\$ 738,120
<b>Derivative Instruments</b>		
Balance, beginning of year	\$ (441,300)	\$ (49,584)
Add (deduct):		
Unrealized loss on derivative instruments	(500,086)	(650,586)
Income tax benefit	195,439	253,774
	(304,647)	(396,812)
Minority share of unrealized losses	1,706	5,096
Net change in unrealized gains (losses) on derivative instruments included in comprehensive income	(302,941)	(391,716)
Balance, end of year	\$ (744,241)	\$ (441,300)
<b>Accumulated Other Comprehensive Income</b>		
Balance, beginning of year	\$ 296,820	\$ 191,704
Net change in marketable equity security	379,626	496,832
Net change in derivative instruments	(302,941)	(391,716)
Net change in unrealized gains (losses) included in comprehensive income	76,685	105,116
Balance, end of year	\$ 373,505	\$ 296,820

## 20 DIVIDEND REINVESTMENT, INCENTIVE AND COMPENSATION PLANS

The following table summarizes Common and Series A Common Shares issued, including reissued Treasury Shares, for the employee stock purchase plans and dividend reinvestment plans described below.

Year Ended December 31,	2004	2003
Common Shares		
Dividend reinvestment plan	58,000	66,000
Employee stock purchase plan	19,000	16,000
Stock-based compensation plans	518,000	49,000
	<u>595,000</u>	<u>131,000</u>
Series A Common Shares		
dividend reinvestment plan	17,000	25,000

### Tax-Deferred Savings Plan

TDS had reserved 45,000 Common Shares at December 31, 2004, for issuance under the TDS Tax-Deferred Savings Plan, a qualified profit-sharing plan pursuant to Sections 401(a) and 401(k) of the Internal Revenue Code. Participating employees have the option of investing their contributions and TDS's contributions in a TDS Common Share fund, a U.S. Cellular Common Share fund or certain unaffiliated funds.

### Dividend Reinvestment Plans

TDS had reserved 295,000 Common Shares at December 31, 2004, for issuance under the Automatic Dividend Reinvestment and Stock Purchase Plan and 79,000 Series A Common Shares for issuance under the Series A Common Share Automatic Dividend Reinvestment Plan. These plans enable holders of TDS's Common Shares and Preferred Shares to reinvest cash dividends in Common Shares and holders of Series A Common Shares to reinvest cash dividends in Series A Common Shares. The purchase price of the shares is 95% of the market value, based on the average of the daily high and low sales prices for TDS's Common Shares on the American Stock Exchange for the ten trading days preceding the date on which the purchase is made.

### Employee Stock Purchase Plan

TDS had reserved 221,000 Common Shares at December 31, 2004, under the 2003 Employee Stock Purchase Plan, which will terminate on December 31, 2008. The plan became effective April 1, 2003, and provides for eligible employees of TDS and its subsidiaries to purchase a limited number of TDS Common Shares on a quarterly basis. The per share cost to each participant is at 85% of the market value of the Common Shares as of the issuance date.

### Stock-Based Compensation Plans

TDS accounts for stock options, restricted stock awards and employee stock purchase plans under APB Opinion No. 25. No compensation costs have been recognized for options granted in 2004. TDS recorded compensation expense of \$0.3 million on 53,000 options granted in 2003. No compensation costs have been recognized for the remaining 615,000 options granted in 2003. No compensation costs have been recognized for the stock option plans in 2002 and employee stock purchase plans in 2004, 2003 and 2002. Compensation costs were recognized for restricted stock awards as expenses in the Statement of Operations.

TDS had reserved 4,255,000 Common Shares at December 31, 2004, for options granted and to be granted to key employees. TDS has established certain plans that provide for the grant of stock options to officers and employees. The options are exercisable over a specified period not in excess of ten years. Options vest from three months to four years from the date of grant. The options expire from 2005 to 2014 or three months after the date of the employee's termination of employment, if earlier. Employees who leave at the age of retirement have one year within which to exercise their stock options.

A summary of the status of TDS stock option plans at December 31, 2004, 2003 and 2002 and changes during the years then ended is presented in the table and narrative that follows:

	Number of Shares	Weighted Average Option Prices	Weighted Average Black-Scholes Values of Option Grants
Stock options:			
Outstanding December 31, 2001			
(1,031,000 exercisable)	1,391,000	\$ 80.37	
Granted	467,000	\$ 59.32	\$ 22.62
Exercised	(41,000)	\$ 43.03	
Canceled	(20,000)	\$107.25	
Outstanding December 31, 2002			
(1,355,000 exercisable)	1,797,000	\$ 75.24	
Granted	668,000	\$ 45.80	\$ 17.24
Exercised	(49,000)	\$ 43.51	
Canceled	(63,000)	\$ 82.66	
Outstanding December 31, 2003			
(1,762,000 exercisable)	2,353,000	\$ 67.32	
Granted	547,000	\$ 65.98	\$25.73
Exercised	(518,000)	\$ 49.08	
Canceled	(51,000)	\$ 77.07	
Outstanding December 31, 2004			
(1,791,000 exercisable)	2,331,000	\$ 70.76	

At December 31, 2004, 1,791,000 options were exercisable, have exercise prices between \$33.87 and \$127.00 and a weighted average exercise price of \$75.04. The weighted average exercise price of options exercisable at December 31, 2003 and 2002 was \$70.68 and \$72.09, respectively.

The following table provides certain details concerning TDS stock options outstanding at December 31, 2004:

Range of Exercise Prices	Stock Options Outstanding	Weighted Average Exercise Price	Weighted Average Contractual Life Remaining (Years)
\$ 33.87-\$ 49.99	583,000	\$ 42.63	5.7
\$ 50.00-\$ 74.99	1,067,000	\$ 62.18	8.4
\$ 75.00-\$ 99.99	166,000	\$ 98.36	6.4
\$100.00-\$127.00	515,000	\$111.44	5.5



The following table provides certain details concerning TDS stock options exercisable at December 31, 2004:

Range of Exercise Prices	Stock Options Exercisable	Weighted Average Exercise Price
\$ 33.87–\$49.99	373,000	\$ 42.37
\$ 50.00–\$74.99	737,000	\$ 60.86
\$ 75.00–\$99.99	166,000	\$ 98.36
\$100.00–\$127.00	515,000	\$111.44

The fair value of each option grant was estimated on the date of the grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants in 2004, 2003 and 2002, respectively: risk-free interest rates of 4.5%, 3.7% and 4.2%; expected dividend yields of 1.0%, 1.4% and 1.3%; expected lives of 7.3 years, 8.6 years and 8.6 years, and expected volatility of 31.8%, 31.7% and 29.9%.

U.S. Cellular has granted key employees restricted shares of stock that fully vest after three years. The number of shares granted were 86,000, 142,000 and 87,000 in the years 2004, 2003 and 2002, respectively. The weighted-average values of the shares granted were \$38.65, \$23.70 and \$39.71 in 2004, 2003 and 2002, respectively. The expenses included in operating income due to grants of restricted shares were \$4.2 million, \$2.8 million and \$1.6 million in 2004, 2003 and 2002, respectively.

U.S. Cellular has established stock option plans that provide for the grant of stock options to officers and employees and has reserved 6,256,000 Common Shares at December 31, 2004 for options granted and to be granted to key employees. The options under the plan are exercisable from the date of vesting through 2005 to 2014, or 30 days following the date of the employee's termination of employment, if earlier.

A summary of the status of U.S. Cellular's stock option plans at December 31, 2004, 2003 and 2002 and changes during the years then ended is presented in the table and narrative as follows:

	Number of Shares	Weighted Average Option Prices	Weighted Average Black-Scholes Values of Option Grants
Stock options:			
Outstanding December 31, 2001			
(200,000 exercisable)	884,000	\$ 50.42	
Granted	869,000	\$ 38.80	\$ 19.74
Exercised	(9,000)	\$ 29.45	
Canceled	(201,000)	\$ 47.17	
Outstanding December 31, 2002			
(336,000 exercisable)	1,543,000	\$ 45.15	
Granted	1,435,000	\$ 23.85	\$ 10.99
Exercised	(2,000)	\$ 24.37	
Canceled	(448,000)	\$ 40.18	
Outstanding December 31, 2003			
(496,000 exercisable)	2,528,000	\$ 33.87	
Granted	796,000	\$ 37.46	\$16.27
Exercised	(220,000)	\$ 27.26	
Canceled	(248,000)	\$ 32.97	
Outstanding December 31, 2004			
(883,000 exercisable)	2,856,000	\$ 35.44	

At December 31, 2004, 883,000 stock options were exercisable, have exercise prices between \$23.61 and \$73.31 and a weighted average exercise price of \$41.33. The weighted average exercise price of options exercisable at December 31, 2003 and 2002, was \$46.22 and \$46.71, respectively.

The following table provides certain details concerning U.S. Cellular stock options outstanding at December 31, 2004:

Range of Exercise Prices	Stock Options Outstanding	Weighted Average Exercise Price	Weighted Average Contractual Life Remaining (Years)
\$23.20–\$36.99	1,405,000	\$26.04	8.2
\$37.00–\$49.99	1,221,000	\$40.60	7.9
\$50.00–\$73.31	230,000	\$65.76	4.8

The following table provides certain details concerning U.S. Cellular stock options exercisable at December 31, 2004:

Range of Exercise Prices	Stock Options Exercisable	Weighted Average Exercise Price
\$23.61–\$36.99	275,000	\$25.53
\$37.00–\$49.99	452,000	\$42.50
\$50.00–\$73.31	156,000	\$66.23

The fair value of each option grant was estimated on the date of the grant using the Black-Scholes option pricing model with the following weighted-average assumptions used for grants in 2004, 2003 and 2002, respectively: risk-free interest rates of 3.6%, 3.7% and 4.6%; expected dividend yield of zero for all years; expected lives of 6.6 years, 9.3 years and 9.4 years, and expected volatility of 36.0%, 29.4% and 39.4%.

## 21 EMPLOYEE BENEFIT PLANS

### Pension Plan

TDS sponsors a qualified noncontributory defined contribution pension plan. The plan provides benefits for the employees of TDS Corporate, TDS Telecom and U.S. Cellular. Under this plan, pension costs are calculated separately for each participant and are funded currently. Total pension costs were \$12.3 million, \$12.1 million and \$11.0 million in 2004, 2003 and 2002, respectively.

TDS also sponsors an unfunded nonqualified deferred supplemental executive retirement plan to supplement the benefits under the plan to offset the reduction of benefits caused by the limitation on annual employee compensation under the tax laws.

### Other Post-Retirement Benefits

TDS sponsors two defined benefit post-retirement plans that cover most of the employees of TDS Corporate, TDS Telecom and the subsidiaries of TDS Telecom. One plan provides medical benefits and the other provides life insurance benefits. Both plans are contributory, with retiree contributions adjusted annually. The medical plan anticipates future cost sharing changes that reflect TDS's intent to increase retiree contributions as a portion of total cost.

Total accumulated contributions to fund the costs of future retiree medical benefits are restricted to an amount not to exceed 25 percent of the total accumulated contributions to the pension trust. An additional contribution equal to a reasonable amortization of the past service cost may be made without regard to the 25 percent limitation.

The following table reconciles the beginning and ending balances of the benefit obligation and the fair value of plan assets for the other post-retirement benefit plans.

December 31,	2004	2003
(Dollars in thousands)		
Change in benefit obligation		
Benefit obligation at beginning of year	\$ 43,154	\$ 36,007
Service cost	2,362	1,676
Interest cost	2,674	2,480
Acquisitions	—	2,581
Amendments	(4,425)	(6,448)
Actuarial loss	4,764	8,197
Benefits paid	(2,265)	(1,339)
Special termination benefits <sup>(1)</sup>	616	—
Benefit obligation at end of year	46,880	43,154
Change in plan assets		
Fair value of plan assets at beginning of year	16,442	14,659
Actual return on plan assets	2,084	3,076
Employer contribution	7,018	46
Benefits paid	(2,265)	(1,339)
Fair value of plan assets at end of year	23,279	16,442
Funded status	(23,601)	(26,712)
Unrecognized net actuarial loss	24,281	20,444
Unrecognized prior service cost	(10,989)	(7,278)
(Accrued) benefit cost	\$(10,309)	\$(13,546)

(1) Due to an early retirement incentive program that was offered to certain employees at TDS Telecom during 2003.

Net periodic benefit cost for the years ended December 31, 2004, 2003 and 2002 includes the following components.

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Service cost	\$ 2,362	\$ 1,676	\$ 1,249
Interest cost on			
accumulated post-retirement			
benefit obligation	2,674	2,480	1,967
Expected return on plan assets	(1,776)	(1,197)	(1,487)
Amortization of:			
Unrecognized prior service cost <sup>(1)</sup>	(715)	(128)	(128)
Unrecognized net loss (gain) <sup>(2)</sup>	949	494	—
Net post-retirement (income) cost	\$ 3,494	\$ 3,325	\$ 1,601

(1) Based on straight-line amortization over the average time remaining before active employees become fully eligible for plan benefits.

(2) Based on straight-line amortization over the average time remaining before active employees retire.

The following assumptions were used to determine benefit obligations and net periodic benefit cost.

December 31,	2004	2003
Discount rate	5.75%	6.25%
Expected return on plan assets	8.5%	8.5%

The measurement date for actuarial determination was December 31, 2004. For measurement purposes, a 12.0% annual rate of increase in the per capita cost of covered health care benefits was assumed

for 2004 and 2003. The 2004 annual rate of increase is expected to reduce to 10.9% in 2005 and then decrease to 5.25% by 2010, while the 2003 annual rate of increase was expected to remain at 12.0% in 2004 and then decrease to 5.25% by 2010.

The health care cost trend rate assumption has a significant effect on the amounts reported. A one percentage point increase or decrease in assumed health care cost trend rates would have the following effects.

	One Percentage Point	
	Increase	Decrease
(Dollars in thousands)		
Effect on total of service and interest cost components	\$1,267	\$(1,011)
Effect on post-retirement benefit obligation	\$9,481	\$(7,912)

The following table describes how plan assets are invested.

Investment Category	Target Asset Allocation	Allocation of Plan Assets At December 31,	
		2004	2003
U.S. Equities	50%	49.8%	49.7%
International Equities	15%	15.1%	15.1%
Debt Securities	35%	35.1%	35.2%

The post-retirement benefit fund engages multiple asset managers to ensure proper diversification of the investment portfolio within each asset category. The investment objective is to exceed the rate of return of a performance index comprised of 50% Wilshire 5000 Stock Index, 15% MSCI World (excluding U.S.) Stock Index, and 35% Lehman Brothers Aggregate Bond Index. Historical average annual rates of return for this index exceed 8.5%, the expected rate of return used for planning.

The post-retirement benefit fund does not hold any debt or equity securities issued by TDS, U.S. Cellular or any related parties.

TDS is not required to set aside current funds for its future retiree health and life insurance benefits. The decision to contribute to the plan assets is based upon several factors, including the funded status of the plan, market conditions, alternative investment opportunities, tax benefits and other circumstances. TDS expects to fund \$5.3 million in 2005 for the 2004 contribution to the plan.

The following estimated future benefit payments, which reflect expected future service, are expected to be paid:

Year	Post-retirement Insurance Paid
(Dollars in thousands)	
2005	\$ 2,087
2006	1,871
2007	1,824
2008	1,905
2009	2,003
2010-2014	\$11,289

On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the "Act") was enacted. The Act expands Medicare coverage, primarily by adding a prescription drug

benefit for Medicare-eligible participants starting in 2006. The Act provides employers currently sponsoring prescription drug programs for Medicare-eligible participants with a range of options for coordinating with the new government-sponsored program to potentially reduce employers' costs. These options include supplementing the government program on a secondary payor basis or accepting a direct subsidy from the government to support a portion of the cost of the employer's program.

TDS has reviewed the impact of the Act on the TDS retiree medical plan, and has concluded that the plan is not expected to provide benefits which are the actuarial equivalent of the standard Medicare Part D benefit. Therefore, TDS would not be eligible to receive the federal subsidy offered under the Act.

The FASB published guidance on the accounting for the government subsidy in FSP 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003," that is effective beginning July 1, 2004. As a result of the conclusion that the plan is not expected to qualify for the federal subsidy, TDS believes that the effect of the Act on the TDS retiree medical plan is not a significant event pursuant to paragraph 73 of SFAS No. 106, "Employers' Accounting for Post-retirement Benefits Other Than Pensions," and TDS did not remeasure plan assets and obligations as of the effective date of FSP 106-2.

TDS intends to clarify the plan's design to advise participants that all retiree benefits will be coordinated with Medicare. The effects of this plan clarification will be recognized in future periods after the changes are implemented and communicated to employees.

## 22 COMMITMENTS AND CONTINGENCIES

### Capital Expenditures

U.S. Cellular's anticipated capital expenditures for 2005 primarily reflect plans for construction, system expansion and the buildout of certain of its personal communication service licensed areas. U.S. Cellular plans to finance its construction program using internally generated cash and short-term financing. U.S. Cellular's estimated capital spending for 2005 is \$570 million to \$610 million. These expenditures primarily address the following needs:

- Expand and enhance U.S. Cellular's coverage in its service areas.
- Provide additional capacity to accommodate increased network usage by current customers.
- Enhance U.S. Cellular's retail store network and office systems.

U.S. Cellular's overlay of its previously utilized technologies, primarily Time Division Multiple Access ("TDMA"), with Code Division Multiple Access ("CDMA-1XRTT") technology was completed in 2004. U.S. Cellular will utilize CDMA-1XRTT technology in building out the licenses it has acquired and expects to acquire in the future from AT&T Wireless.

While U.S. Cellular does not expect a significant portion of its capital spending in 2005 to be related to the buildout of newly acquired licensed areas, it does expect that capital spending related to these areas could be significant in 2006 and over the following several years.

TDS Telecom's estimated capital spending for 2005 is \$150 million to \$165 million. The incumbent local exchange companies are expected to spend \$120 million to \$130 million to provide for normal growth and to upgrade plant and equipment to provide enhanced services. The competitive local exchange companies are expected to spend \$30 million to \$35 million primarily to build switching and transmission facilities to meet the needs of a growing customer base. TDS Telecom plans to finance its construction program using primarily internally generated cash.

TDS Telecom currently has three Fiber-to-the-Premises trials underway. First is a complete fiber build-out of a large subdivision in one of the incumbent local exchange carrier markets. Second is a combination Fiber-to-the-Premises overbuild and asymmetric digital subscriber line deployment in one of the existing incumbent local exchange carrier markets. Lastly is a Fiber-to-the-Premises overbuild in a Regional Bell Operating Company market where TDS Telecom is currently a competitive local exchange carrier. The capital spending guidance provided above includes the impact of these projects that relates to 2005.

### Lease Commitments

TDS and its subsidiaries have leases for certain plant facilities, office space, retail sites, cell sites and data processing equipment, most of which are classified as operating leases. Certain leases have renewal options and/or fixed rental increases. Renewal options that are reasonably assured are included in determining the lease term. For the years 2004, 2003 and 2002, rent expense for noncancelable, long-term leases was \$117.6 million, \$99.1 million and \$68.2 million, respectively, and rent expense under cancelable, short-term leases was \$11.5 million, \$3.5 million and \$14.2 million, respectively. Rental revenue totaled \$12.8 million, \$10.0 million and \$8.5 million in 2004, 2003 and 2002, respectively. At December 31, 2004, the aggregate minimum rental payments required and rental receipts expected under noncancelable, long-term operating leases were as follows:

	Minimum Future Rental Payments	Minimum Future Rental Receipts
(Dollars in thousands)		
2005	\$ 96,850	\$11,492
2006	84,100	9,267
2007	68,187	7,172
2008	54,390	5,753
2009	38,715	3,584
Thereafter	\$205,397	\$ 3,566

### Indemnifications

TDS enters into agreements in the normal course of business that provide for indemnification of counterparties. These include certain asset sales and financings with other parties. The term of the indemnification varies by agreement. The events or circumstances that would require TDS to perform under these indemnities are transaction specific; however, these agreements may require TDS to indemnify the counterparty for costs and losses incurred from litigation or claims arising from the underlying transaction. TDS is unable to estimate the maximum potential liability for these types of indemnifications as the amounts are dependent on the outcome

of future events, the nature and likelihood of which cannot be determined at this time. Historically, TDS has not made any significant indemnification payments under such agreements.

TDS is party to an indemnity agreement with T-Mobile USA, Inc. ("T-Mobile") regarding certain contingent liabilities at Aerial Communications, Inc. ("Aerial") for the period prior to Aerial's merger with VoiceStream Wireless. At December 31, 2004, TDS has recorded liabilities of \$9.3 million relating to this indemnity.

#### Legal Proceedings

TDS is involved in legal proceedings before the Federal Communications Commission and various state and federal courts from time to time. Management does not believe that any of such proceedings will have a materially adverse impact on the financial position, results of operations or cash flows of TDS.

### 23 DISCONTINUED OPERATIONS

TDS is party to an indemnity agreement with T-Mobile (formerly known as VoiceStream Wireless) regarding certain contingent liabilities at Aerial Communications for the period prior to Aerial's merger into VoiceStream Wireless Corporation in 2000. In 2004, TDS recorded a gain of \$10.2 million (\$6.4 million, net of income tax benefit of \$3.8 million), or \$0.11 per diluted share for a reduction in the indemnity accrual. The accrual was reduced due to favorable outcomes of federal and state tax audits which reduced the potential indemnity obligation, recorded as discontinued operations in the Statements of Operations.

During 2003, it was estimated that the indemnity for certain contingent liabilities would be greater than previously provided. TDS took an additional charge of \$2.8 million (\$1.6 million, net of income tax expense of \$1.2 million), or \$(0.03) per diluted share with respect to the additional liability, recorded as discontinued operations in the Statements of Operations.

### 24 SUBSEQUENT EVENTS

U.S. Cellular is a limited partner in Carroll Wireless, L.P. ("Carroll Wireless"), an entity which participated in the auction of wireless spectrum designated by the FCC as Auction 58. Carroll Wireless was qualified to bid on spectrum which was available only to companies that fall under the FCC definition of "designated entities," which are small businesses that have a limited amount of assets. Carroll Wireless was a successful bidder for 17 licensed areas in Auction 58, which ended on February 15, 2005. These 17 licensed areas cover portions of 11 states and are in markets which are either adjacent to or overlap current U.S. Cellular licensed areas.

On March 4, 2005, Carroll Wireless increased the amount on deposit with the FCC to approximately \$26 million and filed an application with the FCC seeking a grant of the subject licenses. The aggregate amount due to the FCC for the 17 licenses is \$129.9 million, net of all bidding credits to which Carroll Wireless is entitled as a designated entity. U.S. Cellular consolidates Carroll Wireless for financial

reporting purposes, pursuant to the guidelines of FIN 46R, as U.S. Cellular anticipates absorbing a majority of Carroll Wireless' expected gains or losses.

Carroll Wireless is in the process of developing its long-term business and financing plans. As of March 4, 2005, U.S. Cellular has made capital contributions and advances to Carroll Wireless and/or its general partner of approximately \$26 million. Pending finalization of Carroll Wireless' permanent financing plan, and upon request by Carroll Wireless, U.S. Cellular may make capital contributions and advances to Carroll Wireless and/or its general partner of up to \$130 million to fund the payments to the FCC and additional working capital.

On February 17, 2005, the TDS Board of Directors (the "TDS Board") unanimously approved a proposal (the "Special Common Share Proposal"), to be submitted to TDS shareholders at a special meeting of shareholders of TDS scheduled for April 11, 2005, to approve an amendment (the "Amendment") to the Restated Certificate of Incorporation of TDS to increase the authorized number of Special Common Shares of TDS from 20,000,000 to 165,000,000.

On February 17, 2005, the TDS Board also approved a distribution of one Special Common Share in the form of a stock dividend with respect to each outstanding Common Share and Series A Common Share of TDS (the "Distribution"), which is expected to be effective May 13, 2005 to shareholders of record on April 29, 2005, subject to the approval of the Special Common Share Proposal by shareholders, the effectiveness of the Amendment, and certain other conditions.

Following approval and effectiveness of the Special Common Share Proposal, at some time in the future TDS may possibly offer to issue Special Common Shares in exchange for all of the Common Shares of U.S. Cellular that are not owned by TDS (a "Possible U.S. Cellular Transaction"). TDS currently owns approximately 82% of the shares of common stock of U.S. Cellular. A Possible U.S. Cellular Transaction would cause U.S. Cellular to become a wholly owned subsidiary of TDS. TDS has set no time frame for a Possible U.S. Cellular Transaction and there are no assurances that a transaction will occur.

### 25 BUSINESS SEGMENT INFORMATION

TDS conducts substantially all of its wireless telephone operations through its 82.0%-owned subsidiary, U.S. Cellular. At December 31, 2004, U.S. Cellular provided cellular telephone service in 27 states to 4.9 million customers. TDS conducts its wireline telephone operations through its wholly owned subsidiary, TDS Telecommunications Corporation ("TDS Telecom"). TDS Telecom provides service through local telephone operations, or incumbent local exchange carrier companies and through competitive local exchange carrier companies. At December 31, 2004, TDS Telecom operated 111 incumbent local exchange telephone companies serving 730,400 equivalent access lines in 28 states, and a competitive local exchange carrier serving 426,800 equivalent access lines in five states.



U.S. Cellular and TDS Telecom are billed for all services they receive from TDS, consisting primarily of information processing and general management services. Such billings are based on expenses specifically identified to U.S. Cellular and TDS Telecom and on allocations of common expenses. Management believes the method

used to allocate common expenses is reasonable and that all expenses and costs applicable to U.S. Cellular and TDS Telecom are reflected in the accompanying business segment information on a basis that is representative of what they would have been if U.S. Cellular and TDS Telecom operated on a stand-alone basis.

Financial data for TDS's business segments for each of the years ended December 31, 2004, 2003 and 2002 are as follows:

Year Ended or at December 31, 2004	U.S. Cellular	TDS Telecom		All Other <sup>(1)</sup>	Total
		ILEC	CLEC		
(Dollars in thousands)					
Operating revenues	\$2,837,619	\$ 658,522	\$ 228,692	\$ (4,444)	\$ 3,720,389
Cost of services and products	1,050,021	164,824	91,983	(2,657)	1,304,171
Selling, general and administrative expense	1,122,700	174,951	125,103	(1,787)	1,420,967
Operating income before depreciation, amortization and accretion and loss on assets held for sale and impairments <sup>(2)</sup>	664,898	318,747	11,606	—	995,251
Depreciation, amortization and accretion expense	497,942	131,665	38,349	—	667,956
Loss on impairment of intangible assets	—	—	29,440	—	29,440
(Gain) loss on assets held for sale	(10,806)	—	—	—	(10,806)
Loss on impairment of long-lived assets	—	—	87,910	—	87,910
Operating income (loss)	177,762	187,082	(144,093)	—	220,751
Significant noncash items:					
Investment income	68,481	958	—	184	69,623
Gain (loss) on investments	24,436	12,909	—	(491)	36,854
Marketable equity securities	282,829	—	—	3,115,975	3,398,804
Investment in unconsolidated entities	162,764	19,721	—	24,278	206,763
Total assets	5,181,868	1,777,139	154,184	3,880,650	10,993,841
Capital expenditures	\$ 655,120	\$ 103,069	\$ 35,178	\$ 4,885	\$ 798,252

  

Year Ended or at December 31, 2003	U.S. Cellular	TDS Telecom		All Other <sup>(1)</sup>	Total
		ILEC	CLEC		
(Dollars in thousands)					
Operating revenues	\$ 2,582,783	\$ 652,782	\$ 213,501	\$ (3,850)	\$ 3,445,216
Cost of services and products	931,309	167,342	86,377	(2,143)	1,182,885
Selling, general and administrative expense	1,004,655	180,171	115,175	(1,707)	1,298,294
Operating income before depreciation, amortization and accretion and loss on assets held for sale and impairments <sup>(2)</sup>	646,819	305,269	11,949	—	964,037
Depreciation, amortization and accretion expense	432,333	130,036	33,363	—	595,732
Loss on impairment of intangible assets	49,595	—	—	—	49,595
(Gain) loss on assets held for sale	45,908	—	—	—	45,908
Loss on impairment of long-lived assets	—	351	4,563	—	4,914
Operating income (loss)	118,983	174,882	(25,977)	—	267,888
Significant noncash items:					
Investment income	52,063	875	—	216	53,154
(Loss) on investments	(5,200)	(5,000)	—	—	(10,200)
Marketable equity securities	260,188	—	—	2,512,222	2,772,410
Investment in unconsolidated entities	170,569	19,606	—	24,710	214,885
Total assets	4,945,721	1,808,511	235,329	3,203,777	10,193,338
Capital expenditures	\$ 632,526	\$ 111,924	\$ 27,294	\$ 5,223	\$ 776,967

## Notes to Consolidated Financial Statements

Year Ended or at December 31, 2002	U.S. Cellular	TDS Telecom		All Other <sup>(1)</sup>	Total
		ILEC	CLEC		
(Dollars in thousands)					
Operating revenues	\$ 2,197,586	\$ 626,787	\$ 176,602	\$ (2,501)	\$ 2,998,474
Cost of services and products	735,273	142,618	85,909	(1,040)	962,760
Selling, general and administrative expense	829,993	186,023	124,359	(1,461)	1,138,914
Operating income before depreciation, amortization and accretion <sup>(2)</sup>	632,320	298,146	(33,666)	—	896,800
Depreciation, amortization and accretion expense	351,154	130,232	29,059	—	510,445
Operating income (loss)	281,166	167,914	(62,725)	—	386,355
Significant noncash items:					
Investment income	42,068	530	—	1,077	43,675
(Loss) on investments	(295,454)	(95,518)	—	(1,497,419)	(1,888,391)
Marketable equity securities	185,961	—	—	1,758,978	1,944,939
Investment in unconsolidated entities	161,451	18,965	—	25,579	205,995
Total assets	4,768,888	1,858,923	246,185	2,797,788	9,671,784
Capital expenditures	\$ 730,645	\$ 116,486	\$ 51,919	\$ —	\$ 899,050

(1) Consists of the TDS Corporate operations, TDS Telecom intercompany eliminations, TDS Corporate and TDS Telecom marketable equity securities and all other businesses.

(2) Operating income before depreciation, amortization and accretion and loss on assets held for sale and impairments and Operating income before depreciation, amortization and accretion are measures of profit and loss used by the chief operating decision maker to review the operating performance of each reportable business segment and is reported above in accordance with SFAS No. 131, "Disclosure about Segments of an Enterprise and Related Information."

Year Ended December 31,	2004	2003	2002
(Dollars in thousands)			
Total operating income from reportable segments	\$220,751	\$ 267,888	\$ 386,355
Investment and other income and expense	(71,405)	(137,152)	(1,942,024)
Income from continuing operations before income taxes and minority interest	\$149,346	\$ 130,736	\$(1,555,669)