ALLTEL CORP
Form 10-Q
August 08, 2006

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

FORM 10-Q

[x] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2006
OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 1-4996

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

| | |
|---|---|
| Delaware<br>(State or other jurisdiction of incorporation or organization) | 34-0868285<br>(I.R.S. Employer Identification No.) |
| One Allied Drive, Little Rock, Arkansas<br>(Address of principal executive offices) | 72202<br>(Zip Code) |

Registrant’s telephone number, including area code (501) 905-8000

(Former name, former address and former fiscal year, if changed since last report)

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

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). ¨ YES x NO

Number of common shares outstanding as of July 31, 2006: 388,143,286

The Exhibit Index is located on page 52.

**ALLTEL CORPORATION**
**FORM 10-Q**
**TABLE OF CONTENTS**



* No reportable information under this item.

Forward-Looking Statements

This Report on Form 10-Q includes, and future filings by the Company on Form 10-K, Form 10-Q and Form 8-K and future oral and written statements by ALLTEL Corporation ("Alltel") and its management may include, certain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are subject to uncertainties that could cause actual future events and results to differ materially from those expressed in the forward-looking statements. These forward-looking statements are based on estimates, projections, beliefs, and assumptions and are not guarantees of future events and results. Words such as "expects", "anticipates", "intends", "plans", "believes", "seeks", "estimates", and "should", and variations of these words and s expressions, are intended to identify these forward-looking statements. Alltel disclaims any obligation to update or revise any forward-looking statement based on the occurrence of future events, the receipt of new information, or otherwise.

Actual future events and results may differ materially from those expressed in these forward-looking statements as a result of a number of important factors. Representative examples of these factors include (without limitation) adverse changes in economic conditions in the markets served by Alltel; the extent, timing, and overall effects of competition in the communications business; material changes in the communications industry generally that could adversely affect vendor relationships with equipment and network suppliers and customer relationships with wholesale customers; changes in communications technology; the risks associated with the pending acquisition of Midwest Wireless; the risks associated with the integration of acquired businesses; adverse changes in the terms and conditions of the wireless roaming agreements of Alltel; the potential for adverse changes in the ratings given to Alltel's debt securities by nationally accredited ratings organizations; the uncertainties related to Alltel's strategic investments; the effects of litigation; and the effects of federal and state legislation, rules, and regulations governing the communications industry.

In addition to these factors, actual future performance, outcomes and results may differ materially because of more general factors including (without limitation) general industry and market conditions and growth rates, economic conditions, and governmental and public policy changes.

**ALLTEL CORPORATION**
**FORM 10-Q**
**PART I - FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**CONSOLIDATED BALANCE SHEETS (UNAUDITED)**

| (Dollars in millions, except per share amounts) | | June 30, 2006 | | December 31, 2005 |
|---|---|---|---|---|
| **Assets** | | | | |
| **Current Assets:** | | | | |
| Cash and short-term investments | $ | 2,531.4 | $ | 989.2 |
| Accounts receivable (less allowance for doubtful accounts of $81.2 and $84.7, respectively) | | 1,093.6 | | 1,077.2 |
| Inventories | | 160.9 | | 232.6 |
| Prepaid expenses and other | | 187.2 | | 115.2 |
| Assets held for sale | | - | | 1,951.2 |
| Total current assets | | 3,973.1 | | 4,365.4 |
| Investments | | 365.9 | | 358.4 |
| Goodwill | | 9,067.1 | | 8,677.3 |
| Other intangibles | | 2,214.0 | | 2,179.1 |
| **Property, Plant and Equipment:** | | | | |
| Land | | 313.5 | | 298.6 |
| Building and improvements | | 1,243.0 | | 1,211.4 |
| Wireline | | 7,021.0 | | 6,942.0 |
| Wireless | | 7,062.7 | | 6,852.6 |
| Information processing | | 1,266.8 | | 1,187.2 |
| Other | | 541.3 | | 530.3 |
| Under construction | | 525.8 | | 475.4 |
| Total property, plant and equipment | | 17,974.1 | | 17,497.5 |
| Less accumulated depreciation | | 9,976.1 | | 9,433.9 |
| Net property, plant and equipment | | 7,998.0 | | 8,063.6 |
| Other assets | | 315.5 | | 369.3 |
| **Total Assets** | $ | 23,933.6 | $ | 24,013.1 |
| | | | | |
| **Liabilities and Shareholders' Equity** | | | | |
| **Current Liabilities:** | | | | |
| Current maturities of long-term debt | $ | 1,594.1 | $ | 205.1 |
| Accounts payable | | 583.3 | | 645.4 |
| Advance payments and customer deposits | | 244.0 | | 240.5 |
| Accrued taxes | | 384.5 | | 174.7 |
| Accrued dividends | | 150.1 | | 147.8 |
| Accrued interest | | 102.3 | | 102.5 |
| Current deferred income taxes | | - | | 339.0 |
| Other current liabilities | | 199.2 | | 255.4 |
| Liabilities related to assets held for sale | | - | | 294.4 |
| Total current liabilities | | 3,257.5 | | 2,404.8 |
| Long-term debt | | 4,262.8 | | 5,782.9 |
| Deferred income taxes | | 1,894.2 | | 1,860.9 |
| Other liabilities | | 907.5 | | 949.0 |
| **Shareholders' Equity:** | | | | |

| | | | | |
|---|---|---|---|---|
| Preferred stock, Series C, $2.06, no par value, 10,382 and 11,122 | | | | |
| shares issued and outstanding, respectively | | 0.3 | | 0.3 |
| Common stock, par value $1 per share, 1.0 billion shares authorized, | | | | |
| 389,562,540 and 383,605,936 shares issued and outstanding, respectively | | 389.6 | | 383.6 |
| Additional paid-in capital | | 5,484.0 | | 5,339.3 |
| Unrealized holding gain on investments | | 38.0 | | 22.3 |
| Foreign currency translation adjustment | | - | | (2.8) |
| Retained earnings | | 7,699.7 | | 7,272.8 |
| Total shareholders' equity | | 13,611.6 | | 13,015.5 |
| **Total Liabilities and Shareholders' Equity** | $ | 23,933.6 | $ | 24,013.1 |

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

**CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)**

| (Millions, except per share amounts) | Three Months Ended June 30, 2006 | Three Months Ended June 30, 2005 | Six Months Ended June 30, 2006 | Six Months Ended June 30, 2005 |
|---|---|---|---|---|
| **Revenues and sales:** | | | | |
| Service revenues | $ 2,334.6 | $ 1,989.2 | $ 4,582.3 | $ 3,887.5 |
| Product sales | 339.1 | 270.9 | 631.1 | 498.6 |
| Total revenues and sales | 2,673.7 | 2,260.1 | 5,213.4 | 4,386.1 |
| **Costs and expenses:** | | | | |
| Cost of services (excluding depreciation of $256.5, $244.2, $507.8, and $486.1, respectively, included below) | 762.4 | 660.9 | 1,494.1 | 1,287.2 |
| Cost of products sold | 384.7 | 308.1 | 740.5 | 589.9 |
| Selling, general, administrative and other | 510.8 | 420.6 | 1,009.8 | 828.0 |
| Depreciation and amortization | 411.9 | 348.3 | 816.4 | 689.5 |
| Integration expenses and other charges | 12.0 | - | 31.5 | - |
| Total costs and expense | 2,081.8 | 1,737.9 | 4,092.3 | 3,394.6 |
| **Operating income** | 591.9 | 522.2 | 1,121.1 | 991.5 |
| | | | | |
| Equity earnings in unconsolidated partnerships | 15.4 | 15.2 | 28.3 | 25.9 |
| Minority interest in consolidated partnerships | (11.5) | (18.9) | (25.4) | (37.2) |
| Other income, net | 21.1 | 8.0 | 33.0 | 128.7 |
| Interest expense | (90.6) | (76.3) | (179.6) | (163.0) |
| Gain on exchange or disposal of assets and other | 176.6 | 188.3 | 176.6 | 188.3 |
| | | | | |
| Income from continuing operations before income taxes | 702.9 | 638.5 | 1,154.0 | 1,134.2 |
| Income taxes | 265.4 | 236.4 | 436.9 | 419.1 |
| | | | | |
| Income from continuing operations | 437.5 | 402.1 | 717.1 | 715.1 |
| Income (loss) from discontinued operations (net of income taxes of $2.3 million and $31.1million) | (8.6) | - | 9.2 | - |
| | | | | |
| Net income | 428.9 | 402.1 | 726.3 | 715.1 |
| Preferred dividends | - | 0.1 | - | 0.1 |
| Net income applicable to common shares | $ 428.9 | $ 402.0 | $ 726.3 | $ 715.0 |
| **Earnings per share:** | | | | |

| | | | | |
|---|---|---|---|---|
| Basic: | | | | |
| Income from continuing operations | $1.12 | $1.28 | $1.85 | $2.32 |
| Income (loss) from discontinued operations | (.02) | - | .02 | - |
| Net income | $1.10 | $1.28 | $1.87 | $2.32 |
| Diluted: | | | | |
| Income from continuing operations | $1.12 | $1.27 | $1.84 | $2.31 |
| Income (loss) from discontinued operations | (.02) | - | .02 | - |
| Net income | $1.10 | $1.27 | $1.86 | $2.31 |

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

**CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)**

| (Millions) | Six Months Ended June 30, 2006 | 2005 |
|---|---|---|
| **Cash Provided from Operations:** | | |
| Net income | $ 726.3 | $ 715.1 |
| Adjustments to reconcile net income to net cash provided from operations: | | |
| Income from discontinued operations | (9.2) | - |
| Depreciation and amortization | 816.4 | 689.5 |
| Provision for doubtful accounts | 123.6 | 90.7 |
| Non-cash portion of gain on exchange or disposal of assets and other | (107.6) | (202.2) |
| Change in deferred income taxes | 9.5 | 6.3 |
| Other, net | (4.3) | 11.1 |
| Changes in operating assets and liabilities, net of effects of acquisitions and dispositions: | | |
| Accounts receivable | (130.4) | (105.8) |
| Inventories | 72.8 | (2.3) |
| Accounts payable | (59.1) | (31.3) |
| Other current liabilities | (229.3) | 100.6 |
| Other, net | (45.0) | (28.1) |
| Net cash provided from operations | 1,163.7 | 1,243.6 |
| **Cash Flows from Investing Activities:** | | |
| Additions to property, plant and equipment | (598.2) | (611.1) |
| Additions to capitalized software development costs | (16.5) | (26.9) |
| Additions to investments | - | (0.9) |
| Purchases of property, net of cash acquired | (645.8) | (223.7) |
| Proceeds from the sale of assets | - | 36.2 |
| Proceeds from the sale of investments | 199.9 | 353.4 |
| Proceeds from the return on investments | 22.4 | 20.4 |
| Other, net | (8.4) | 3.1 |
| Net cash used in investing activities | (1,046.6) | (449.5) |
| **Cash Flows from Financing Activities:** | | |
| Dividends on common and preferred stock | (297.1) | (220.7) |
| Repayments of long-term debt | (0.9) | (452.9) |
| Conversion of convertible notes | (59.8) | - |
| Distributions to minority investors | (20.3) | (27.0) |
| Excess tax benefits from stock option exercises | 3.2 | - |
| Long-term debt issued | - | 50.0 |
| Common stock issued | 88.6 | 1,399.3 |
| Net cash provided from (used in) financing activities | (286.3) | 748.7 |
| **Cash Flows from Discontinued Operations:** | | |
| Cash provided from operating activities | 47.0 | - |
| Cash provided from investing activities | 1,669.1 | - |
| Cash provided from financing activities | 1.2 | - |
| Net cash provided from discontinued operations | 1,717.3 | - |

| | | | | |
|---|---|---|---|---|
| Effect of exchange rate changes on cash and short-term investments | | (5.9) | | - |
| Increase in cash and short-term investments | | 1,542.2 | | 1,542.8 |
| **Cash and Short-term Investments:** | | | | |
| Beginning of the period | | 989.2 | | 484.9 |
| End of the period | $ | 2,531.4 | $ | 2,027.7 |

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

**CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY (UNAUDITED)**

| (Millions) | Preferred Stock | Common Stock | Additional Paid-In Capital | Unrealized Holding Gain On Investments | Foreign Currency Translation Adjustment | Retained Earnings | Total |
|---|---|---|---|---|---|---|---|
| Balance at December 31, 2005 | $ 0.3 | $ 383.6 | $ 5,339.3 | $ 22.3 | $ (2.8) | $ 7,272.8 | $ 13,015.5 |
| Net income | - | - | - | - | - | 726.3 | 726.3 |
| Other comprehensive loss, net of tax: (See Note 12) | | | | | | | |
| Unrealized holding losses on investments, | | | | | | | |
| net of reclassification adjustments | - | - | - | 15.7 | - | - | 15.7 |
| Foreign currency translation adjustment | | | | | | | |
| net of reclassification adjustments | - | - | - | - | 2.8 | - | 2.8 |
| Comprehensive income | - | - | - | 15.7 | 2.8 | 726.3 | 744.8 |
| Employee plans, net | - | 2.2 | 85.8 | - | - | - | 88.0 |
| Restricted stock | - | 0.3 | - | - | - | - | 0.3 |
| Amortization of unearned compensation (See Note 2) | - | - | 17.5 | - | - | - | 17.5 |
| Tax benefit for non-qualified stock options | - | - | 4.7 | - | - | - | 4.7 |
| Conversion of convertible notes (See Note 3) | - | 3.5 | 36.7 | - | - | - | 40.2 |
| Dividends: | | | | | | | |
| Common - $.77 per share | - | - | - | - | - | (299.4) | (299.4) |
| Preferred | - | - | - | - | - | - | - |
| Balance at June 30, 2006 | $ 0.3 | $ 389.6 | $ 5,484.0 | $ 38.0 | $ - | $ 7,699.7 | $ 13,611.6 |

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

## NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

**1. General:**

Basis of Presentation - The consolidated financial statements at June 30, 2006 and December 31, 2005 and for the three and six month periods ended June 30, 2006 and 2005 of ALLTEL Corporation ("Alltel" or the "Company") are unaudited. The consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial reporting and Securities and Exchange Commission ("SEC") rules and regulations. Certain information and footnote disclosures have been condensed or omitted in accordance with those rules and regulations. The consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the interim periods presented.

**2. Accounting Changes:**

Change in Business Segment Reporting - Effective January 1, 2006, Alltel retrospectively changed its business segment reporting to exclude from wireless segment income the effects of amortization expense related to intangible assets recorded in connection with the acquisition of wireless properties. This amortization expense is now included in corporate expenses. The change in segment reporting reflected a first quarter 2006 decision by Alltel's management to evaluate the financial performance of the Company's wireless segment based on operating results that exclude the effects of amortization expense related to acquired intangible assets. Alltel's management, including the chief operating decision-maker, uses the revised measurement of wireless segment income consistently for all purposes, including internal reporting, evaluation of business objectives, opportunities and performance, resource allocation and the determination of management compensation. In accordance with Statement of Financial Accounting Standards ("SFAS") No. 131 "Disclosures about Segments of an Enterprise and Related Information", all prior period segment information has been reclassified to conform to this new financial reporting presentation.

Changes in Accounting Estimates - Effective April 1, 2006 and January 1, 2006, the Company prospectively reduced depreciation rates for its incumbent local exchange carrier operations in Alabama, North Carolina and Pennsylvania to reflect the results of studies of depreciable lives completed by Alltel during the first half of 2006. The depreciable lives were lengthened to reflect the estimated remaining useful lives of the wireline plant based on the Company's expected future network utilization and capital expenditure levels required to provide service to its customers. The effect of these changes resulted in decreases in depreciation expense of $8.0 million and $12.4 million, and increases in net income of $5.0 million and $7.7 million or $.01 and $.02 per share for the three and six months ended June 30, 2006, respectively.

Changes in Accounting Principle - In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 123(R), "Share-Based Payment", which is a revision of SFAS No. 123, "Accounting for Stock-Based Compensation" and supercedes Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees" and related Interpretations". On March 25, 2005, the SEC staff issued Staff Accounting Bulletin ("SAB") 107, which summarized the staff's views regarding the interaction between SFAS No. 123(R) and certain SEC rules and regulations and provided additional guidance regarding the valuation of share-based payment arrangements for public companies. SFAS No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be valued at fair value on the date of grant, and to be expensed over the employee's requisite service period. Effective January 1, 2006, the Company adopted the provisions of SFAS No. 123(R) using the modified prospective application method and applied the provisions of SAB 107 in its adoption of SFAS No. 123(R). Under the modified prospective transition method, Alltel is required to recognize compensation cost for all stock option awards granted after January 1, 2006 and for all existing awards for which the requisite service had not been rendered as of the date of adoption. Compensation expense for the unvested awards outstanding as of January 1, 2006 will be recognized over the remaining requisite service period based on the fair value of the awards on the date of grant, as previously calculated by Alltel in developing its pro forma disclosures in accordance with the provisions of SFAS No. 123. Operating results for prior periods have not been restated.

Upon adoption of SFAS No. 123(R), Alltel elected to continue to value its share-based payment transactions using a Black-Scholes valuation model, which was previously used by the Company for purposes of preparing the pro forma disclosures under SFAS No. 123. Under the provisions of SFAS No. 123(R), stock-based compensation expense recognized during the period is based on the portion of the share-based payment awards that is ultimately expected to vest. Accordingly, stock-based compensation expense recognized in the three and six months ended June 30, 2006 has been reduced for estimated forfeitures. SFAS No. 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Pre-vesting forfeitures were estimated to be 5.1 percent based on Alltel's historical experience. In the Company's pro forma information required under SFAS No. 123, Alltel accounted for forfeitures as they occurred.

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**2. Accounting Changes, Continued:**

Compensation expense for stock option awards granted after January 1, 2006 will be expensed using a straight-line single option method, which is the same attribution method that was used by Alltel for purposes of its pro forma disclosures under SFAS No. 123. Stock-based compensation expense recognized for the three and six months ended June 30, 2006 was as follows:

| (Millions, except per share amounts) | Three Months Ended | Six Months Ended |
|---|---|---|
| Compensation expense related to stock options issued by Alltel | $ 5.4 | $ 10.2 |
| Compensation expense related to stock options converted to Alltel stock options | | |
| in connection with the acquisition of Western Wireless Corporation | 0.5 | 1.0 |
| Compensation expense related to restricted stock awards | 2.6 | 6.3 |
| Compensation expense before income taxes | 8.5 | 17.5 |
| Income tax benefit | (2.6) | (5.4) |
| Compensation expense, net of tax | $ 5.9 | $ 12.1 |
| Earnings per share effects of compensation expense, net of tax | | |
| Basic earnings per share | $.02 | $.03 |
| Diluted earnings per share | $.02 | $.03 |

Comparatively, stock-based compensation expense recognized for the three and six months ended June 30, 2005 was $1.6 million and $3.2 million, consisting solely of expense related to restricted stock awards. Stock-based compensation expense is included in selling, general, administrative and other expenses within the Company's unaudited interim consolidated statements of income. For the three and six months ended June 30, 2006, stock-based compensation expense allocated to business segments totaled $7.0 million and $14.3 million to the wireless segment and $1.5 million and $2.4 million to the wireline segment, respectively. Stock-based compensation expense charged to corporate expenses totaled $0.8 million for the six months ended June 30, 2006. As presented in the table above, the effect of adopting SFAS No. 123(R) consisted of compensation expense for stock options issued by Alltel and resulted in pretax charges of $5.4 million and $10.2 million, which decreased net income $4.1 million and $7.7 million or $.01 per share and $.02 per share for the three and six months ended June 30, 2006, respectively.

Prior to adopting the provisions of SFAS No. 123(R), the Company recorded estimated compensation cost for employee stock options based upon the intrinsic value of the option on the date of grant consistent with the recognition and measurement principles of APB Opinion No. 25. Because Alltel had established the exercise price of its employee stock options based on the fair market value of the Company's stock at the date of grant, the stock options had no intrinsic value upon grant, and accordingly, Alltel did not record compensation expense for employee stock options prior to adopting SFAS No. 123(R). The following table illustrates the effects on net income and earnings per share had the Company applied the fair value recognition provisions of SFAS No. 123 to its stock-based employee compensation plans for the three and six months ended June 30, 2005:

| (Millions, except per share amounts) | Three Months Ended | Six Months Ended |
|---|---|---|
| Net income as reported | $ 402.1 | $ 715.1 |

| | | | | | |
|---|---|---|---|---|---|
| Add stock-based compensation expense included in | | | | | |
| net income, net of related tax effects | | | 1.0 | | 2.0 |
| Deduct stock-based employee compensation expense determined | | | | | |
| under fair value method for all awards, net of related tax effects | | | (6.4) | | (13.0) |
| Pro forma net income | | $ | 396.7 | $ | 704.1 |
| Basic earnings per share: | As reported | | $1.28 | | $2.32 |
| | Pro forma | | $1.26 | | $2.28 |
| Diluted earnings per share: | As reported | | $1.27 | | $2.31 |
| | Pro forma | | $1.26 | | $2.27 |

See Note 6 for a further discussion of the Company's stock-based compensation plans.

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**2. Accounting Changes, Continued:**

Effective January 1, 2005, the Company changed its accounting for operating leases with scheduled rent increases. Previously, Alltel had not recognized the scheduled increases in rent expense on a straight-line basis in accordance with the provisions of SFAS No. 13, “Accounting for Leases”, and FASB Technical Bulletin No. 85-3, “Accounting for Operating Leases with Scheduled Rent Increases”. The effect of this change, which is included in cost of services, was not material to Alltel’s 2005 or previously reported consolidated results of operations, financial position or cash flows.

**3. Acquisitions:**

On June 1, 2006, Alltel completed the purchase of wireless properties representing approximately 242,000 potential customers (“POPs”) in Virginia from Virginia Cellular, Inc. for $45.9 million in cash. Alltel has completed a preliminary purchase price allocation for this transaction based upon a fair value analysis of the net tangible and identifiable intangible assets acquired and assigned the excess of the aggregate purchase price over the fair market value of the tangible net assets acquired of $43.3 million to customer list ($9.5 million), cellular licenses ($7.2 million) and goodwill ($26.6 million). The Company expects substantially all of the goodwill and other identified intangible assets recorded in connection with this transaction will be deductible for income tax purposes. On May 1, 2006, Alltel completed the purchase of wireless properties representing approximately 485,000 POPs in Illinois from First Cellular of Southern Illinois for $140.9 million in cash. Alltel also has completed a preliminary purchase price allocation for this transaction based upon a fair value analysis of the net tangible and identifiable intangible assets acquired and assigned the excess of the aggregate purchase price over the fair market value of the tangible net assets acquired of $130.9 million to customer list ($20.0 million), cellular licenses ($15.5 million) and goodwill ($95.4 million). None of the goodwill and other identified intangible assets recorded in connection with this transaction will be deductible for income tax purposes. Given the close proximity to quarter end that these transactions were completed, the values of certain assets and liabilities have been based on preliminary valuations and are subject to adjustment as additional information is obtained. Accordingly, the purchase price allocations are subject to adjustment based upon the final determination of fair values.

On March 16, 2006, Alltel purchased from Palmetto MobileNet, L.P. for $456.3 million in cash the remaining ownership interests in ten wireless partnerships that cover approximately 2.0 million POPs in North and South Carolina. Prior to this transaction, Alltel owned a 50 percent interest in each of the ten wireless partnerships. During the second quarter of 2006, Alltel completed the purchase price allocation for this transaction based upon a fair value analysis of the net tangible and identifiable intangible assets acquired and assigned the excess of the aggregate purchase price over the fair market value of the tangible net assets acquired of $408.9 million to customer list ($39.9 million), cellular licenses ($41.4 million) and goodwill ($327.6 million). During the first quarter of 2006, Alltel also acquired the remaining ownership interest in a wireless property in Wisconsin in which the Company owned a majority interest. In connection with this acquisition, the Company paid $2.6 million in cash and assigned the excess of the aggregate purchase price over the fair market value of the tangible net assets acquired of $1.0 million to goodwill. The Company expects the goodwill and other identified intangible assets recorded in connection with these first quarter 2006 acquisitions to be deductible for income tax purposes.

The customer lists recorded in connection with the transactions discussed above are being amortized over a five-year period using the sum-of-the-years digits method. The cellular licenses recorded in connection with these transactions are classified as indefinite-lived intangible assets and are not subject to amortization. For the acquisitions completed in the second quarter of 2006, Alltel paid a premium (i.e., goodwill) over the fair value of the net tangible and identified intangible assets acquired because the acquisitions expanded the Company’s wireless operations into new markets in Illinois and Virginia and added a combined 112,000 new customers to Alltel’s wireless customer base. For the acquisitions completed in the first quarter of 2006, Alltel paid a premium (i.e. goodwill) over the fair value of the net tangible and identifiable intangible assets acquired in order to gain full control over the day-to-day operations of the wireless markets in North Carolina, South Carolina and Wisconsin. In addition, Alltel will no longer incur certain general and administrative expenses, such as audit and legal fees, attributable to managing its relationship with the other partners. Unaudited pro forma financial information related to the Company's 2006 acquisitions has not been presented because these acquisitions, individually or in the aggregate were not material to the Company's consolidated results of operations for the interim periods ended June 30, 2006.

On August 1, 2005, Alltel and Western Wireless Corporation ("Western Wireless") completed the merger of Western Wireless into a wholly-owned subsidiary of Alltel. As a result of the merger, Alltel added approximately 1.3 million domestic wireless customers, adding wireless operations in nine new states, including California, Idaho, Minnesota, Montana, Nevada, North Dakota, South Dakota, Utah and Wyoming, and expanding its wireless operations in Arizona, Colorado, New Mexico and Texas. In the merger, each share of Western Wireless common stock was exchanged for 0.535 shares of Alltel common stock and $9.25 in cash unless the shareholder made an all-cash election, in which case the shareholder received $40 in cash. Western Wireless shareholders making an all-stock election were subject to proration and

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**3. Acquisitions, Continued:**

received approximately 0.539 shares of Alltel common stock and $9.18 in cash. In the aggregate, Alltel issued approximately 54.3 million shares of stock valued at $3,430.4 million and paid approximately $933.4 million in cash. Through its wholly-owned subsidiary that merged with Western Wireless, Alltel also assumed debt of approximately $2.1 billion and acquired cash of $12.6 million. On the date of closing, Alltel repaid approximately $1.3 billion of term loans representing all borrowings outstanding under Western Wireless' credit facility that, as a result of a change in control, became due and payable immediately upon the closing of the merger. On August 1, 2005, Alltel also announced a tender offer to purchase all of the issued and outstanding 9.25 percent senior notes due July 15, 2013 of Western Wireless, representing an aggregate principal amount of $600.0 million, as well as a related consent solicitation to amend the indenture governing the senior notes. During the third quarter of 2005, Alltel repurchased all $600.0 million of the senior notes.

As part of the acquisition, Alltel assumed $115.0 million of 4.625 percent convertible subordinated notes due 2023 that were issued by Western Wireless in June 2003 (the "Western Wireless notes"). Upon closing of the merger, each $1,000 principal amount of Western Wireless notes became convertible into 34.6144 shares of Alltel common stock and $598.47 in cash based on the mixed-election exchange ratio. During January and February 2006, an aggregate principal amount of $100.0 million of the Western Wireless notes were converted. As a result of the conversion, Alltel issued 3.5 million shares of its common stock and paid approximately $59.8 million in cash to holders of the Western Wireless notes.

During the first six months of 2006, Alltel adjusted the purchase price allocation related to the Western Wireless acquisition to reflect the resolution of a pre-acquisition contingency concerning universal service fund support that Western Wireless had received as an Eligible Telecommunications Carrier ("ETC") in the State of Kansas and to adjust certain income tax liabilities related to the international operations. The effects of these adjustments resulted in a reduction in goodwill of $65.0 million. During the first quarter of 2006, Alltel completed the integration of the domestic operations acquired from Western Wireless. In connection with this integration, the Company incurred integration expenses, principally consisting of costs for branding, signage, retail store redesigns and computer system conversions. (See Note 8 for a discussion of integration expenses recorded by Alltel during the first quarter of 2006). Employee termination benefits of $23.8 million, including involuntary severance and related benefits to be provided to 337 former Western Wireless employees, and employee retention bonuses of $7.4 million payable to approximately 1,150 former Western Wireless employees were recorded during 2005. These employee benefit costs were recognized in accordance with Emerging Issues Task Force Issue No. 95-3, "Recognition of Liabilities in Connection with a Purchase Business Combination", as liabilities assumed in the business combination. As of June 30, 2006, Alltel had paid $28.0 million in employee termination and retention benefits, and 292 of the scheduled employee terminations had been completed.

As a condition of receiving approval for the merger from the U.S. Department of Justice ("DOJ") and Federal Communications Commission ("FCC"), Alltel agreed to divest certain wireless operations of Western Wireless in 16 markets in Arkansas, Kansas and Nebraska, as well as the "Cellular One" brand. On December 19, 2005, Alltel completed an exchange of wireless properties with United States Cellular Corporation ("U.S. Cellular") that included a substantial portion of the divestiture requirements related to the Company's merger with Western Wireless. During December 2005, Alltel completed the sale of the Cellular One brand to Dobson Cellular Systems, Inc. and on March 24, 2006, Alltel completed the sale of the remaining market in Arkansas to Cingular Wireless LLC ("Cingular"). During 2005, Alltel completed the sales of Western Wireless' international operations in Georgia, Ghana and Ireland. On April 28, 2006, Alltel completed the sales of the Western Wireless international operations in Austria and Haiti. In June

2006, Alltel completed the dispositions of the remaining international operations acquired from Western Wireless in Bolivia, Côte d'Ivoire and Slovenia. Accordingly, the acquired international operations and interests of Western Wireless and the domestic markets required to be divested by Alltel have been classified as discontinued operations in the accompanying unaudited interim consolidated financial statements. (See Note 11).

Under terms of the agreement with U.S. Cellular, Alltel acquired two rural markets in Idaho that are adjacent to the Company's existing operations and received $48.2 million in cash in exchange for 15 rural markets in Kansas and Nebraska formerly owned by Western Wireless. During the second quarter of 2006, Alltel completed the purchase price allocation for this exchange based upon a fair value analysis of the tangible and identifiable intangible assets acquired and the wireless property interests relinquished. The excess of the aggregate purchase price over the fair market value of the tangible net assets acquired of $100.1 million was assigned to customer list, cellular licenses and goodwill. The customer list recorded in connection with this transaction is being amortized over a five-year period using the sum-of-the-years digits method. The cellular licenses are classified as indefinite-lived intangible assets and are not subject to amortization. The finalization of the purchase price allocation resulted in a reduction to the preliminary values assigned to cellular licenses ($1.5 million), customer list ($0.5 million), and acquired net tangible assets ($2.2 million) with an increase to goodwill ($4.2 million)

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**3. Acquisitions, Continued:**
compared to the corresponding values that had been previously recorded in the Company's consolidated balance sheet as of December 31, 2005.

The following unaudited pro forma consolidated results of operations of the Company for the three and six months ended June 30, 2005 assume that the acquisition of wireless properties from Western Wireless occurred as of January 1, 2005:

| (Millions, except per share amounts) | Three Months Ended | Six Months Ended |
|---|---|---|
| Revenues and sales | $ 2,518.0 | $ 4,884.5 |
| Income from continuing operations | $ 406.8 | $ 724.8 |
| Combined earnings per share from continuing operations: | | |
| Basic earnings per share | $1.07 | $1.93 |
| Diluted earning per share | $1.05 | $1.89 |
| Net income | $ 419.9 | $ 764.2 |
| Combined earnings per share: | | |
| Basic earnings per share | $1.10 | $2.04 |
| Diluted earning per share | $1.08 | $2.00 |

The pro forma amounts represent the historical operating results of the properties acquired from Western Wireless with appropriate adjustments that give effect to depreciation and amortization and interest expense. The pro forma amounts also give effect to the May 17, 2005 issuance of approximately 24.5 million shares of Alltel common stock to settle the purchase contract obligation related to the Company's outstanding equity units (see Note 5), the proceeds of which were used to finance the cash portion of the merger transaction and a portion of the repayment of Western Wireless' long-term debt. The pro forma amounts also include the effects of non-acquisition-related special charges and unusual items, as more fully discussed in Notes 9 and 10 below. The pro forma amounts are not necessarily indicative of the operating results that would have occurred if the Western Wireless properties had been operated by Alltel during the periods presented. In addition, the pro forma amounts do not reflect potential cost savings related to full network optimization and the redundant effect of selling and general and administrative expenses.

**4. Goodwill and Other Intangible Assets:**
Goodwill represents the excess of cost over the fair value of net identifiable tangible and intangible assets acquired through various business combinations. The Company has acquired identifiable intangible assets through its acquisitions of interests in various wireless and wireline properties. The cost of acquired entities at the date of the acquisition is allocated to identifiable assets, and the excess of the total purchase price over the amounts assigned to identifiable assets is recorded as goodwill. As of January 1, 2006, Alltel completed the annual impairment reviews of its goodwill and other indefinite-lived intangible assets and determined that no write-down in the carrying value of these assets was required. The changes in the carrying amount of goodwill by business segment for the six months ended June 30, 2006 were as follows:

| | Communications | | | |
|---|---|---|---|---|
| (Millions) | Wireless | Wireline | Support Services | Total |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Balance at December 31, 2005 | $ | 7,427.4 | $ | 1,247.6 | $ | 2.3 | $ | 8,677.3 |
| Acquired during the period | | 450.6 | | - | | - | | 450.6 |
| Other adjustments | | (60.8) | | - | | - | | (60.8) |
| Balance at June 30, 2006 | $ | 7,817.2 | $ | 1,247.6 | $ | 2.3 | $ | 9,067.1 |

The carrying values of indefinite-lived intangible assets other than goodwill were as follows:

| (Millions) | | June 30, 2006 | | December 31, 2005 |
|---|---|---|---|---|
| Cellular licenses | $ | 1,454.9 | $ | 1,392.3 |
| Personal Communications Services licenses | | 79.1 | | 79.1 |
| Franchise rights - wireline | | 265.0 | | 265.0 |
| | $ | 1,799.0 | $ | 1,736.4 |

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**4. Goodwill and Other Intangible Assets, Continued:**
Intangible assets subject to amortization were as follows:

| | June 30, 2006 | | |
|---|---|---|---|
| (Millions) | Gross Cost | Accumulated Amortization | Net Carrying Value |
| Customer lists | $ 829.3 | $ (424.1) | $ 405.2 |
| Franchise rights | 22.5 | (17.1) | 5.4 |
| Roaming agreement | 6.1 | (1.7) | 4.4 |
| | $ 857.9 | $ (442.9) | $ 415.0 |

| | December 31, 2005 | | |
|---|---|---|---|
| (Millions) | Gross Cost | Accumulated Amortization | Net Carrying Value |
| Customer lists | $ 760.4 | $ (329.2) | $ 431.2 |
| Franchise rights | 22.5 | (16.4) | 6.1 |
| Roaming agreement | 6.1 | (0.7) | 5.4 |
| | $ 789.0 | $ (346.3) | $ 442.7 |

Amortization expense for intangible assets subject to amortization was $49.1 million and $96.6 million for the three and six month periods ended June 30, 2006, compared to $16.7 million and $32.5 million for the same periods of 2005. Amortization expense for intangible assets subject to amortization is estimated to be $175.3 million in 2006, $137.6 million in 2007, $100.6 million in 2008, $56.4 million in 2009 and $26.8 million in 2010. See Note 3 for a discussion of the acquisitions completed during the first six months of 2006 that resulted in the recognition of goodwill and other intangible assets.

**5. Equity Units:**
During 2002, the Company issued and sold 27.7 million equity units in an underwritten public offering and received net proceeds of $1.34 billion. Each equity unit consisted of a corporate unit, with a $50 stated amount, comprised of a purchase contract and a $50 principal amount senior note. The purchase contract obligated the holder to purchase, and obligated Alltel to sell, on May 17, 2005, a variable number of newly-issued common shares of Alltel common stock for $50. The number of Alltel shares issued to the holders of each equity unit to settle the purchase contract was calculated by dividing $50 by the average closing price per share of Alltel's common stock for the 20 consecutive trading days that ended May 12, 2005. Upon settlement of the purchase contract obligation, Alltel received cash proceeds of approximately $1,385.0 million and delivered approximately 24.5 million shares of Alltel common stock in the aggregate to the holders of the equity units. The proceeds from the stock issuance were utilized to finance certain obligations associated with Alltel's merger with Western Wireless, as further discussed in Note 3. The $50 principal amount senior notes become payable on May 17, 2007. The senior notes accrued interest through February 17, 2005 at an initial annual rate of 6.25 percent. On February 17, 2005, Alltel completed a remarketing of the senior notes that reset the annual interest rate on the notes to 4.656 percent for periods subsequent to February 17, 2005. The proceeds of the remarketed senior notes were used to purchase a portfolio of U.S. Treasury securities that were pledged to secure the corporate unit holders' obligations under the purchase contract component of the corporate unit until settlement.

**6. Stock-Based Compensation:**

Under the Company's stock-based compensation plans, Alltel may grant fixed and performance-based incentive and non-qualified stock options, restricted stock, and other equity securities to officers and other management employees. The maximum number of shares of the Company's common stock that may be issued to officers and other management employees under all stock compensation plans in effect at June 30, 2006 was 30.0 million shares.

Stock Options - Fixed stock options granted under the stock-based compensation plans generally become exercisable over a period of one to five years after the date of grant. Certain fixed options granted in 2000 become exercisable in increments of 50%, 25% and 25% over a five-year period beginning three years after the date of grant. Under Alltel's stock option plan for non-employee directors (the "Directors' Plan"), the Company grants fixed, non-qualified stock options to directors for up to 1.0 million shares of common stock. Under the Directors' Plan, directors receive a one-time option grant to purchase 10,000 shares of common stock when they join the Board. Directors are also granted each year, on the date of the annual meeting of stockholders, an option to purchase a specified number of shares of common stock (currently 6,500 shares). Options granted under the Directors' Plan become exercisable the day immediately preceding the date of the first annual

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**6. Stock-Based Compensation, Continued:**

meeting of stockholders following the date of grant. For all plans, the exercise price of the option equals the market value of Alltel's common stock on the date of grant. For fixed stock options, the maximum term for each option granted is 10 years. The Company's practice has been to issue new shares of common stock upon the exercise of stock options.

The weighted average fair value of stock options granted during the six months ended June 30, 2006 was $18.55 per share using the Black-Scholes option-pricing model and the following weighted average assumptions:

| | |
|---|---|
| Expected life | 5.9 years |
| Expected volatility | 22.9% |
| Dividend yield | 0.8% |
| Risk-free interest rate | 4.5% |

The expected life assumption was determined based on the Company's historical stock option exercise experience using a rolling 10-year average for three separate groups of employees that exhibited similar historical exercise behavior. Alltel believes that its historical experience is the best estimate of future exercise patterns currently available. The expected volatility assumption was based on a combination of the implied volatility derived from publicly traded options to purchase Alltel common stock and the Company's historical common stock volatility. Implied volatility was derived from two-year traded options, while historical volatility was calculated using the weighted average of historical daily price changes of the Company's common stock over the most recent period equal to the expected life of the stock option on the date of grant. Alltel believes that estimating expected volatility based on a combination of implied and historical volatility is more representative of future stock price trends than using historical volatility alone.

The expected dividend yield was based on the Company's approved annual dividend rate in effect at the date of grant adjusted to reflect the expected reduction in Alltel's dividend rate from $1.54 to $.50 per share following the completion of the spin off of the Company's wireline operations to Alltel's shareholders (see Note 16). Future increases to the dividend rate were not included in the development of the dividend yield assumption because Alltel's board of directors has not approved any increase to the dividend rate following completion of the spin off.

The risk-free interest rate was determined using the implied yield currently available for zero-coupon U.S. government issues with a remaining term equal to the expected life of the stock options.

Activity under all of the Company's stock options plans for the six months ended June 30, 2006 was as follows:

| | (Thousands) Number of Shares | Weighted Average Price Per Share |
|---|---|---|
| Outstanding at December 31, 2005 | 17,316.5 | $53.94 |
| Granted | 1,357.1 | 63.25 |
| Exercised | (2,207.8) | 40.12 |
| Forfeited | (96.0) | 58.93 |
| Expired | (13.8) | 31.83 |
| Outstanding at June 30, 2006 | 16,356.0 | $56.57 |

| | | |
|---|---|---|
| Exercisable at end of period | 11,986.3 | $57.06 |

The total intrinsic value of stock options exercised during the six months ended June 30, 2006 was $52.8 million, and Alltel received $88.0 million in cash from the exercise of stock options. The total intrinsic value of stock options outstanding and exercisable as of June 30, 2006 was $94.6 million.

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**6. Stock-Based Compensation, Continued:**

The following is a summary of stock options outstanding and exercisable as of June 30, 2006:

| | Options Outstanding | | | Options Exercisable | |
|---|---|---|---|---|---|
| Range of Exercise Prices | (Thousands) Number of Shares | Weighted Average Remaining Contractual Life | Weighted Average Exercise Price Per Share | (Thousands) Number of Shares | Weighted Average Exercise Price Per Share |
| $ 7.57 - $14.71 | 209.4 | 3.7 years | $10.26 | 179.3 | $10.70 |
| $26.61 - $32.37 | 425.2 | 2.2 years | 31.92 | 371.3 | 31.86 |
| $33.88 - $37.75 | 1,104.2 | 1.2 years | 34.50 | 1,102.8 | 34.50 |
| $43.12 - $50.28 | 2,376.5 | 6.7 years | 48.41 | 1,213.5 | 47.89 |
| $50.81 - $58.46 | 4,144.5 | 6.7 years | 54.84 | 2,380.0 | 54.92 |
| $62.07 - $68.25 | 7,954.7 | 4.8 years | 65.23 | 6,597.9 | 65.64 |
| $70.75 - $73.13 | 141.5 | 3.2 years | 72.43 | 141.5 | 72.43 |
| | 16,356.0 | 5.2 years | $56.57 | 11,986.3 | $57.06 |

Non-vested stock options as of June 30, 2006 and changes during the six months ended June 30, 2006 were as follows:

| | (Thousands) Number of Shares | Weighted Average Price Per Share |
|---|---|---|
| Non-vested at December 31, 2005 | 5,051.4 | $51.94 |
| Granted | 1,357.1 | 63.25 |
| Vested | (2,000.3) | 52.40 |
| Forfeited | (38.5) | 52.80 |
| Non-vested at June 30, 2006 | 4,369.7 | $55.23 |

At June 30, 2006, the total unamortized compensation cost for non-vested stock option awards amounted to $50.1 million and is expected to be recognized over a weighted average period of 3.5 years. Unrecognized compensation expense for stock options was included in additional paid-in capital in the accompanying consolidated balance sheet and statement of shareholders' equity.

Restricted Stock - During 2006, 2005 and 2004, Alltel granted to certain senior management employees and non-employee directors restricted stock awards which had an aggregate fair value on the date of grant of $18.6 million, $11.1 million and $8.5 million, respectively. The cost of the restricted stock awards is determined based on the fair market value of the shares at the date of grant reduced by the $1.00 par value per share charged to the employee and is expensed ratably over the vesting period. The restricted shares granted to employees in 2006 will vest in equal increments over a three-year period following the date of grant, except for awards representing 96,000 shares, which will vest in increments of 40%, 30% and 30% over a five-year period beginning three years after the date of grant. The restricted shares granted to employees in 2005 vest three years from the date of grant, except that one-third of the restricted shares may vest after each of the first two-year anniversaries from the grant date if Alltel achieves a certain targeted total stockholder return for its peer group during the three-year period preceding each of those two years. The restricted shares granted to employees in 2004 will vest in equal increments over a three-year period following the date of grant. Restricted shares granted to non-employee directors vest one year from the date of grant.

Non-vested restricted stock activity for the six months ended June 30, 2006 was as follows:

| | Number of Shares | Weighted Average Fair Value Per Share |
|---|---|---|
| Non-vested at December 31, 2005 | 302,530 | $52.52 |
| Granted | 302,532 | 61.38 |
| Vested | (52,927) | 49.28 |
| Forfeited | (6,250) | 53.26 |
| Non-vested at June 30, 2006 | 545,885 | $57.74 |

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**6. Stock-Based Compensation, Continued:**

At June 30, 2006, unrecognized compensation expense for the restricted shares amounted to $21.5 million and was included in additional paid-in capital in the accompanying consolidated balance sheet and statement of shareholders' equity. The unrecognized compensation expense for the non-vested restricted shares at June 30, 2006 is expected to be recognized over a weighted average period of 3.7 years.

**7. Employee Benefit Plans and Postretirement Benefits Other Than Pensions:**

The Company maintains a qualified defined benefit pension plan, which covers substantially all employees. In December 2005, the qualified defined benefit pension plan was amended such that future benefit accruals for all eligible nonbargaining employees ceased as of December 31, 2005 (December 31, 2010 for employees who had attained age 40 with two years of service as of December 31, 2005). The Company also maintains a supplemental executive retirement plan that provides unfunded, non-qualified supplemental retirement benefits to a select group of management employees. In addition, Alltel has entered into individual retirement agreements with certain retired executives providing for unfunded supplemental pension benefits. Alltel funds the accrued costs of these plans as benefits are paid. The components of pension expense, including provision for executive retirement agreements, were as follows for the three and six month periods ended June 30:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| (Millions) | 2006 | 2005 | 2006 | 2005 |
| Benefits earned during the year | $ 5.1 | $ 8.3 | $ 11.8 | $ 16.7 |
| Interest cost on benefit obligation | 14.4 | 14.6 | 29.3 | 29.2 |
| Special termination benefits | 4.5 | - | 9.0 | - |
| Settlement and curtailment losses | 2.4 | - | 3.4 | - |
| Amortization of prior service cost | 0.4 | 0.2 | 0.5 | 0.3 |
| Recognized net actuarial loss | 6.8 | 7.7 | 15.2 | 15.3 |
| Expected return on plan assets | (21.0) | (20.7) | (41.9) | (41.4) |
| Net periodic benefit expense | $ 12.6 | $ 10.1 | $ 27.3 | $ 20.1 |

As further discussed in Note 16, on December 9, 2005, Alltel announced that it would spin off its wireline telecommunications business to its stockholders and merge it with Valor Communications Group, Inc. ("Valor"). Two former executive officers of Alltel, who were eligible to receive supplemental retirement benefits payable under the Company's supplemental executive retirement plan, joined the new wireline company formed in the merger of Alltel's wireline business with Valor. As a result, the supplemental executive retirement plan was amended to provide for the immediate pay out of the accrued supplemental retirement benefits earned by the two executives at the time the spin off was consummated. The special termination benefits payable to the two executives and the corresponding settlement and curtailment losses have been included in integration expenses and other charges within the Company's consolidated statement of income for the three and six months ended June 30, 2006. (See Note 8).

Alltel disclosed in its financial statements for the year ended December 31, 2005 that it expected to contribute $20.5 million for retirement benefits in 2006 consisting solely of amounts necessary to fund the expected benefit payments related to the unfunded supplemental retirement plans, a substantial portion of which are for payments to the two executives discussed above. Through June 30, 2006, Alltel had contributed $1.9 million to fund the supplemental retirement plans. Alltel does not expect that any contribution to the qualified defined pension plan calculated in accordance with the minimum funding requirements of the Employee Retirement Income Security Act of 1974 will be required in 2006. Future discretionary contributions to the plan will depend on various factors, including future investment performance, changes in future discount rates and changes in the demographics of the population participating in Alltel's qualified pension plan.

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**7. Employee Benefit Plans and Postretirement Benefits Other Than Pensions, Continued:**

The Company provides postretirement healthcare and life insurance benefits for eligible employees. Employees share in the cost of these benefits. The Company funds the accrued costs of these plans as benefits are paid. The components of postretirement expense were as follows for the three and six month periods ended June 30:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| (Millions) | 2006 | 2005 | 2006 | 2005 |
| Benefits earned during the year | $ 0.1 | $ 0.1 | $ 0.2 | $ 0.2 |
| Interest cost on benefit obligation | 3.4 | 3.5 | 6.7 | 7.0 |
| Amortization of transition obligation | 0.2 | 0.2 | 0.4 | 0.4 |
| Amortization of prior service cost | 0.4 | 0.5 | 0.9 | 1.0 |
| Recognized net actuarial loss | 1.6 | 1.7 | 3.2 | 3.4 |
| Expected return on plan assets | - | - | - | - |
| Net periodic benefit expense | $ 5.7 | $ 6.0 | $ 11.4 | $ 12.0 |

**8. Integration Expenses and Other Charges:**

A summary of the integration expenses and other charges recorded during the six months ended June 30, 2006 is as follows:

| (Millions) | Wireless | Wireline | Total |
|---|---|---|---|
| Rebranding and signage costs | $ 8.3 | $ - | $ 8.3 |
| Computer system conversion and other integration expenses | 2.5 | - | 2.5 |
| Costs associated with pending spin off of wireline operations | - | 20.7 | 20.7 |
| Total integration expenses and other charges | $ 10.8 | $ 20.7 | $ 31.5 |

In connection with the spin off and merger of Alltel's wireline business with Valor, Alltel incurred $20.7 million of incremental costs, primarily consisting of the $12.4 million of special termination benefits payable to the two executives and the corresponding settlement and curtailment losses previously discussed (see Note 7) and additional consulting and legal fees of $3.9 million. The remaining expenses included internal payroll and employee benefit costs, contracted services, relocation expenses and other costs incurred in preparation of separating the wireline operations from Alltel's internal customer billing and operational support systems. Of the total expenses incurred related to the spin-off transaction, $8.7 million were recorded in the first quarter of 2006 and $12.0 million were recorded in the second quarter.

In the first quarter of 2006, the Company incurred $10.8 million of integration expenses related to its acquisition of Western Wireless. These expenses consisted of $8.3 million of rebranding and signage costs and $2.5 million of system conversion and other integration costs. The system conversion and other integration expenses included internal payroll and employee benefit costs, contracted services, relocation expenses and other programming costs incurred in converting Western Wireless' customer billing and operational support systems to Alltel's internal systems, a process which was completed during March 2006.

The following is a summary of the activity related to the liabilities associated with the Company’s integration and other restructuring activities for the six months ended June 30, 2006:

| (Millions) | | |
|---|---|---|
| Balance, beginning of period | $ | 29.7 |
| Integration expenses and other charges recorded during the period | | 31.5 |
| Non-cash portion of integration expenses and other charges | | (0.7) |
| Cash outlays during the period | | (32.2) |
| Balance, end of period | $ | 28.3 |

At June 30, 2006, the remaining unpaid liability related to Alltel’s integration and restructuring activities consisted of investment banker, audit, consulting and legal fees of $28.2 million and lease and contract termination costs of $0.1 million, which were included in accounts payable and other current liabilities, respectively, in the accompanying consolidated balance sheet as of June 30, 2006. The integration expenses and other charges decreased net income $7.5 million and $20.2 million for the three and six months ended June 30, 2006, respectively.

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**9. Investments - Special Dividend:**

On March 28, 2005, Alltel received a special $10 per share cash dividend from Fidelity National Financial, Inc. ("Fidelity National") totaling $111.0 million, related to the shares of Fidelity National common stock received as partial consideration for the sale of Alltel's financial services business to Fidelity National on April 1, 2003. As further discussed in Note 10, on April 6, 2005, Alltel completed the sale of all of its shares of Fidelity National common stock. The special cash dividend was included in other income, net in the accompanying consolidated statement of income for the six months ended June 30, 2005.

**10. Gain on Exchange or Disposal of Assets and Other:**

On November 10, 2005, federal legislation was enacted that included provisions to dissolve and liquidate the assets of the Rural Telephone Bank ("RTB"). In connection with the dissolution and liquidation, during April 2006, the RTB redeemed all outstanding shares of its Class C stock. As a result, Alltel received liquidating cash distributions of $198.7 million in exchange for its $22.1 million investment in RTB Class C stock and recognized a pretax gain of $176.6 million. This transaction increased net income $107.6 million in the three and six month periods ended June 30, 2006.

As previously discussed in Note 3, on April 15, 2005, Alltel and Cingular exchanged certain wireless assets. In connection with this transaction, Alltel recorded a pretax gain of approximately $127.5 million. On April 6, 2005, Alltel completed the sale of all of its shares of Fidelity National common stock to Goldman Sachs for approximately $350.8 million and recognized a pretax gain of approximately $75.8 million. On April 8, 2005, Alltel redeemed all of the issued and outstanding 7.50 percent senior notes due March 1, 2006, representing an aggregate principal amount of $450.0 million. Concurrent with the debt redemption, Alltel also terminated the related pay variable/receive fixed, interest rate swap agreement that had been designated as a fair value hedge against the $450.0 million senior notes. In connection with the early termination of the debt and interest rate swap agreement, Alltel incurred net pretax termination fees of approximately $15.0 million. These transactions increased net income $118.0 million in the three and six month periods ended June 30, 2005.

**11. Discontinued Operations:**

As previously discussed in Note 3, as a condition of receiving approval for the merger with Western Wireless from the DOJ and the FCC, Alltel agreed to divest certain wireless operations of Western Wireless in 16 markets in Arkansas, Kansas and Nebraska, as well as the Cellular One brand. On December 19, 2005, Alltel completed an exchange of wireless properties with U.S. Cellular that included a substantial portion of the divestiture requirements related to the merger. In December 2005, Alltel sold the Cellular One brand to Dobson Cellular Systems, Inc., and on March 24, 2006, Alltel completed the sale of the remaining market in Arkansas to Cingular.

On September 15, 2005, Alltel completed the sale of Western Wireless' international operations in Georgia and Ghana for $51.7 million in cash. On November 23, 2005, Alltel completed the sale of Western Wireless' international operations in Ireland to a subsidiary of eircom Group plc, the Irish fixed-line telecommunications operator, for 420 million euros or approximately $518.6 million. On April 28, 2006, Alltel completed the sale of Western Wireless' international operations in Austria to T-Mobile Austria GmbH, a subsidiary of Deutsche Telekom for 1.3 billion euros or approximately $1.6 billion. On that same day, Alltel also completed the sale of the Western Wireless international operations in Haiti for $70.6 million in cash. On June 6, 2006, Alltel sold Western Wireless' international operations in Bolivia for $39.5 million in cash. During June 2006, Alltel also completed the disposition of the remaining international operations acquired from Western Wireless in Côte d'Ivoire and Slovenia. In connection with the sales of the international operations completed in the second quarter of 2006, Alltel recorded an after tax loss of $9.3 million.

There was no gain or loss realized upon the sales of the international operations in Georgia, Ghana and Ireland and the domestic markets in Arkansas, Kansas and Nebraska.

The acquired international operations and interests of Western Wireless and the domestic market in Arkansas to be divested by Alltel have been classified as discontinued operations in the Company’s interim consolidated financial statements for the periods ended June 30, 2006. Depreciation of long-lived assets related to the international operations and the domestic markets to be divested was not recorded subsequent to the completion of the merger.

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**11. Discontinued Operations, Continued:**

The following table includes certain summary income statement information related to the international operations and the domestic market in Arkansas to be divested reflected as discontinued operations for the three and six months ended June 30, 2006:

| (Millions) | Three Months Ended | Six Months Ended |
|---|---|---|
| Revenues and sales | $ 72.2 | $ 278.6 |
| Operating expenses | 62.0 | 216.6 |
| Operating income | 10.2 | 62.0 |
| Minority interest expense in unconsolidated entities | (1.5) | (6.0) |
| Loss on sale of discontinued operations | (14.8) | (14.8) |
| Other expense, net (a) | (0.2) | (0.9) |
| Pretax income (loss) from discontinued operations | (6.3) | 40.3 |
| Income tax expense (benefit) | 2.3 | 31.1 |
| Income (loss) from discontinued operations | $ (8.6) | $ 9.2 |

Notes:

(a) Except for a $50.0 million credit facility agreement with the Overseas Private Investment Corporation that was assumed by the buyer of the Bolivian operations, Alltel had no outstanding indebtedness directly related to the international operations that were acquired from Western Wireless, and accordingly, no additional interest expense was allocated to discontinued operations for the period presented.

**12. Other Comprehensive Income (Loss):**

Other comprehensive income (loss) consists of unrealized holding gains (losses) on investments in equity securities and foreign currency translation adjustments. Other comprehensive income (loss) was as follows for the three and six month periods ended June 30:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| (Millions) | 2006 | 2005 | 2006 | 2005 |
| Other comprehensive income (loss): | | | | |
| Unrealized holding gains (losses) on investments: | | | | |
| Unrealized holding gains (losses) arising in the period | $ 11.8 | $ (18.4) | $ 24.2 | $ (161.0) |
| Income tax expense (benefit) | 4.1 | (6.5) | 8.5 | (56.4) |
| | 7.7 | (11.9) | 15.7 | (104.6) |
| Reclassification adjustments for gains included | | | | |
| in net income for the period | - | (75.8) | - | (75.8) |
| Income tax expense | - | 26.5 | - | 26.5 |
| | - | (49.3) | - | (49.3) |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Net unrealized gains (losses) in the period | | 11.8 | | (94.2) | | 24.2 | | (236.8) |
| Income tax expense (benefit) | | 4.1 | | (33.0) | | 8.5 | | (82.9) |
| | | 7.7 | | (61.2) | | 15.7 | | (153.9) |
| | | | | | | | | |
| Foreign currency translation adjustment: | | | | | | | | |
| Translation adjustments for the period | | (19.7) | | - | | (2.1) | | - |
| Reclassification adjustments for losses included | | | | | | | | |
| in net income for the period | | 4.9 | | - | | 4.9 | | - |
| | | (14.8) | | - | | 2.8 | | - |
| | | | | | | | | |
| Other comprehensive income (loss) before tax | | (3.0) | | (94.2) | | 27.0 | | (236.8) |
| Income tax expense (benefit) | | 4.1 | | (33.0) | | 8.5 | | (82.9) |
| Other comprehensive income (loss) | $ | (7.1) | $ | (61.2) | $ | 18.5 | $ | (153.9) |

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

## 13. Earnings per Share:

Basic earnings per share of common stock was computed by dividing net income applicable to common shares by the weighted average number of common shares outstanding during each period. Diluted earnings per share reflects the potential dilution that could occur assuming conversion or exercise of all dilutive unexercised stock options and outstanding convertible debt, restricted and preferred stock. The dilutive effect of stock options was determined using the treasury stock method. Under the treasury stock method, the proceeds received from the exercise of stock options, the amount of compensation cost for future service not yet recognized by the Company and the amount of tax benefits that would be recorded in additional paid in capital when the stock options become deductible for income tax purposes are assumed to be used to repurchase shares of the Company’s common stock. The number of stock options that were not included in the computation of diluted earnings per share was approximately 8.8 million shares of common stock for both the three and six month periods ended June 30, 2006, respectively. Conversely, the number of stock options not included in the computation of diluted earnings per share was 7.1 million shares for both the three and six month periods ended June 30, 2005. A reconciliation of the net income and number of shares used in computing basic and diluted earnings per share was as follows for the three and six month periods ended June 30:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| (Millions, except per share amounts) | 2006 | 2005 | 2006 | 2005 |
| **Basic earnings per share:** | | | | |
| Income from continuing operations | $ 437.5 | $ 402.1 | $ 717.1 | $ 715.1 |
| Income (loss) from discontinued operations | (8.6) | - | 9.2 | - |
| Less preferred dividends | - | (0.1) | - | (0.1) |
| Net income applicable to common shares | $ 428.9 | $ 402.0 | $ 726.3 | $ 715.0 |
| Weighted average common shares outstanding for the period | 388.8 | 314.5 | 387.8 | 308.3 |
| Basic earnings per share: | | | | |
| From continuing operations | $1.12 | $1.28 | $1.85 | $2.32 |
| From discontinued operations | (.02) | - | .02 | - |
| Net income | $1.10 | $1.28 | $1.87 | $2.32 |
| **Diluted earnings per share:** | | | | |
| Net income applicable to common shares | $ 428.9 | $ 402.0 | $ 726.3 | $ 715.0 |
| Adjustment for interest expense on convertible notes, net of tax | 0.1 | - | 0.2 | - |
| Adjustment for convertible preferred stock dividends | - | 0.1 | - | 0.1 |
| Net income applicable to common shares assuming conversion of preferred stock and convertible notes | $ 429.0 | $ 402.1 | $ 726.5 | $ 715.1 |
| Weighted average common shares outstanding for the period | 388.8 | 314.5 | 387.8 | 308.3 |
| Increase in shares resulting from: | | | | |

| | | | | |
|---|---|---|---|---|
| Assumed exercise of stock options | 0.9 | 1.0 | 1.1 | 1.0 |
| Assumed conversion of convertible notes | 0.5 | - | 0.8 | - |
| Assumed conversion of preferred stock | 0.2 | 0.2 | 0.2 | 0.2 |
| Non-vested restricted stock awards | 0.1 | 0.1 | 0.1 | 0.1 |
| Weighted average common shares assuming conversion | 390.5 | 315.8 | 390.0 | 309.6 |
| Diluted earnings per share: | | | | |
| From continuing operations | $1.12 | $1.27 | $1.84 | $2.31 |
| From discontinued operations | (.02) | - | .02 | - |
| Net income | $1.10 | $1.27 | $1.86 | $2.31 |

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**14. Business Segment Information:**

Alltel manages its business operations based on differences in products and services. The Company evaluates performance of the segments based on segment income, which is computed as revenues and sales less operating expenses, excluding the effects of the items discussed in Notes 8 and 9, respectively. Items not allocated to the segments are included in corporate operations. In addition, as previously discussed in Note 2, effective January 1, 2006, Alltel retrospectively changed its business segment reporting to exclude from wireless segment income the effects of amortization expense related to intangible assets recorded in connection with the acquisition of wireless properties. As a result of this change, wireless segment income excludes pretax amortization expense of $47.0 million and $92.5 million for the three and six months ended June 30, 2006. Conversely, wireless segment income excludes pretax amortization expense of $14.7 million and $28.5 million for the three and six months ended June 30, 2005, respectively. This amortization expense is now included in corporate expenses. Segment operating results were as follows for the three and six month periods ended June 30:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| (Millions) | 2006 | 2005 | 2006 | 2005 |
| **Revenues and Sales from External Customers:** | | | | |
| Wireless | $ 1,857.5 | $ 1,453.8 | $ 3,613.4 | $ 2,804.2 |
| Wireline | 537.1 | 555.9 | 1,074.1 | 1,111.9 |
| Communications support services | 217.7 | 192.8 | 408.7 | 356.7 |
| Total business segments | $ 2,612.3 | $ 2,202.5 | $ 5,096.2 | $ 4,272.8 |
| **Intersegment Revenues and Sales:** | | | | |
| Wireless | $ 1.6 | $ 1.5 | $ 3.1 | $ 3.1 |
| Wireline | 43.9 | 39.2 | 82.3 | 76.8 |
| Communications support services | 69.0 | 68.4 | 128.9 | 129.2 |
| Total business segments | $ 114.5 | $ 109.1 | $ 214.3 | $ 209.1 |
| **Total Revenues and Sales:** | | | | |
| Wireless | $ 1,859.1 | $ 1,455.3 | $ 3,616.5 | $ 2,807.3 |
| Wireline | 581.0 | 595.1 | 1,156.4 | 1,188.7 |
| Communications support services | 286.7 | 261.2 | 537.6 | 485.9 |
| Total business segments | 2,726.8 | 2,311.6 | 5,310.5 | 4,481.9 |
| Less intercompany eliminations | (53.1) | (51.5) | (97.1) | (95.8) |
| Total revenues and sales | $ 2,673.7 | $ 2,260.1 | $ 5,213.4 | $ 4,386.1 |
| **Segment Income:** | | | | |
| Wireless | $ 392.1 | $ 321.6 | $ 747.6 | $ 606.9 |
| Wireline | 235.4 | 215.3 | 462.0 | 429.8 |
| Communications support services | 31.0 | 11.6 | 52.5 | 23.5 |
| Total segment income | 658.5 | 548.5 | 1,262.1 | 1,060.2 |
| Corporate expenses | (54.6) | (26.3) | (109.5) | (68.7) |
| Integration expenses and other charges | (12.0) | - | (31.5) | - |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Equity earnings in unconsolidated partnerships | | 15.4 | | 15.2 | | 28.3 | | 25.9 |
| Minority interest in consolidated partnerships | | (11.5) | | (18.9) | | (25.4) | | (37.2) |
| Other income, net | | 21.1 | | 8.0 | | 33.0 | | 128.7 |
| Interest expense | | (90.6) | | (76.3) | | (179.6) | | (163.0) |
| Gain on exchange or disposal of assets and other | | 176.6 | | 188.3 | | 176.6 | | 188.3 |
| Income from continuing operations before income taxes | $ | 702.9 | $ | 638.5 | $ | 1,154.0 | $ | 1,134.2 |

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**14. Business Segment Information, Continued:**

Segment assets were as follows:

| (Millions) | | June 30, , 2006 | | December 31,, 2005 |
|---|---|---|---|---|
| Wireless | $ | 15,570.4 | $ | 15,416.3 |
| Wireline | | 5,054.0 | | 4,878.6 |
| Communications support services | | 468.7 | | 533.5 |
| Total business segments | | 21,093.1 | | 20,828.4 |
| Corporate headquarters assets not allocated to segments | | 2,867.5 | | 1,270.1 |
| Assets held for sale | | - | | 1,951.2 |
| Less elimination of intersegment receivables | | (27.0) | | (36.6) |
| Total consolidated assets | $ | 23,933.6 | $ | 24,013.1 |

Supplemental information pertaining to the communications support services segment was as follows for the three and six month periods ended June 30:

| | Three Months Ended | | | | Six Months Ended | | | |
|---|---|---|---|---|---|---|---|---|
| (Millions) | | 2006 | | 2005 | | 2006 | | 2005 |
| **Revenues and Sales from External Customers:** | | | | | | | | |
| Product distribution | $ | 115.1 | $ | 96.3 | $ | 224.0 | $ | 183.9 |
| Long-distance and network management services | | 53.0 | | 48.8 | | 106.6 | | 95.8 |
| Directory publishing | | 45.5 | | 44.2 | | 70.0 | | 68.3 |
| Telecommunications information services | | 4.1 | | 3.5 | | 8.1 | | 8.7 |
| Total | $ | 217.7 | $ | 192.8 | $ | 408.7 | $ | 356.7 |
| | | | | | | | | |
| **Intersegment Revenues and Sales:** | | | | | | | | |
| Product distribution | $ | 35.3 | $ | 39.8 | $ | 65.9 | $ | 72.8 |
| Long-distance and network management services | | 30.5 | | 25.5 | | 57.9 | | 51.1 |
| Directory publishing | | 3.2 | | 3.1 | | 5.1 | | 5.3 |
| Telecommunications information services | | - | | - | | - | | - |
| Total | $ | 69.0 | $ | 68.4 | $ | 128.9 | $ | 129.2 |
| | | | | | | | | |
| **Total Revenues and Sales:** | | | | | | | | |
| Product distribution | $ | 150.4 | $ | 136.1 | $ | 289.9 | $ | 256.7 |
| Long-distance and network management services | | 83.5 | | 74.3 | | 164.5 | | 146.9 |
| Directory publishing | | 48.7 | | 47.3 | | 75.1 | | 73.6 |
| Telecommunications information services | | 4.1 | | 3.5 | | 8.1 | | 8.7 |
| Total revenues and sales | $ | 286.7 | $ | 261.2 | $ | 537.6 | $ | 485.9 |

**15. Pending Acquisition of Wireless Properties:**

On November 18, 2005, Alltel announced that it had entered into a definitive agreement to purchase Midwest Wireless Holdings of Mankato, Minnesota ("Midwest Wireless") for $1.075 billion in cash. Under terms of the agreement, Alltel will acquire wireless properties, including 850 MHz licenses and PCS spectrum covering approximately 2 million potential customers, network assets and approximately 400,000 customers in select markets in southern Minnesota, northern and eastern Iowa, and western Wisconsin. Closing of the transaction is contingent upon regulatory approval, including approval of the FCC and the termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and is expected to occur early in the fourth quarter of 2006.

**16. Subsequent Events:**

Spin Off of Wireline Business and Merger with Valor Communications Group, Inc. - On July 17, 2006, Alltel completed the spin off of the Company's wireline telecommunications business to its stockholders and the merger of that wireline business with Valor. The spin off included the majority of Alltel's communications support services, including directory publishing, information technology outsourcing services, retail long distance and the wireline sales portion of communications products. Pursuant to the plan of distribution and immediately prior to the effective time of the merger with Valor described below, Alltel contributed all of the assets of its wireline telecommunications business to ALLTEL Holding Corp. ("Alltel Holding" or "Spinco"), a wholly owned subsidiary of the Company, in exchange for: (i) the issuance to Alltel of Spinco common stock that was distributed on a pro rata basis to Alltel's stockholders as a tax free stock

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**16. Subsequent Events, Continued:**

dividend, (ii) the payment of a special dividend to Alltel in the amount of $2.3 billion and (iii) the distribution by Spinco to Alltel of certain Spinco debt securities. In connection with the distribution and merger with Valor, Spinco borrowed approximately $800 million through a new senior credit agreement. Spinco also issued debt securities in the private placement market to pay the special dividend and issued debt securities to Alltel, consisting of $1,746.0 million aggregate principal amount of 8.625 percent senior notes due 2016 (the “Spinco Securities”). The Spinco Securities were issued at a discount, and accordingly, at the date of distribution to Alltel, the Spinco Securities had a carrying value of $1,703.2 million (par value of $1,746.0 million less discount of $42.8 million). In connection with the spin off, Alltel also transferred to Spinco approximately $261.0 million of long-term debt that had been issued by the Company’s wireline subsidiaries.

Immediately after the consummation of the spin off, Alltel Holding merged with and into Valor, with Valor continuing as the surviving corporation. As a result of the merger, all of the issued and outstanding shares of Spinco common stock were converted into the right to receive an aggregate number of shares of common stock of Valor. Valor issued in the aggregate approximately 403 million shares of common stock to Alltel stockholders pursuant to the merger, or 1.0339267 shares of Valor common stock for each share of Spinco common stock outstanding as of the effective time of the merger. Upon completion of the merger, Alltel stockholders owned approximately 85 percent of the outstanding equity interests of the surviving corporation, which is named Windstream Corporation (“Windstream”), and the stockholders of Valor owned the remaining 15 percent of such equity interests. As a result of the merger, Windstream assumed approximately $4.2 billion of long-term debt.

In connection with the spin-off transaction, Alltel entered into an exchange agreement (the “Exchange Agreement”), with J.P. Morgan Securities Inc. and Merrill Lynch, Pierce, Fenner & Smith Inc. (together, the “Investment Banks”), and Spinco. Pursuant to the terms of the Exchange Agreement, Alltel agreed to transfer the Spinco Securities to the Investment Banks, in equal amounts, in exchange for the transfer by the Investment Banks to Alltel of all or a portion of the $1.0 billion aggregate principal amount of Alltel’s commercial paper held by the Investment Banks and all or a portion of the $686.6 million aggregate principal amount of Alltel’s 4.656 percent notes due May 17, 2007 held by the Investment Banks. On July 17, 2006, following the completion of the spin-off transaction, Alltel and the Investment Banks completed the exchange of debt securities pursuant to the terms of the Exchange Agreement. The Alltel debt securities exchanged consisted of $988.5 million of outstanding commercial paper borrowings and $685.1 million of Alltel’s 4.656 percent notes due May 17, 2007. The fair value of the Alltel debt obligations to be transferred by the Investment Banks to Alltel had an agreed upon fair market value of approximately $1,673.4 million on the date of the debt exchange. As part of the Exchange Agreement with the Investment Banks, Alltel incurred approximately $29.8 million of costs related to the exchange of its debt securities.

The number of Alltel common shares outstanding did not change as a result of the spin off. For employees and directors remaining with Alltel, the number of shares underlying any outstanding stock options and the related per share exercise price were adjusted to maintain both the aggregate fair market value of stock underlying the stock options and the relationship between the per share exercise price and the related per share market value, pursuant to the terms of the applicable Alltel equity incentive plans and taking into account the change in the market value of Alltel’s common stock as a result of the distribution. Alltel restricted stock awarded pursuant to Alltel’s equity incentive plans and held by employees and directors at the time of the distribution continued to represent the right to receive shares of Alltel common stock. In addition, the holders of these restricted shares received shares of Windstream common stock equivalent to the number of shares of Windstream common stock that was received with respect to each share of unrestricted Alltel common stock at the time of the distribution. As of the spin-off date, employees of the wireline business who transferred to Windstream held vested options to purchase approximately 1.5 million shares of Alltel common stock. The number of shares underlying these stock options and the related per share exercise price were also adjusted to maintain both the aggregate fair market value of stock underlying the stock options and the relationship between the per share exercise price and the related per share market value. Stock options held by employees of the wireline business who transferred to Windstream that were unvested at the date of distribution were cancelled.

**NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)**

**16. Subsequent Events, Continued:**

The following unaudited pro forma consolidated results of operations of Alltel for the three and six months ended June 30, 2006 and 2005, respectively, assume that the spin off of the wireline business occur