

AT&T INC.  
Form 10-Q  
November 03, 2017

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

FORM 10-Q

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

For the quarterly period ended September 30, 2017

or

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

For the transition period from        to

Commission File Number 1-8610

AT&T INC.

Incorporated under the laws of the State of Delaware  
I.R.S. Employer Identification Number 43-1301883

208 S. Akard St., Dallas, Texas 75202  
Telephone Number: (210) 821-4105

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X]

No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes [X]

No [ ]

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

Edgar Filing: AT&T INC. - Form 10-Q

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

If an emerging growth company, indicate by checkmark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Yes

No

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

Yes

No

At October 31, 2017, there were 6,139 million common shares outstanding.

---

## PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

AT&amp;T INC.

## CONSOLIDATED STATEMENTS OF INCOME

Dollars in millions except per share amounts

(Unaudited)

	Three months		Nine months ended	
	ended September 30, 2017	2016	September 30, 2017	2016
Operating Revenues				
Service	\$36,378	\$37,272	\$109,372	\$111,515
Equipment	3,290	3,618	9,498	10,430
Total operating revenues	39,668	40,890	118,870	121,945
Operating Expenses				
Cost of services and sales				
Equipment	4,191	4,455	12,177	13,090
Broadcast, programming and operations	5,284	4,909	15,156	14,239
Other cost of services (exclusive of depreciation and amortization shown separately below)	9,431	9,526	27,714	28,436
Selling, general and administrative	8,317	9,013	24,917	26,363
Depreciation and amortization	6,042	6,579	18,316	19,718
Total operating expenses	33,265	34,482	98,280	101,846
Operating Income	6,403	6,408	20,590	20,099
Other Income (Expense)				
Interest expense	(1,686 )	(1,224 )	(4,374 )	(3,689 )
Equity in net income (loss) of affiliates	11	16	(148 )	57
Other income (expense) – net	246	(7 )	354	154
Total other income (expense)	(1,429 )	(1,215 )	(4,168 )	(3,478 )
Income Before Income Taxes	4,974	5,193	16,422	16,621
Income tax expense	1,851	1,775	5,711	5,803
Net Income	3,123	3,418	10,711	10,818
Less: Net Income Attributable to Noncontrolling Interest	(94 )	(90 )	(298 )	(279 )
Net Income Attributable to AT&T	\$3,029	\$3,328	\$10,413	\$10,539
Basic Earnings Per Share Attributable to AT&T	\$0.49	\$0.54	\$1.69	\$1.70
Diluted Earnings Per Share Attributable to AT&T	\$0.49	\$0.54	\$1.69	\$1.70
Weighted Average Number of Common Shares				
Outstanding – Basic (in millions)	6,162	6,168	6,164	6,171
Weighted Average Number of Common Shares				
Outstanding – with Dilution (in millions)	6,182	6,189	6,184	6,191
Dividends Declared Per Common Share	\$0.49	\$0.48	\$1.47	\$1.44
See Notes to Consolidated Financial Statements.				

AT&T INC.  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Dollars in millions  
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
Net income	\$3,123	\$3,418	\$10,711	\$10,818
Other comprehensive income (loss), net of tax:				
Foreign currency:				
Foreign currency translation adjustment (includes \$10, \$21, \$6 and \$21 attributable to noncontrolling interest), net of taxes of \$74, \$(91), \$580 and \$35	151	(225 )	490	(51 )
Available-for-sale securities:				
Net unrealized gains (losses), net of taxes of \$28, \$28, \$72 and \$15	45	46	128	25
Reclassification adjustment included in net income, net of taxes of \$(50), \$(3), \$(54) and \$(3)	(79 )	(5 )	(86 )	(5 )
Cash flow hedges:				
Net unrealized gains (losses), net of taxes of \$178, \$240, \$(94) and \$99	330	446	(174 )	183
Reclassification adjustment included in net income, net of taxes of \$5, \$5, \$15 and \$15	10	10	29	29
Defined benefit postretirement plans:				
Net prior service credit arising during period, net of taxes of \$0, \$0, \$594 and \$0	-	-	969	-
Amortization of net prior service credit included in net income, net of taxes of \$(157), \$(131), \$(447) and \$(393)	(256 )	(215 )	(731 )	(644 )
Other comprehensive income (loss)	201	57	625	(463 )
Total comprehensive income	3,324	3,475	11,336	10,355
Less: Total comprehensive income attributable to noncontrolling interest	(104 )	(111 )	(304 )	(300 )
Total Comprehensive Income Attributable to AT&T	\$3,220	\$3,364	\$11,032	\$10,055

See Notes to Consolidated Financial Statements.

## AT&amp;T INC.

## CONSOLIDATED BALANCE SHEETS

Dollars in millions except per share amounts

	September 30, 2017 (Unaudited)	December 31, 2016
Assets		
Current Assets		
Cash and cash equivalents	\$ 48,499	\$ 5,788
Accounts receivable - net of allowances for doubtful accounts of \$741 and \$661	15,876	16,794
Prepaid expenses	1,258	1,555
Other current assets	10,724	14,232
Total current assets	76,357	38,369
Property, plant and equipment	326,240	319,648
Less: accumulated depreciation and amortization	(199,778 )	(194,749 )
Property, Plant and Equipment – Net	126,462	124,899
Goodwill	105,668	105,207
Licenses	96,071	94,176
Customer Lists and Relationships – Net	11,573	14,243
Other Intangible Assets – Net	7,775	8,441
Investments in Equity Affiliates	1,627	1,674
Other Assets	18,332	16,812
Total Assets	\$ 443,865	\$ 403,821
Liabilities and Stockholders' Equity		
Current Liabilities		
Debt maturing within one year	\$ 8,551	\$ 9,832
Accounts payable and accrued liabilities	28,928	31,138
Advanced billing and customer deposits	4,503	4,519
Accrued taxes	2,703	2,079
Dividends payable	3,008	3,008
Total current liabilities	47,693	50,576
Long-Term Debt	154,728	113,681
Deferred Credits and Other Noncurrent Liabilities		
Deferred income taxes	64,381	60,128
Postemployment benefit obligation	31,231	33,578
Other noncurrent liabilities	19,723	21,748
Total deferred credits and other noncurrent liabilities	115,335	115,454
Stockholders' Equity		
Common stock (\$1 par value, \$14,000,000,000 authorized at September 30, 2017 and December 31, 2016; issued 6,495,231,088 at September 30, 2017 and December 31, 2016)	6,495	6,495
Additional paid-in capital	89,527	89,604
Retained earnings	36,074	34,734
Treasury stock (355,897,357 at September 30, 2017 and 356,237,141 at December 31, 2016, at cost)	(12,716 )	(12,659 )
Accumulated other comprehensive income	5,580	4,961
Noncontrolling interest	1,149	975
Total stockholders' equity	126,109	124,110

Total Liabilities and Stockholders' Equity	\$ 443,865	\$ 403,821
See Notes to Consolidated Financial Statements.		

AT&T INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
Dollars in millions  
(Unaudited)

	Nine months ended September 30,	
	2017	2016
Operating Activities		
Net income	\$10,711	\$10,818
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	18,316	19,718
Undistributed loss (earnings) from investments in equity affiliates	171	(22 )
Provision for uncollectible accounts	1,216	1,036
Deferred income tax expense	3,254	3,011
Net loss (gain) from sale of investments, net of impairments	(114 )	(88 )
Actuarial loss (gain) on pension and postretirement benefits	(259 )	-
Changes in operating assets and liabilities:		
Accounts receivable	(652 )	(1,108 )
Other current assets	(106 )	1,805
Accounts payable and other accrued liabilities	(1,437 )	(1,173 )
Equipment installment receivables and related sales	1,116	207
Deferred fulfillment costs	(1,102 )	(1,883 )
Retirement benefit funding	(420 )	(770 )
Other - net	(1,420 )	(2,349 )
Total adjustments	18,563	18,384
Net Cash Provided by Operating Activities	29,274	29,202
Investing Activities		
Capital expenditures:		
Purchase of property and equipment	(15,756)	(15,283)
Interest during construction	(718 )	(669 )
Acquisitions, net of cash acquired	1,154	(2,922 )
Dispositions	56	184
(Purchases) sales of securities, net	(2 )	501
Net Cash Used in Investing Activities	(15,266)	(18,189)
Financing Activities		
Issuance of long-term debt	46,761	10,140
Repayment of long-term debt	(10,309)	(10,688)
Purchase of treasury stock	(460 )	(444 )
Issuance of treasury stock	26	137
Dividends paid	(9,030 )	(8,850 )
Other	1,715	(534 )
Net Cash Provided by (Used in) Financing Activities	28,703	(10,239)
Net increase in cash and cash equivalents	42,711	774
Cash and cash equivalents beginning of year	5,788	5,121
Cash and Cash Equivalents End of Period	\$48,499	\$5,895
Cash paid during the nine months ended September 30 for:		
Interest	\$5,031	\$4,430
Income taxes, net of refunds	\$1,861	\$3,166

See Notes to Consolidated Financial Statements.

5

---



AT&amp;T INC.

## CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

Dollars and shares in millions except per share amounts

(Unaudited)

	September 30, 2017	
	Shares	Amount
<b>Common Stock</b>		
Balance at beginning of year	6,495	\$6,495
Issuance of stock	-	-
Balance at end of period	6,495	\$6,495
<b>Additional Paid-In Capital</b>		
Balance at beginning of year		\$89,604
Issuance of treasury stock		4
Share-based payments		(81 )
Balance at end of period		\$89,527
<b>Retained Earnings</b>		
Balance at beginning of year		\$34,734
Net income attributable to AT&T (\$1.69 per diluted share)		10,413
Dividends to stockholders (\$1.47 per share)		(9,075 )
Other		2
Balance at end of period		\$36,074
<b>Treasury Stock</b>		
Balance at beginning of year	(356 )	\$(12,659 )
Repurchase and acquisition of common stock	(14 )	(530 )
Issuance of treasury stock	14	473
Balance at end of period	(356 )	\$(12,716 )
<b>Accumulated Other Comprehensive Income Attributable to AT&amp;T, net of tax</b>		
Balance at beginning of year		\$4,961
Other comprehensive income attributable to AT&T		619
Balance at end of period		\$5,580
<b>Noncontrolling Interest</b>		
Balance at beginning of year		\$975
Net income attributable to noncontrolling interest		298
Distributions		(270 )
Acquisition of noncontrolling interest		140
Translation adjustments attributable to noncontrolling interest, net of taxes		6
Balance at end of period		\$1,149
Total Stockholders' Equity at beginning of year		\$124,110
Total Stockholders' Equity at end of period		\$126,109
See Notes to Consolidated Financial Statements.		

AT&T INC.  
SEPTEMBER 30, 2017

For ease of reading, AT&T Inc. is referred to as "we," "AT&T" or the "Company" throughout this document, and the names of the particular subsidiaries and affiliates providing the services generally have been omitted. AT&T is a holding company whose subsidiaries and affiliates operate in the communications and digital entertainment services industry. Our subsidiaries and affiliates provide services and equipment that deliver voice, video and broadband services both domestically and internationally. You should read this document in conjunction with the consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2016. The results for the interim periods are not necessarily indicative of those for the full year.

In the tables throughout this document, percentage increases and decreases that are not considered meaningful are denoted with a dash.

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Dollars in millions except per share amounts

#### NOTE 1. PREPARATION OF INTERIM FINANCIAL STATEMENTS

**Basis of Presentation** These consolidated financial statements include all adjustments that are necessary to present fairly the results for the presented interim periods, consisting of normal recurring accruals and other items. The consolidated financial statements include the accounts of the Company and our subsidiaries and affiliates over which we exercise control.

All significant intercompany transactions are eliminated in the consolidation process. Investments in unconsolidated subsidiaries and partnerships where we have significant influence are accounted for under the equity method. Earnings from certain investments accounted for using the equity method are included for periods ended within up to one quarter of our period end. We also record our proportionate share of our equity method investees' other comprehensive income (OCI) items, including cumulative translation adjustments.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes, including estimates of probable losses and expenses. Actual results could differ from those estimates.

#### Recently Adopted Accounting Standards

**Income Taxes** As of January 1, 2017, we adopted Accounting Standards Update (ASU) No. 2016-16, "Income Taxes (Topic 740)" (ASU 2016-16), with modified retrospective application, resulting in our recognition of an immaterial adjustment to retained earnings. Under ASU 2016-16, we recognize the income tax effects of intercompany sales or transfers of assets other than inventory (e.g., intellectual property or property, plant and equipment) during the period of intercompany sale or transfer instead of the period of either sale or transfer to a third party or recognition of depreciation or impairment.

#### New Accounting Standards

**Pension and Other Postretirement Benefits** In March 2017, the Financial Accounting Standards Board (FASB) issued ASU No. 2017-07, "Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost" (ASU 2017-07), which changes the presentation of periodic benefit cost components. Under ASU 2017-07, we will continue to present service costs within our operating expenses but present amortization of prior service credits and other components of our net periodic benefit cost in "other income (expense) – net" in our consolidated statements of income. ASU 2017-07 is effective for annual

reporting periods beginning after December 15, 2017. See Note 5 for our components of net periodic benefit cost.

**Revenue Recognition** In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)" (ASC 606), and has modified the standard thereafter. This standard replaces existing revenue recognition rules with a comprehensive revenue measurement and recognition standard and expanded disclosure requirements. ASC 606, as amended, becomes effective for annual reporting periods beginning after December 15, 2017, at which point we plan to adopt the standard using the "modified retrospective method." Under that method, we will apply the rules to all open contracts existing as of January 1, 2018, recognizing in beginning retained earnings an adjustment for the cumulative effect of the change and providing additional disclosures comparing results to previous accounting standards.

AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

NOTE 2. EARNINGS PER SHARE

A reconciliation of the numerators and denominators of basic and diluted earnings per share for the three months and nine months ended September 30, 2017 and 2016, is shown in the table below:

	Three months ended September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
Numerators				
Numerator for basic earnings per share:				
Net Income	\$3,123	\$3,418	\$10,711	\$10,818
Less: Net income attributable to noncontrolling interest	(94 )	(90 )	(298 )	(279 )
Net Income attributable to AT&T	3,029	3,328	10,413	10,539
Dilutive potential common shares:				
Share-based payment	3	3	9	9
Numerator for diluted earnings per share	\$3,032	\$3,331	\$10,422	\$10,548
Denominators (000,000)				
Denominator for basic earnings per share:				
Weighted average number of common shares outstanding	6,162	6,168	6,164	6,171
Dilutive potential common shares:				
Share-based payment (in shares)	20	21	20	20
Denominator for diluted earnings per share	6,182	6,189	6,184	6,191
Basic earnings per share attributable to AT&T	\$0.49	\$0.54	\$1.69	\$1.70
Diluted earnings per share attributable to AT&T	\$0.49	\$0.54	\$1.69	\$1.70

AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

NOTE 3. OTHER COMPREHENSIVE INCOME

Changes in the balances of each component included in accumulated other comprehensive income (accumulated OCI) are presented below. All amounts are net of tax and exclude noncontrolling interest.

	Foreign Currency Translation Adjustment	Net Unrealized Gains (Losses) on Available-for-Sale Securities	Net Unrealized Gains (Losses) on Cash Flow Hedges	Defined Benefit Postretirement Plans	Accumulated Other Comprehensive Income
Balance as of December 31, 2016	\$ (1,995)	\$ 541	\$ 744	\$ 5,671	\$ 4,961
Other comprehensive income (loss) before reclassifications	484	128	(174)	969	1,407
Amounts reclassified from accumulated OCI	-	<sup>1</sup> (86)	<sup>1</sup> 29	<sup>2</sup> (731)	<sup>3</sup> (788)
Net other comprehensive income (loss)	484	42	(145)	238	619
Balance as of September 30, 2017	\$ (1,511)	\$ 583	\$ 599	\$ 5,909	\$ 5,580

	Foreign Currency Translation Adjustment	Net Unrealized Gains (Losses) on Available-for-Sale Securities	Net Unrealized Gains (Losses) on Cash Flow Hedges	Defined Benefit Postretirement Plans	Accumulated Other Comprehensive Income
Balance as of December 31, 2015	\$ (1,198)	\$ 484	\$ 16	\$ 6,032	\$ 5,334
Other comprehensive income	(72)	25	183	-	136

(loss) before reclassifications						
Amounts reclassified from accumulated OCI	-	<sup>1</sup> (5)	<sup>1</sup> 29	<sup>2</sup> (644)	<sup>3</sup> (620)	
Net other comprehensive income (loss)	(72)	20	212	(644)	(484)	
Balance as of September 30, 2016	\$ (1,270)	\$ 504	\$ 228	\$ 5,388	\$ 4,850	

<sup>1</sup> (Gains) losses are included in Other income (expense) - net in the consolidated statements of income.

<sup>2</sup> (Gains) losses are included in Interest expense in the consolidated statements of income (see Note 6).

<sup>3</sup> The amortization of prior service credits associated with postretirement benefits, net of amounts capitalized as part of construction labor, are included in Cost of services and sales and Selling, general and administrative in the consolidated statements of income (see Note 5).

#### NOTE 4. SEGMENT INFORMATION

Our segments are strategic business units that offer products and services to different customer segments over various technology platforms and/or in different geographies that are managed accordingly. We analyze our segments based on Segment Contribution, which consists of operating income, excluding acquisition-related costs and other significant items (as discussed below), and equity in net income (loss) of affiliates for investments managed within each segment. We have four reportable segments: (1) Business Solutions, (2) Entertainment Group, (3) Consumer Mobility and (4) International.

We also evaluate segment performance based on EBITDA and/or EBITDA margin, which is defined as Segment Contribution excluding equity in net income (loss) of affiliates and depreciation and amortization. We believe EBITDA to be a relevant and useful measurement to our investors as it is part of our internal management reporting and planning processes and it is an important metric that management uses to evaluate segment operating performance. EBITDA does not give effect

AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

to cash used for debt service requirements and thus does not reflect available funds for distributions, reinvestment or other discretionary uses. EBITDA margin is EBITDA divided by total revenues.

The Business Solutions segment provides services to business customers, including multinational companies; governmental and wholesale customers; and individual subscribers who purchase wireless services through employer-sponsored plans. We provide advanced IP-based services including Virtual Private Networks (VPN); Ethernet-related products and broadband, collectively referred to as fixed strategic services; as well as traditional data and voice products. We utilize our wireless and wired networks to provide a complete communications solution to our business customers.

The Entertainment Group segment provides video, internet, voice communication, and interactive and targeted advertising services to customers located in the United States or in U.S. territories. We utilize our copper and IP-based wired network and our satellite technology.

The Consumer Mobility segment provides nationwide wireless service to consumers, wholesale and resale wireless subscribers located in the United States or in U.S. territories. We utilize our network to provide voice and data services, including high-speed internet, video and home monitoring services over wireless devices.

The International segment provides entertainment services in Latin America and wireless services in Mexico. Video entertainment services are provided to primarily residential customers using satellite technology. We utilize our regional and national networks in Mexico to provide consumer and business customers with wireless data and voice communication services. Our international subsidiaries conduct business in their local currency, and operating results are converted to U.S. dollars using official exchange rates.

In reconciling items to consolidated operating income and income before income taxes, Corporate and Other includes: (1) operations that are not considered reportable segments and that are no longer integral to our operations or which we no longer actively market, and (2) impacts of corporate-wide decisions for which the individual segments are not being evaluated, including interest costs and expected return on plan assets for our pension and postretirement benefit plans.

Certain operating items are not allocated to our business segments, and those include:

Acquisition-related items which consists of (1) items associated with the merger and integration of acquired businesses and (2) the noncash amortization of intangible assets acquired in acquisitions.

Certain significant items which consists of (1) noncash actuarial gains and losses from pension and other postretirement benefits, (2) employee separation charges associated with voluntary and/or strategic offers, (3) losses resulting from abandonment or impairment of assets and (4) other items for which the segments are not being evaluated.

Interest expense and other income (expense) – net, are managed only on a total company basis and are, accordingly, reflected only in consolidated results.

Our operating assets are utilized by multiple segments and consist of our wireless and wired networks as well as our satellite fleet. Our domestic communications business strategies reflect bundled product offerings that increasingly cut across product lines and utilize our asset base. Therefore, asset information and capital expenditures by segment are

not presented. Depreciation is allocated based on asset utilization by segment.

10

---



AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

For the three months ended September 30, 2017

	Revenues	Operations and Support Expenses	EBITDA	Depreciation and Amortization	Operating Income (Loss)	Equity in Net Income (Loss) of Affiliates	Segment Contribution
Business Solutions	\$ 17,061	\$ 10,233	\$ 6,828	\$ 2,325	\$ 4,503	\$ -	\$ 4,503
Entertainment Group	12,648	9,953	2,695	1,379	1,316	(6 )	1,310
Consumer Mobility	7,748	4,551	3,197	877	2,320	-	2,320
International	2,099	1,937	162	304	(142 )	17	(125 )
Segment Total	39,556	26,674	12,882	4,885	7,997	\$ 11	\$ 8,008
Corporate and Other	201	89	112	21	91		
Acquisition-related items	-	134	(134 )	1,136	(1,270 )		
Certain significant items	(89 )	326	(415 )	-	(415 )		
AT&T Inc.	\$ 39,668	\$ 27,223	\$ 12,445	\$ 6,042	\$ 6,403		

For the nine months ended September 30, 2017

	Revenues	Operations and Support Expenses	EBITDA	Depreciation and Amortization	Operating Income (Loss)	Equity in Net Income (Loss) of Affiliates	Segment Contribution
Business Solutions	\$ 51,016	\$ 30,722	\$ 20,294	\$ 6,972	\$ 13,322	\$ -	\$ 13,322
Entertainment Group	37,953	29,112	8,841	4,256	4,585	(23 )	4,562
Consumer Mobility	23,279	13,599	9,680	2,621	7,059	-	7,059
International	6,054	5,468	586	905	(319 )	62	(257 )
Segment Total	118,302	78,901	39,401	14,754	24,647	\$ 39	\$ 24,686
Corporate and Other	657	397	260	54	206		
Acquisition-related items	-	622	(622 )	3,508	(4,130 )		
Certain significant items	(89 )	44	(133 )	-	(133 )		
AT&T Inc.	\$ 118,870	\$ 79,964	\$ 38,906	\$ 18,316	\$ 20,590		

AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

For the three months ended September 30, 2016

	Revenues	Operations and Support Expenses	EBITDA	Depreciation and Amortization	Operating Income (Loss)	Equity in Net Income (Loss) of Affiliates	Segment Contribution
Business Solutions	\$17,767	\$10,925	\$6,842	\$2,539	\$4,303	\$-	\$4,303
Entertainment Group	12,720	9,728	2,992	1,504	1,488	-	1,488
Consumer Mobility	8,267	4,751	3,516	944	2,572	-	2,572
International	1,879	1,640	239	293	(54)	1	(53)
Segment Total	40,633	27,044	13,589	5,280	8,309	\$1	\$8,310
Corporate and Other	270	270	-	17	(17)		
Acquisition-related items	-	290	(290)	1,282	(1,572)		
Certain significant items	(13)	299	(312)	-	(312)		
AT&T Inc.	\$40,890	\$27,903	\$12,987	\$6,579	\$6,408		

For the nine months ended September 30, 2016

	Revenues	Operations and Support Expenses	EBITDA	Depreciation and Amortization	Operating Income (Loss)	Equity in Net Income (Loss) of Affiliates	Segment Contribution
Business Solutions	\$52,955	\$32,584	\$20,371	\$7,568	\$12,803	\$-	\$12,803
Entertainment Group	38,089	28,875	9,214	4,481	4,733	1	4,734
Consumer Mobility	24,781	14,343	10,438	2,798	7,640	-	7,640
International	5,374	4,951	423	868	(445)	24	(421)
Segment Total	121,199	80,753	40,446	15,715	24,731	\$25	\$24,756
Corporate and Other	759	940	(181)	54	(235)		
Acquisition-related items	-	818	(818)	3,949	(4,767)		
Certain significant items	(13)	(383)	370	-	370		
AT&T Inc.	\$121,945	\$82,128	\$39,817	\$19,718	\$20,099		

AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

The following table is a reconciliation of Segment Contribution to "Income Before Income Taxes" reported on our consolidated statements of income.

	Three months ended		Nine months ended	
	September 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016
Business Solutions	\$4,503	\$4,303	\$13,322	\$12,803
Entertainment Group	1,310	1,488	4,562	4,734
Consumer Mobility	2,320	2,572	7,059	7,640
International	(125 )	(53 )	(257 )	(421 )
Segment Contribution	8,008	8,310	24,686	24,756
Reconciling Items:				
Corporate and Other	91	(17 )	206	(235 )
Merger and integration charges	(134 )	(290 )	(622 )	(818 )
Amortization of intangibles acquired	(1,136)	(1,282)	(3,508 )	(3,949 )
Actuarial gain (loss)	-	-	259	-
Employee separation costs	(208 )	(260 )	(268 )	(314 )
Gain (loss) on wireless spectrum transactions	-	(22 )	181	714
Natural disaster costs and revenue credits	(207 )	(30 )	(207 )	(30 )
Venezuela devaluation	-	-	(98 )	-
Segment equity in net (income) loss of affiliates	(11 )	(1 )	(39 )	(25 )
AT&T Operating Income	6,403	6,408	20,590	20,099
Interest expense	1,686	1,224	4,374	3,689
Equity in net income (loss) of affiliates	11	16	(148 )	57
Other income (expense) - net	246	(7 )	354	154
Income Before Income Taxes	\$4,974	\$5,193	\$16,422	\$16,621

NOTE 5. PENSION AND POSTRETIREMENT BENEFITS

Many of our employees are covered by one of our noncontributory pension plans. We also provide certain medical, dental, life insurance and death benefits to certain retired employees under various plans and accrue actuarially determined postretirement benefit costs. Our objective in funding these plans, in combination with the standards of the Employee Retirement Income Security Act of 1974, as amended (ERISA), is to accumulate assets sufficient to provide benefits described in the plans to employees upon their retirement.

In 2013, we made a voluntary contribution of a preferred equity interest in AT&T Mobility II LLC (Mobility II), the primary holding company for our domestic wireless business, to the pension trust used to pay benefits under our qualified pension plans. The preferred equity interest had a value of \$9,354 at September 30, 2017. The trust is entitled to receive cumulative cash distributions of \$560 per annum, which are distributed quarterly by Mobility II to the trust, in equal amounts and accounted for as contributions. Mobility II distributed \$420 to the trust during the nine months ended September 30, 2017. So long as those distributions are made, we will have no limitations on our ability to declare a dividend or repurchase shares. This preferred equity interest is a plan asset under ERISA and is

recognized as such in the plan's separate financial statements. However, because the preferred equity interest is not unconditionally transferable to an unrelated party, it is not reflected in plan assets in our consolidated financial statements and instead has been eliminated in consolidation.

The preferred equity interest is not transferable by the trust except through its put and call features. In early September 2017, AT&T notified the trust and the fiduciary of the preferred equity interest that AT&T committed that it would not exercise its call option of the preferred interest until at least September 9, 2022, which resulted in an increase in the fair value of the preferred interest of approximately \$1,245.

AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

We recognize actuarial gains and losses on pension and postretirement plan assets in our operating results at our annual measurement date of December 31, unless earlier remeasurements are required. During the second quarter of 2017, a substantive plan change involving the frequency of considering potential health reimbursement account credit increases was communicated to our retirees. This plan change triggered a remeasurement of our postretirement obligations and resulted in additional prior service credits recognized in other comprehensive income, reducing our liability by \$1,563. Such credits amortize through earnings over a period approximating the average service period to full eligibility. Upon our adoption of ASU 2017-07, the amortization of these prior service credits will be recorded in other income (expense) – net.

The following table details pension and postretirement benefit costs included in operating expenses in the accompanying consolidated statements of income. A portion of these expenses is capitalized as part of internal construction projects, providing a small reduction in the net expense recorded. Service costs and prior service credits are reported in our segment results while interest costs and expected return on plan assets are included with Corporate and Other (see Note 4).

	Three months ended September 30, 2017		Nine months ended September 30, 2016	
Pension cost:				
Service cost – benefits earned during the period	\$282	\$278	\$846	\$834
Interest cost on projected benefit obligation	484	495	1,452	1,485
Expected return on assets	(783)	(778)	(2,350)	(2,336)
Amortization of prior service credit	(31 )	(26 )	(93 )	(77 )
Net pension (credit) cost	\$(48 )	\$(31 )	\$(145 )	\$(94 )
Postretirement cost:				
Service cost – benefits earned during the period	\$32	\$48	\$107	\$144
Interest cost on accumulated postretirement benefit obligation	193	243	617	729
Expected return on assets	(81 )	(88 )	(240 )	(266 )
Amortization of prior service credit	(382)	(320)	(1,084)	(958 )
Actuarial (gain) loss	-	-	(259 )	-
Net postretirement (credit) cost	\$(238)	\$(117)	\$(859 )	\$(351 )
Combined net pension and postretirement (credit) cost	\$(286)	\$(148)	\$(1,004)	\$(445 )

As part of our second-quarter 2017 remeasurement, we decreased the weighted-average discount rate used to measure our postretirement benefit obligation to 4.10%. The discount rate in effect for determining postretirement service and interest costs after remeasurement is 4.50% and 3.30%, respectively.

We also provide senior- and middle-management employees with nonqualified, unfunded supplemental retirement and savings plans. For the third quarter ended 2017 and 2016, net supplemental pension benefits costs not included in the table above were \$22 and \$23. For the first nine months of 2017 and 2016, net supplemental pension benefit costs were \$67 and \$70.



AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

NOTE 6. FAIR VALUE MEASUREMENTS AND DISCLOSURE

The Fair Value Measurement and Disclosure framework provides a three-tiered fair value hierarchy that gives highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that we have the ability to access.

Level 2 Inputs to the valuation methodology include:

- Quoted prices for similar assets and liabilities in active markets.
- Quoted prices for identical or similar assets or liabilities in inactive markets.
- Inputs other than quoted market prices that are observable for the asset or liability.
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

- Fair value is often based on developed models in which there are few, if any, external observations.

The fair value measurements level of an asset or liability within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Our valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs.

The valuation methodologies described above may produce a fair value calculation that may not be indicative of future net realizable value or reflective of future fair values. We believe our valuation methods are appropriate and consistent with other market participants. The use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date. There have been no changes in the methodologies used since December 31, 2016.

Long-Term Debt and Other Financial Instruments

The carrying amounts and estimated fair values of our long-term debt, including current maturities, and other financial instruments, are summarized as follows:

	September 30, 2017		December 31, 2016	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Notes and debentures <sup>1</sup>	\$162,450	\$171,025	\$122,381	\$128,726
Bank borrowings	2	2	4	4
Investment securities	2,565	2,565	2,587	2,587

<sup>1</sup> Includes credit agreement borrowings.

The carrying amount of debt with an original maturity of less than one year approximates market value. The fair value measurements used for notes and debentures are considered Level 2 and are determined using various methods, including quoted prices for identical or similar securities in both active and inactive markets.





AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

Following is the fair value leveling for available-for-sale securities and derivatives as of September 30, 2017 and December 31, 2016:

	September 30, 2017			
	Level		Level	Total
	1	Level 2	3	
<b>Available-for-Sale Securities</b>				
Domestic equities	\$1,274	\$-	\$ -	\$1,274
International equities	380	-	-	380
Fixed income bonds	-	659	-	659
<b>Asset Derivatives <sup>1</sup></b>				
Interest rate swaps	-	45	-	45
Cross-currency swaps	-	967	-	967
<b>Liability Derivatives <sup>1</sup></b>				
Interest rate swaps	-	(34 )	-	(34 )
Cross-currency swaps	-	(1,809)	-	(1,809)

<sup>1</sup> Derivatives designated as hedging instruments are reflected as "Other assets," "Other noncurrent liabilities" and, for a portion of interest rate swaps, "Other current assets" in our consolidated balance sheets.

	December 31, 2016			
	Level		Level	Total
	1	Level 2	3	
<b>Available-for-Sale Securities</b>				
Domestic equities	\$1,215	\$-	\$ -	\$1,215
International equities	594	-	-	594
Fixed income bonds	-	508	-	508
<b>Asset Derivatives <sup>1</sup></b>				
Interest rate swaps	-	79	-	79
Cross-currency swaps	-	89	-	89
<b>Liability Derivatives <sup>1</sup></b>				
Interest rate swaps	-	(14 )	-	(14 )
Cross-currency swaps	-	(3,867)	-	(3,867)

<sup>1</sup> Derivatives designated as hedging instruments are reflected as "Other assets," "Other noncurrent liabilities" and, for a portion of interest rate swaps, "Other current assets" in our consolidated balance sheets.

**Investment Securities**

Our investment securities include equities, fixed income bonds and other securities. A substantial portion of the fair values of our available-for-sale securities was estimated based on quoted market prices. Investments in securities not traded on a national securities exchange are valued using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. Realized gains and losses on securities are included in "Other income

(expense) – net" in the consolidated statements of income using the specific identification method. Unrealized gains and losses, net of tax, on available-for-sale securities are recorded in accumulated OCI. Unrealized losses that are considered other than temporary are recorded in "Other income (expense) – net" with the corresponding reduction to the carrying basis of the investment. Fixed income investments of \$509 have maturities of less than one year, \$33 within one to three years, \$32 within three to five years and \$85 for five or more years.

Our cash equivalents (money market securities), short-term investments (certificate and time deposits) and nonrefundable customer deposits are recorded at amortized cost, and the respective carrying amounts approximate fair values. Short-term investments and nonrefundable customer deposits are recorded in "Other current assets" and our investment securities are recorded in "Other Assets" on the consolidated balance sheets.

AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

Derivative Financial Instruments

We enter into derivative transactions to manage certain market risks, primarily interest rate risk and foreign currency exchange risk. This includes the use of interest rate swaps, interest rate locks, foreign exchange forward contracts and combined interest rate foreign exchange contracts (cross-currency swaps). We do not use derivatives for trading or speculative purposes. We record derivatives on our consolidated balance sheets at fair value that is derived from observable market data, including yield curves and foreign exchange rates (all of our derivatives are Level 2). Cash flows associated with derivative instruments are presented in the same category on the consolidated statements of cash flows as the item being hedged.

**Fair Value Hedging** We designate our fixed-to-floating interest rate swaps as fair value hedges. The purpose of these swaps is to manage interest rate risk by managing our mix of fixed-rate and floating-rate debt. These swaps involve the receipt of fixed-rate amounts for floating interest rate payments over the life of the swaps without exchange of the underlying principal amount. Accrued and realized gains or losses from interest rate swaps impact interest expense in the consolidated statements of income. Unrealized gains on interest rate swaps are recorded at fair market value as assets, and unrealized losses on interest rate swaps are recorded at fair market value as liabilities. Changes in the fair values of the interest rate swaps are exactly offset by changes in the fair value of the underlying debt. Gains or losses realized upon early termination of our fair value hedges are recognized in interest expense. In the nine months ended September 30, 2017 and September 30, 2016, no ineffectiveness was measured on interest rate swaps designated as fair value hedges.

**Cash Flow Hedging** We designate our cross-currency swaps as cash flow hedges. We have entered into multiple cross-currency swaps to hedge our exposure to variability in expected future cash flows that are attributable to foreign currency risk generated from the issuance of our Euro, British pound sterling, Canadian dollar and Swiss franc denominated debt. These agreements include initial and final exchanges of principal from fixed foreign currency denominated amounts to fixed U.S. dollar denominated amounts, to be exchanged at a specified rate that is usually determined by the market spot rate upon issuance. They also include an interest rate swap of a fixed or floating foreign currency-denominated rate to a fixed U.S. dollar denominated interest rate.

Unrealized gains on derivatives designated as cash flow hedges are recorded at fair value as assets, and unrealized losses on derivatives designated as cash flow hedges are recorded at fair value as liabilities. For derivative instruments designated as cash flow hedges, the effective portion is reported as a component of accumulated OCI until reclassified into interest expense in the same period the hedged transaction affects earnings. The gain or loss on the ineffective portion is recognized as "Other income (expense) – net" in the consolidated statements of income in each period. We evaluate the effectiveness of our cross-currency swaps each quarter. In the nine months ended September 30, 2017 and September 30, 2016, no ineffectiveness was measured on cross-currency swaps designated as cash flow hedges.

Periodically, we enter into and designate interest rate locks to partially hedge the risk of changes in interest payments attributable to increases in the benchmark interest rate during the period leading up to the probable issuance of fixed-rate debt. We designate our interest rate locks as cash flow hedges. Gains and losses when we settle our interest rate locks are amortized into income over the life of the related debt, except where a material amount is deemed to be ineffective, which would be immediately reclassified to "Other income (expense) – net" in the consolidated statements of income. Over the next 12 months, we expect to reclassify \$59 from accumulated OCI to interest expense due to the amortization of net losses on historical interest rate locks.

We hedge a portion of the exchange risk involved in anticipation of highly probable foreign currency-denominated transactions. In anticipation of these transactions, we often enter into foreign exchange contracts to provide currency at a fixed rate. Gains and losses at the time we settle or take delivery on our designated foreign exchange contracts are amortized into income in the same period the hedged transaction affects earnings, except where an amount is deemed to be ineffective, which would be immediately reclassified to "Other income (expense) – net" in the consolidated statements of income. In the nine months ended September 30, 2017 and September 30, 2016, no ineffectiveness was measured on foreign exchange contracts designated as cash flow hedges.

*Collateral and Credit-Risk Contingency* We have entered into agreements with our derivative counterparties establishing collateral thresholds based on respective credit ratings and netting agreements. At September 30, 2017, we had posted

17

---

AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

collateral of \$837 (a deposit asset) and held collateral of \$338 (a receipt liability). Under the agreements, if AT&T's credit rating had been downgraded one rating level by Fitch Ratings, before the final collateral exchange in September, we would have been required to post additional collateral of \$141. If DIRECTV Holdings LLC's credit rating had been downgraded below BBB- (S&P), we would have been required to post additional collateral of \$221. At December 31, 2016, we had posted collateral of \$3,242 (a deposit asset) and held no collateral. We do not offset the fair value of collateral, whether the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) exists, against the fair value of the derivative instruments.

Following are the notional amounts of our outstanding derivative positions:

	September 30, 2017	December 31, 2016
Interest rate swaps	\$ 10,775	\$ 9,650
Cross-currency swaps	38,694	29,642
Total	\$ 49,469	\$ 39,292

Following are the related hedged items affecting our financial position and performance:

Effect of Derivatives on the Consolidated  
Statements of Income

	Three months ended September 30, 2017		Nine months ended September 30, 2016	
Fair Value Hedging Relationships	2017	2016	2017	2016
Interest rate swaps (Interest expense):				
Gain (Loss) on interest rate swaps	\$(3)	\$(54)	\$(51)	\$17
Gain (Loss) on long-term debt	3	54	51	(17)

In addition, the net swap settlements that accrued and settled in the quarter ended September 30 were offset against interest expense.

	Three months ended September 30, 2017		Nine months ended September 30, 2016	
Cash Flow Hedging Relationships	2017	2016	2017	2016
Cross-currency swaps:				
Gain (Loss) recognized in accumulated OCI	\$ 429	\$ 686	\$(268)	\$ 282

Interest rate locks:

Gain (Loss) recognized in accumulated OCI	79	-	-	-
Interest income (expense) reclassified from accumulated OCI into income	(15)	(15)	(44)	(44)

NOTE 7. ACQUISITIONS, DISPOSITIONS AND OTHER ADJUSTMENTS

Acquisitions

Auction 1000 On April 13, 2017, the Federal Communications Commission (FCC) announced that we were the successful bidder for \$910 of spectrum in 18 markets. We provided the FCC an initial deposit of \$2,348 in July 2016 and received a refund of \$1,438 in April 2017, which was recorded as cash from investing activities on our consolidated statements of cash flows.

AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

Dispositions

YP Holdings LLC In June 2017, YP Holdings LLC was acquired by Dex Media. Our results include a gain of \$36 for our portion of the proceeds.

Pending Acquisitions

Time Warner Inc. On October 22, 2016, we entered into and announced a merger agreement (Merger Agreement) to acquire Time Warner Inc. (Time Warner) in a 50% cash and 50% stock transaction for \$107.50 per share of Time Warner common stock, or approximately \$85,400 at the date of the announcement (Merger). Combined with Time Warner's net debt at September 30, 2017, the total transaction value is approximately \$105,834. Each share of Time Warner common stock will be exchanged for \$53.75 per share in cash and a number of shares of AT&T common stock equal to the exchange ratio. If the average stock price (as defined in the Merger Agreement) at the time of closing the Merger is between (or equal to) \$37.411 and \$41.349 per share, the exchange ratio will be the quotient of \$53.75 divided by the average stock price. If the average stock price is greater than \$41.349, the exchange ratio will be 1.300. If the average stock price is less than \$37.411, the exchange ratio will be 1.437. Post-transaction, Time Warner shareholders will own between 14.4% and 15.7% of AT&T shares on a fully-diluted basis based on the number of AT&T shares outstanding. The cash portion of the purchase price will be financed with new debt and cash.

Time Warner is a global leader in media and entertainment whose major businesses encompass an array of some of the most respected and successful media brands. The deal combines Time Warner's vast library of content and ability to create new premium content for audiences around the world with our extensive customer relationships and distribution, one of the world's largest pay-TV subscriber bases and leading scale in TV, mobile and broadband distribution.

The Merger Agreement was approved by Time Warner shareholders on February 15, 2017. The transaction has been approved by all requisite foreign jurisdictions and remains subject to review by the U.S. Department of Justice. The transaction is expected to close before year-end 2017. If the Merger is terminated as a result of reaching the termination date (and at that time one or more of the conditions relating to certain regulatory approvals have not been satisfied) or there is a final, non-appealable order preventing the transaction relating to antitrust laws, communications laws, utilities laws or foreign regulatory laws, then under certain circumstances, we would be obligated to pay Time Warner \$500. On October 20, 2017, to facilitate obtaining final regulatory approval required to close the merger, AT&T and Time Warner elected to extend the October 22, 2017 termination date of the agreement for a short period of time.

Other Events

FirstNet On March 30, 2017, the First Responder Network Authority (FirstNet) announced its selection of AT&T to build and manage the first nationwide broadband network dedicated to America's first responders. FirstNet will provide 20 MHz of valuable telecommunications spectrum and success-based payments of \$6,500 over the next five years to support network buildout. We expect to spend about \$40,000, in part recoverable from FirstNet, over the life of the 25-year contract to build, operate and maintain the network. AT&T will construct and operate the network and provide sustainability payments to FirstNet. Sustainability payments are required to be used for the operating expenses of FirstNet and to fund network improvements included in our \$40,000 estimate. FirstNet's operating expenses are anticipated to be in the \$75-\$100 range annually, and when adjusted for inflation, we expect to be in the \$3,000 range over the life of the 25-year contract. After FirstNet's operating expenses are paid, we anticipate that the remaining amount, expected to be in the \$15,000 range, will be reinvested into the network. As of November 2, 2017, 30 states

and territories have opted-in to the program, representing 38%, or approximately \$6,900, of this total sustainability payment commitment. The actual reach of the network and our investment over the 25-year period will be determined by the number of individual states and territories electing to participate in FirstNet.

States have until December 28, 2017 to elect to opt-out of the federally funded program, after which any state that did not formally make an election will automatically be opted-in. We do not expect FirstNet to materially impact our 2017 results.



AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

NOTE 8. SALES OF EQUIPMENT INSTALLMENT RECEIVABLES

We offer our customers the option to purchase certain wireless devices in installments over a period of up to 30 months and, in many cases, they have the right to trade in the original equipment for a new device within a set period and have the remaining unpaid balance satisfied. As of September 30, 2017 and December 31, 2016, gross equipment installment receivables of \$4,176 and \$5,665 were included on our consolidated balance sheets, of which \$2,485 and \$3,425 are notes receivable that are included in "Accounts receivable - net."

In 2014, we entered into an uncommitted agreement pertaining to the sale of equipment installment receivables and related security with Citibank and various other relationship banks as purchasers (collectively, the Purchasers). Under this agreement, we transfer certain receivables to the Purchasers for cash and additional consideration upon settlement of the receivables, referred to as the deferred purchase price. Since 2014, we have made beneficial modifications to the agreement. During 2017, we modified the agreement and entered into a second uncommitted agreement with the Purchasers such that we receive more upfront cash consideration at the time the receivables are transferred to the Purchasers. Additionally, in the event a customer trades in a device prior to the end of the installment contract period, we agree to make a payment to the Purchasers equal to any outstanding remaining installment receivable balance. Accordingly, we record a guarantee obligation to the Purchasers for this estimated amount at the time the receivables are transferred. Under the terms of the agreement, we continue to bill and collect the payments from our customers on behalf of the Purchasers. Since inception, cash proceeds received, net of remittances (excluding amounts returned as deferred purchase price), were \$4,019.

The following table sets forth a summary of equipment installment receivables sold during the three and nine months ended September 30, 2017 and 2016:

	Three months ended September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
Gross receivables sold	\$1,619	\$1,485	\$6,217	\$5,812
Net receivables sold <sup>1</sup>	1,478	1,336	5,698	5,263
Cash proceeds received	1,292	891	4,139	3,538
Deferred purchase price recorded	285	463	1,767	1,745
Guarantee obligation recorded	65	-	139	-

<sup>1</sup> Receivables net of allowance, imputed interest and trade-in right guarantees.

The deferred purchase price and guarantee obligation are initially recorded at estimated fair value and subsequently carried at the lower of cost or net realizable value. The estimation of their fair values is based on remaining installment payments expected to be collected and the expected timing and value of device trade-ins. The estimated value of the device trade-ins considers prices offered to us by independent third parties that contemplate changes in value after the launch of a device model. The fair value measurements used for the deferred purchase price and the guarantee obligation are considered Level 3 under the Fair Value Measurement and Disclosure framework (see Note 6).



AT&T INC.  
SEPTEMBER 30, 2017

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

Dollars in millions except per share amounts

The following table shows the equipment installment receivables, previously sold to the Purchasers, which we repurchased in exchange for the associated deferred purchase price during the three months and nine months ended September 30, 2017 and 2016:

	Three months ended September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
Fair value of repurchased receivables	\$567	\$749	\$1,281	\$1,281
Carrying value of deferred purchase price	507	722	1,147	1,261
Gain (loss) on repurchases <sup>1</sup>	\$60	\$27	\$134	\$20

<sup>1</sup> These gains (losses) are included in "Selling, general and administrative" in the consolidated statements of income.

At September 30, 2017 and December 31, 2016, our deferred purchase price receivable was \$3,170 and \$3,090, respectively, of which \$2,023 and \$1,606 are included in "Other current assets" on our consolidated balance sheets, with the remainder in "Other Assets." Our maximum exposure to loss as a result of selling these equipment installment receivables is limited to the total amount of our deferred purchase price and guarantee obligation.

The sales of equipment installment receivables did not have a material impact on our consolidated statements of income or to "Total Assets" reported on our consolidated balance sheets. We reflect the cash flows related to the arrangement as operating activities in our consolidated statements of cash flows because the cash received from the Purchasers upon both the sale of the receivables and the collection of the deferred purchase price is not subject to significant interest rate risk.

**Derecognized Installment Receivables**

The following table sets forth a summary of equipment installment receivables that were sold to Purchasers and are no longer considered our assets.

	2017
Outstanding derecognized receivables at January 1,	\$7,232
Gross receivables sold	6,217
Collections on cash purchase price	(3,556)
Collections on deferred purchase price	(665 )
Trade ins and other	(295 )
Fair value of repurchased receivables	(1,281)
Outstanding derecognized receivables at September 30,	\$7,652

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Dollars in millions except per share and per subscriber amounts

RESULTS OF OPERATIONS

AT&T is a holding company whose subsidiaries and affiliates operate in the communications and digital entertainment services industry. Our subsidiaries and affiliates provide services and equipment that deliver voice, video and broadband services both domestically and internationally. You should read this discussion in conjunction with the consolidated financial statements and accompanying notes. A reference to a "Note" in this section refers to the accompanying Notes to Consolidated Financial Statements.

Consolidated Results Our financial results in the third quarter and for the first nine months of 2017 and 2016 are summarized as follows:

	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Operating Revenues						
Service	\$36,378	\$37,272	(2.4 )%	\$109,372	\$111,515	(1.9 )%
Equipment	3,290	3,618	(9.1 )	9,498	10,430	(8.9 )
Total Operating Revenues	39,668	40,890	(3.0 )	118,870	121,945	(2.5 )
Operating expenses						
Cost of services and sales						
Equipment	4,191	4,455	(5.9 )	12,177	13,090	(7.0 )
Broadcast, programming and operations	5,284	4,909	7.6	15,156	14,239	6.4
Other cost of services	9,431	9,526	(1.0 )	27,714	28,436	(2.5 )
Selling, general and administrative	8,317	9,013	(7.7 )	24,917	26,363	(5.5 )
Depreciation and amortization	6,042	6,579	(8.2 )	18,316	19,718	(7.1 )
Total Operating Expenses	33,265	34,482	(3.5 )	98,280	101,846	(3.5 )
Operating Income	6,403	6,408	(0.1 )	20,590	20,099	2.4
Income Before Income Taxes	4,974	5,193	(4.2 )	16,422	16,621	(1.2 )
Net Income	3,123	3,418	(8.6 )	10,711	10,818	(1.0 )
Net Income Attributable to AT&T	\$3,029	\$3,328	(9.0 )%	\$10,413	\$10,539	(1.2 )%

Overview

Operating revenues decreased \$1,222, or 3.0%, in the third quarter and \$3,075, or 2.5%, for the first nine months of 2017.

Service revenues decreased \$894, or 2.4%, in the third quarter and \$2,143, or 1.9%, for the first nine months of 2017. The decreases were primarily due to continued declines in legacy wireline voice and data products and lower wireless service revenues reflecting increased adoption of unlimited plans. Additionally, we waived \$89 in service revenues for customers in areas affected by natural disasters during the third quarter of 2017. These were partially offset by increased revenues from strategic business services.

Equipment revenues decreased \$328, or 9.1%, in the third quarter and \$932, or 8.9%, for the first nine months of 2017. The decreases were primarily due to lower wireless handset sales and upgrades. Equipment revenue is becoming increasingly unpredictable as many customers are choosing to upgrade devices less frequently or are bringing their own devices.

Operating expenses decreased \$1,217, or 3.5%, in the third quarter and \$3,566, or 3.5%, for the first nine months of 2017.

Equipment expenses decreased \$264, or 5.9%, in the third quarter and \$913, or 7.0%, for the first nine months of 2017. The decreases were driven by a decline in devices sold reflecting a change in customer buying habits.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

Broadcast, programming and operations expenses increased \$375, or 7.6%, in the third quarter and \$917, or 6.4%, for the first nine months of 2017, reflecting annual content cost increases and additional programming costs for DIRECTV NOW.

Other cost of services expenses decreased \$95, or 1.0%, in the third quarter and \$722, or 2.5%, for the first nine months of 2017. The decreases reflect our continued focus on cost management and the utilization of automation and digitalization where appropriate, as well as lower Federal Universal Service Fund (USF) rates and fees. The decrease for the first nine months also includes an actuarial gain from the second-quarter 2017 remeasurement of our postretirement benefit obligation. These expense declines were partially offset by an increase in amortization of deferred customer fulfillment cost.

Selling, general and administrative expenses decreased \$696, or 7.7%, in the third quarter and \$1,446, or 5.5%, for the first nine months of 2017. The decreases were attributable to our disciplined cost management, lower selling and wireless commission costs from reduced volumes, fewer advertising costs, and, for the nine month period, the actuarial gain resulting from the second-quarter remeasurement of our postretirement benefit obligation. The decreases in the third quarter were partially offset by costs arising from natural disasters, and, for the first nine months, lower gains on wireless spectrum transactions during 2017 than in the comparable period of 2016. We are continuing to assess network damage from the natural disasters that occurred in the third quarter as well as the recent fires in California, and expect additional pressure in the fourth quarter.

Depreciation and amortization expense decreased \$537, or 8.2%, in the third quarter and \$1,402, or 7.1%, for the first nine months of 2017. Depreciation expense decreased \$393, or 7.4%, in the third quarter and \$962, or 6.1%, for the first nine months of 2017. The decreases were primarily due to our fourth-quarter 2016 change in estimated useful lives and salvage values of certain assets associated with our transition to an IP-based network, which accounted for \$327 of the decrease in the third quarter and \$980 of the decrease for the first nine months. Also contributing to lower depreciation expenses were network assets becoming fully depreciated. These decreases were partially offset by increases resulting from ongoing capital spending for upgrades and expansion.

Amortization expense decreased \$144, or 11.2%, in the third quarter and \$440, or 11.1%, for the first nine months of 2017 due to lower amortization of intangibles for the customer lists associated with acquisitions.

Operating income decreased \$5, or 0.1%, in the third quarter and increased \$491, or 2.4%, for the first nine months of 2017. Our operating income margin in the third quarter increased from 15.7% in 2016 to 16.1% in 2017, and for the first nine months increased from 16.5% in 2016 to 17.3% in 2017.

Interest expense increased \$462, or 37.7%, in the third quarter and \$685, or 18.6%, for the first nine months of 2017. The increases were primarily due to higher debt balances in anticipation of closing our acquisition of Time Warner Inc. (Time Warner) and an increase in average interest rates when compared to the prior year. Financing fees related to pending acquisitions also contributed to higher interest expense in 2017.

Equity in net income (loss) of affiliates decreased \$5, or 31.3%, in the third quarter and \$205 for the first nine months of 2017, predominantly from losses from our legacy publishing business (which we sold in June 2017), partially offset by income from our investments in video-related businesses.

Other income (expense) – net increased \$253 in the third quarter and \$200 for the first nine months. The increases were primarily due to higher net gains from the sale of non-strategic assets and investments of \$123 and \$26, respectively, and growth in interest and dividend income of \$91 and \$146, including interest on cash held in anticipation of closing our acquisition of Time Warner.

Income taxes increased \$76, or 4.3%, in the third quarter and decreased \$92, or 1.6%, for the first nine months of 2017. Our effective tax rate was 37.2% in the third quarter and 34.8% for the first nine months of 2017, as compared to 34.2% in the third quarter and 34.9% for the first nine months of 2016. The increase in the third quarter was primarily due to state-level legislation changes that resulted in a remeasurement of our deferred tax liabilities offset by lower income before income taxes. The decrease for the first nine months of 2017 was primarily due to lower income before income taxes and the

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

recognition of tax benefits related to the restructuring of a portion of our wireless business offset by state-level legislation changes.

Selected Financial and Operating Data

	September 30,			
	2017	2016		
Subscribers and connections in (000s)				
Domestic wireless subscribers	138,826	133,338		
Mexican wireless subscribers	13,779	10,698		
North American wireless subscribers	152,605	144,036		
North American branded subscribers	106,098	100,821		
North American branded net additions	2,782	3,881		
Domestic satellite and over-the-top video subscribers	21,392	20,777		
AT&T U-verse® (U-verse) video subscribers	3,718	4,544		
Latin America satellite video subscribers <sup>1</sup>	13,490	12,476		
Total video subscribers	38,600	37,797		
Total domestic broadband connections	15,715	15,618		
Network access lines in service	12,249	14,603		
U-verse VoIP connections	5,774	5,707		
Debt ratio <sup>2</sup>	56.4	%	50.1	%
Net debt ratio <sup>3</sup>	39.7	%	47.8	%
Ratio of earnings to fixed charges <sup>4</sup>	3.55		3.91	
Number of AT&T employees	256,800		273,140	

<sup>1</sup> Excludes subscribers of our International segment equity investments in SKY Mexico, in which we own a 41.3% stake. At June 30, 2017, SKY Mexico had 8.0 million subscribers.

<sup>2</sup> Debt ratios are calculated by dividing total debt (debt maturing within one year plus long-term debt) by total capital (total debt plus total stockholders' equity) and do not consider cash available to pay down debt. See our "Liquidity and Capital Resources" section for discussion.

<sup>3</sup> Net debt ratios are calculated by deriving total debt (debt maturing within one year plus long-term debt) less cash available by total capital (total debt plus total stockholders' equity).

<sup>4</sup> See Exhibit 12.

Segment Results

Our segments are strategic business units that offer different products and services over various technology platforms and/or in different geographies that are managed accordingly. Our segment results presented in Note 4 and discussed below for each segment follow our internal management reporting. We analyze our segments based on Segment Contribution, which consists of operating income, excluding acquisition-related costs and other significant items, and equity in net income (loss) of affiliates for investments managed within each segment. We have four reportable segments: (1) Business Solutions, (2) Entertainment Group, (3) Consumer Mobility and (4) International.



We also evaluate segment performance based on EBITDA and/or EBITDA margin, which is defined as Segment Contribution, excluding equity in net income (loss) of affiliates and depreciation and amortization. We believe EBITDA to be a relevant and useful measurement to our investors as it is part of our internal management reporting and planning processes and it is an important metric that management uses to evaluate operating performance. EBITDA does not give effect to cash used for debt service requirements and thus does not reflect available funds for distributions, reinvestment or other discretionary uses. EBITDA margin is EBITDA divided by total revenues.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

The Business Solutions segment provides services to business customers, including multinational companies; governmental and wholesale customers; and individual subscribers who purchase wireless services through employer-sponsored plans. We provide advanced IP-based services including Virtual Private Networks (VPN); Ethernet-related products and broadband, collectively referred to as fixed strategic services; as well as traditional data and voice products. We utilize our wireless and wired networks to provide a complete integrated communications solution to our business customers.

The Entertainment Group segment provides video, internet, voice communication, and interactive and targeted advertising services to customers located in the United States or in U.S. territories. We utilize our copper and IP-based wired network and our satellite technology.

The Consumer Mobility segment provides nationwide wireless service to consumers, wholesale and resale wireless subscribers located in the United States or in U.S. territories. We utilize our networks to provide voice and data services, including high-speed internet, video and home monitoring services over wireless devices.

The International segment provides entertainment services in Latin America and wireless services in Mexico. Video entertainment services are provided to primarily residential customers using satellite technology. We utilize our regional and national networks in Mexico to provide consumer and business customers with wireless data and voice communication services. Our international subsidiaries conduct business in their local currency, and operating results are converted to U.S. dollars using official exchange rates. Our International segment is subject to foreign currency fluctuations.

Our operating assets are utilized by multiple segments and consist of our wireless and wired networks as well as an international satellite fleet. Our domestic communications business strategies reflect bundled product offerings that increasingly cut across product lines and utilize our asset base. Therefore asset information and capital expenditures by segment are not presented. Depreciation is allocated based on asset utilization by segment. In expectation of the close of our acquisition of Time Warner, we are beginning to realign our operations and strategies. We are pushing down administrative activities into the business units to better manage costs and serve our customers.

Business Solutions  
Segment Results

	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Segment operating revenues						
Wireless service	\$8,034	\$8,050	(0.2 )%	\$23,969	\$23,868	0.4 %
Fixed strategic services	3,087	2,913	6.0	9,089	8,469	7.3
Legacy voice and data services	3,434	4,042	(15.0 )	10,572	12,577	(15.9 )
Other service and equipment	852	886	(3.8 )	2,513	2,619	(4.0 )
Wireless equipment	1,654	1,876	(11.8 )	4,873	5,422	(10.1 )
Total Segment Operating Revenues	17,061	17,767	(4.0 )	51,016	52,955	(3.7 )
Segment operating expenses						
Operations and support	10,233	10,925	(6.3 )	30,722	32,584	(5.7 )

Edgar Filing: AT&T INC. - Form 10-Q

Depreciation and amortization	2,325	2,539	(8.4 )	6,972	7,568	(7.9 )
Total Segment Operating Expenses	12,558	13,464	(6.7 )	37,694	40,152	(6.1 )
Segment Operating Income	4,503	4,303	4.6	13,322	12,803	4.1
Equity in Net Income of Affiliates	-	-	-	-	-	-
Segment Contribution	\$4,503	\$4,303	4.6 %	\$13,322	\$12,803	4.1 %

25

---

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

The following tables highlight other key measures of performance for the Business Solutions segment:

(in 000s)	September 30,		Percent	
	2017	2016	Change	
Business Wireless Subscribers				
Postpaid/Branded	51,412	50,014	2.8	%
Reseller	77	58	32.8	
Connected devices <sup>1</sup>	35,909	29,355	22.3	
Total Business Wireless Subscribers	87,398	79,427	10.0	

Business IP Broadband Connections	1,017	963	5.6	%
-----------------------------------	-------	-----	-----	---

<sup>1</sup> Includes data-centric devices such as session-based tablets, monitoring devices and primarily wholesale automobile systems.

Excludes postpaid tablets.

(in 000s)	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Business Wireless Net Additions <sup>1, 4</sup>						
Postpaid/Branded	15	191	(92.1)%	(74)	509	-
Reseller	2	1	-	3	(34)	-
Connected devices <sup>2</sup>	2,292	1,290	77.7	7,015	4,067	72.5
Business Wireless Net Subscriber Additions	2,309	1,482	55.8	6,944	4,542	52.9
Business Wireless Postpaid Churn <sup>1, 3, 4</sup>	1.01 %	0.97 %	4 BP	1.02 %	0.97 %	5 BP

Business IP Broadband Net Additions	25	15	66.7 %	41	52	(21.2)%
-------------------------------------	----	----	--------	----	----	---------

<sup>1</sup> Excludes migrations between AT&T segments and/or subscriber categories and acquisition-related additions during the period.

<sup>2</sup> Includes data-centric devices such as session-based tablets, monitoring devices and primarily wholesale automobile systems.

Excludes postpaid tablets.

<sup>3</sup> Calculated by dividing the aggregate number of wireless subscribers who canceled service during a period divided by the total number

of wireless subscribers at the beginning of that period. The churn rate for the period is equal to the average of the churn rate for each month of that period.

<sup>4</sup> 2017 excludes the impact of the 2G shutdown, which was reflected in beginning of period subscribers.

Operating Revenues decreased \$706, or 4.0%, in the third quarter and \$1,939, or 3.7%, for the first nine months of 2017. Revenue declines reflect technological shifts away from legacy products, as well as decreasing wireless equipment revenues resulting from changes in customer buying habits. These decreases were partially offset by fixed

strategic services, which represent 41% of non-wireless revenues. Our revenues continue to be pressured by slower fixed business investment.

Wireless service revenues decreased \$16, or 0.2%, in the third quarter and increased \$101, or 0.4%, for the first nine months of 2017. The decrease in the third quarter was primarily due to customers shifting to our unlimited plans as well as fewer migrations from our Consumer Mobility segment during the quarter. The increase in the first nine months was primarily due to the migration of customers from our Consumer Mobility segment.

At September 30, 2017, we served 87.4 million subscribers, an increase of 10.0% from the prior year. Postpaid subscribers increased 2.8% from the prior year reflecting the addition of new customers as well as migrations from our Consumer Mobility segment, partially offset by continuing competitive pressures in the industry. Connected devices, which have lower average revenue per average subscriber (ARPU) and churn, increased 22.3% from the prior year reflecting growth in our connected car business and other data centric devices that utilize the network to connect and control physical devices using embedded computing systems and/or software, commonly called the Internet of Things (IoT).

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

The effective management of subscriber churn is critical to our ability to maximize revenue growth and to maintain and improve margins. In the third quarter, business wireless postpaid churn increased to 1.01% in 2017 from 0.97% in 2016, and for the first nine months increased to 1.02% in 2017 from 0.97% in 2016.

Fixed strategic services revenues increased \$174, or 6.0%, in the third quarter and \$620, or 7.3%, for the first nine months of 2017. Our revenues increased in the third quarter and first nine months of 2017 primarily due to: Ethernet of \$77 and \$243; Dedicated Internet services of \$46 and \$150; and VoIP of \$41 and \$159, respectively.

Legacy wired voice and data service revenues decreased \$608, or 15.0%, in the third quarter and \$2,005, or 15.9%, for the first nine months of 2017. In the third quarter and first nine months of 2017, legacy voice billings decreased \$324 and \$1,068 and traditional data billings decreased \$284 and \$937, respectively. These decreases were primarily due to lower demand, as customers continue to shift to our more advanced IP-based offerings or to competitors.

Wireless equipment revenues decreased \$222, or 11.8%, in the third quarter and \$549, or 10.1%, for the first nine months of 2017. The decreases were primarily due to decreases in device upgrades reflecting a change in customer buying habits.

Operations and support expenses decreased \$692, or 6.3%, in the third quarter and \$1,862, or 5.7%, for the first nine months of 2017. Operations and support expenses consist of costs incurred to provide our products and services, including costs of operating and maintaining our networks and personnel costs, such as compensation and benefits.

Decreased operations and support expenses in the third quarter and first nine months were primarily due to lower equipment sales and wireless upgrade transactions, which decreased equipment costs by \$336 and \$732, and efforts to automate and digitize our support activities improved results \$146 and \$543, respectively. As of September 30, 2017, approximately 45% of our network functions have been moved to software-based systems. Expense reductions also reflect lower administrative costs, contributing to a reduction in expenses of \$49 and \$213, and fewer traffic compensation and wireless interconnect costs, resulting in declines of \$44 and \$155, respectively, in access and interconnect costs. Lower selling and wireless commission costs also contributed to decreased expenses for the first nine months.

Depreciation expense decreased \$214, or 8.4%, in the third quarter and \$596, or 7.9%, for the first nine months of 2017. The decreases were primarily due to our fourth-quarter 2016 change in estimated useful lives and salvage value of certain network assets. Also contributing to lower depreciation expenses were network assets becoming fully depreciated, partially offset by ongoing capital spending for network upgrades and expansion.

Operating income increased \$200, or 4.6%, in the third quarter and \$519, or 4.1%, for the first nine months of 2017. Our Business Solutions segment operating income margin in the third quarter increased from 24.2% in 2016 to 26.4% in 2017, and for the first nine months increased from 24.2% in 2016 to 26.1% in 2017. Our Business Solutions EBITDA margin in the third quarter increased from 38.5% in 2016 to 40.0% in 2017, and for the first nine months increased from 38.5% in 2016 to 39.8% in 2017.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

Entertainment Group  
Segment Results

	Third Quarter			Nine-Month Period			
	2017	2016	Percent Change	2017	2016	Percent Change	
Segment operating revenues							
Video entertainment	\$9,200	\$9,026	1.9 %	\$27,373	\$26,893	1.8 %	
High-speed internet	1,916	1,892	1.3	5,784	5,562	4.0	
Legacy voice and data services	949	1,168	(18.8 )	3,010	3,725	(19.2 )	
Other service and equipment	583	634	(8.0 )	1,786	1,909	(6.4 )	
Total Segment Operating Revenues	12,648	12,720	(0.6 )	37,953	38,089	(0.4 )	
Segment operating expenses							
Operations and support	9,953	9,728	2.3	29,112	28,875	0.8	
Depreciation and amortization	1,379	1,504	(8.3 )	4,256	4,481	(5.0 )	
Total Segment Operating Expenses	11,332	11,232	0.9	33,368	33,356	-	
Segment Operating Income	1,316	1,488	(11.6 )	4,585	4,733	(3.1 )	
Equity in Net Income (Loss) of Affiliates	(6 )	-	-	(23 )	1	-	
Segment Contribution	\$1,310	\$1,488	(12.0 )%	\$4,562	\$4,734	(3.6 )%	

The following tables highlight other key measures of performance for the Entertainment Group segment:

(in 000s)	September 30,		Percent
	2017	2016	Change
Video Connections			
Satellite	20,605	20,777	(0.8 )%
U-verse	3,691	4,515	(18.3 )
DIRECTV NOW <sup>1</sup>	787	-	-
Total Video Connections	25,083	25,292	(0.8 )
Broadband Connections			
IP	13,367	12,752	4.8
DSL	964	1,424	(32.3 )
Total Broadband Connections	14,331	14,176	1.1
Retail Consumer Switched Access Lines	4,996	6,155	(18.8 )
U-verse Consumer VoIP Connections	5,337	5,378	(0.8 )
Total Retail Consumer Voice Connections	10,333	11,533	(10.4 )%

<sup>1</sup> Consistent with industry practice, DIRECTV NOW includes over-the-top connections that are on a free-trial.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

(in 000s)	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Video Net Additions						
Satellite <sup>1</sup>	(251)	323	- %	(407)	993	- %
U-verse <sup>1</sup>	(134)	(326)	58.9	(562)	(1,099)	48.9
DIRECTV NOW <sup>2</sup>	296	-	-	520	-	-
Net Video Additions	(89 )	(3 )	-	(449)	(106 )	-
Broadband Net Additions						
IP	125	156	(19.9 )	479	396	21.0
DSL	(96 )	(161)	40.4	(327)	(506 )	35.4
Net Broadband Additions	29	(5 )	- %	152	(110 )	- %

<sup>1</sup> Includes disconnections for customers that migrated to DIRECTV NOW.

<sup>2</sup> Consistent with industry practice, DIRECTV NOW includes over-the-top connections that are on a free-trial.

Operating revenues decreased \$72, or 0.6%, in the third quarter and \$136, or 0.4%, for the first nine months of 2017, largely due to lower revenues from legacy voice and data products, partially offset by growth in revenues from consumer IP broadband services.

As consumers continue to demand more mobile access to video, we provide streaming access to our subscribers, including mobile access for existing satellite and U-verse subscribers. In November 2016, we launched DIRECTV NOW, our newest video streaming option that does not require either satellite or U-verse service (commonly called over-the-top video service).

Video entertainment revenues increased \$174, or 1.9%, in the third quarter and \$480, or 1.8%, for the first nine months of 2017. These increases include a third-quarter 2017 pay-per-view event and reflect a 4.5% and 3.3% increase in average revenue per linear (combined satellite and U-verse) video connection. Advertising revenues also increased \$41 and \$113, respectively.

Linear video subscriber losses, and associated margin pressure, continued their recent trend, with some of the losses due to the impact from hurricanes as well as tightening of our credit policies. We are also seeing the impact of customers wanting mobile and over-the-top offerings, which is contributing to growth in DIRECTV NOW connections and partially offsetting linear video subscriber losses. DIRECTV NOW connections continue to grow as we add eligible devices and increase content choices. Our strategy to bundle services has positively impacted subscriber trends and churn, with customers who bundle our wireless and video having nearly half the rate of churn as customers with a single service. Customers with linear video but no wireless service through AT&T increased churn during the quarter, partially due to pricing increases associated with annual content cost increases and involuntary churn.

High-speed internet revenues increased \$24, or 1.3%, in the third quarter and \$222, or 4.0%, for the first nine months of 2017, reflecting a 4.8% increase in IP broadband subscribers when compared to the prior year. Average revenue per IP broadband connection (ARPU) decreased 3.7% in the third quarter and 0.8% for the first nine months of 2017. Our



bundling strategy is also helping to lower churn for broadband subscribers, with subscribers who bundle broadband with another AT&T service having about 30% lower churn than broadband-only subscribers. To compete more effectively against other broadband providers in the midst of ongoing declines in DSL subscribers, we continued to deploy our all-fiber, high-speed wireline network, which has improved customer retention rates. We also expect our planned 5G national deployment to aid our ability to provide more locations with competitive broadband speeds.

Legacy voice and data service revenues decreased \$219, or 18.8%, in the third quarter and \$715, or 19.2%, for the first nine months of 2017. For the nine months ended September 30, 2017, legacy voice and data services represented approximately 8% of our total Entertainment Group revenue compared to 10% for the September 30, 2016 period, and reflect third quarter and year to date decreases of \$148 and \$483 in local voice and long-distance, and \$70 and \$232 in traditional data billings, respectively. The decreases reflect the continued migration of customers to our more advanced IP-based offerings or to

AT&T INC.  
SEPTEMBER 30, 2017

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued**

Dollars in millions except per share and per subscriber amounts

competitors. At September 30, 2017, approximately 7% of our broadband connections were DSL compared to 10% at September 30, 2016.

Operations and support expenses increased \$225, or 2.3%, in the third quarter and increased \$237, or 0.8%, for the first nine months of 2017. Operations and support expenses consist of costs associated with providing video content, and expenses incurred to provide our products and services, which include costs of operating and maintaining our networks, as well as personnel charges for compensation and benefits.

Increased operations and support expenses in the third quarter and for the first nine months of 2017 were primarily due to annual content cost increases, a pay-per-view event, deferred customer fulfillment cost amortization, and video platform development costs. Partially offsetting these increases were the impact of our ongoing focus on cost efficiencies and merger synergies, as well as workforce reductions and lower marketing costs.

Depreciation expense decreased \$125, or 8.3%, in the third quarter, and \$225, or 5.0%, for the first nine months of 2017. The decreases were primarily due to our fourth-quarter 2016 change in estimated useful lives and salvage value of certain assets. Also contributing to lower depreciation expenses were network assets becoming fully depreciated. These decreases were offset by ongoing capital spending for network upgrades and expansion.

Operating income decreased \$172, or 11.6%, in the third quarter and \$148, or 3.1%, for the first nine months of 2017. Our Entertainment Group segment operating income margin in third quarter decreased from 11.7% in 2016 to 10.4% in 2017, and for the first nine months decreased from 12.4% in 2016 to 12.1% in 2017. Our Entertainment Group segment EBITDA margin in the third quarter decreased from 23.5% in 2016 to 21.3% in 2017, and for the first nine months decreased from 24.2% in 2016 to 23.3% in 2017.

Consumer Mobility  
Segment Results

	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Segment operating revenues						
Service	\$6,507	\$6,914	(5.9 )%	\$19,644	\$20,805	(5.6 )%
Equipment	1,241	1,353	(8.3 )	3,635	3,976	(8.6 )
Total Segment Operating Revenues	7,748	8,267	(6.3 )	23,279	24,781	(6.1 )
Segment operating expenses						
Operations and support	4,551	4,751	(4.2 )	13,599	14,343	(5.2 )
Depreciation and amortization	877	944	(7.1 )	2,621	2,798	(6.3 )
Total Segment Operating Expenses	5,428	5,695	(4.7 )	16,220	17,141	(5.4 )
Segment Operating Income	2,320	2,572	(9.8 )	7,059	7,640	(7.6 )
Equity in Net Income of Affiliates	-	-	-	-	-	-
Segment Contribution	\$2,320	\$2,572	(9.8 )%	\$7,059	\$7,640	(7.6 )%

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

The following tables highlight other key measures of performance for the Consumer Mobility segment:

(in 000s)	September 30,		Percent Change
	2017	2016	
Consumer Mobility Subscribers			
Postpaid	26,003	27,374	(5.0 )%
Prepaid <sup>2</sup>	15,136	13,035	16.1
Branded	41,139	40,409	1.8
Reseller	9,800	12,566	(22.0 )
Connected devices <sup>1, 2</sup>	489	936	(47.8 )
Total Consumer Mobility Subscribers	51,428	53,911	(4.6 )%

<sup>1</sup> Includes data-centric devices such as session-based tablets, monitoring devices and postpaid automobile systems. Excludes postpaid tablets. See (2) below.

<sup>2</sup> Beginning in July 2017, we are reporting prepaid IoT connections, which primarily consist of "connected" cars, as a component of prepaid subscribers. The prepaid subscriber base at September 30, 2017 now includes approximately 543 subscribers that were formerly included in connected devices.

(in 000s)	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Consumer Mobility Net Additions <sup>1, 4</sup>						
Postpaid	102	21	- %	127	89	42.7 %
Prepaid <sup>5</sup>	324	304	6.6	873	1,169	(25.3 )
Branded Net Additions	426	325	31.1	1,000	1,258	(20.5 )
Reseller	(394)	(316)	(24.7 )	(1,345)	(1,140)	(18.0 )
Connected devices <sup>2, 5</sup>	(18 )	41	-	87	14	-
Consumer Mobility Net Subscriber Additions	14	50	(72.0 )%	(258 )	132	- %

Total Churn <sup>1, 3, 4</sup>	2.37 %	2.11 %	26 BP	2.32 %	2.06 %	26 BP
Postpaid Churn <sup>1, 3, 4</sup>	1.17 %	1.19 %	(2) BP	1.16 %	1.17 %	(1) BP

<sup>1</sup> Excludes migrations between AT&T segments and/or subscriber categories and acquisition-related additions during the period.

<sup>2</sup> Includes data-centric devices such as session-based tablets, monitoring devices and postpaid automobile systems. Excludes postpaid tablets. See (5) below.

<sup>3</sup> Calculated by dividing the aggregate number of wireless subscribers who canceled service during a month divided by the total number of wireless subscribers at the beginning of that month. The churn rate for the period is equal to the average of the churn rate for

each month of that period.

<sup>4</sup> 2017 excludes the impact of the 2G shutdown and a true-up to the reseller subscriber base, which were reflected in beginning of period subscribers.

<sup>5</sup> Beginning in July 2017, we are reporting prepaid IoT connections, which primarily consist of "connected" cars, as a component of prepaid subscribers, resulting in 97 additional prepaid net adds in the quarter. Had we restated our prior periods, prepaid net adds for the comparable periods would have been 381 in the third quarter of 2016, and 1,060 and 1,324 for the first nine months of 2017 and 2016, respectively.

Operating Revenues decreased \$519, or 6.3%, in the third quarter and \$1,502, or 6.1%, for the first nine months of 2017. Decreased revenues reflect declines in postpaid service revenues due to customers migrating to our Business Solutions segment and choosing unlimited plans, partially offset by higher prepaid service revenues. Our business wireless offerings allow for individual subscribers to purchase wireless services through employer-sponsored plans for a reduced price. The migration of these subscribers to the Business Solutions segment negatively impacted our consumer postpaid subscriber total and service revenue growth.

31

---

AT&T INC.  
SEPTEMBER 30, 2017

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued**

Dollars in millions except per share and per subscriber amounts

Service revenue decreased \$407, or 5.9%, in the third quarter and \$1,161, or 5.6%, for the first nine months of 2017. The decreases were largely due to postpaid customers continuing to shift to discounted monthly service charges under our unlimited plans and the migration of subscribers to Business Solutions. Revenues from postpaid customers declined \$419, or 8.6%, in the third quarter and \$1,422, or 9.5%, for the first nine months of 2017. Without the migration of customers to Business Solutions, postpaid wireless revenues would have decreased approximately 4.6% and 5.2%, respectively. The decreases were partially offset by higher prepaid service revenues of \$155, or 10.7%, in the third quarter and \$595, or 14.5%, for the first nine months primarily from growth in Cricket and AT&T PREPAID<sup>SM</sup> subscribers.

Equipment revenue decreased \$112, or 8.3%, in the third quarter and \$341, or 8.6%, for the first nine months of 2017. The decreases in equipment revenues resulted from lower handset sales and upgrades. As previously discussed, equipment revenue is becoming increasingly unpredictable as customers are choosing to upgrade devices less frequently or bring their own.

Operations and support expenses decreased \$200, or 4.2%, in the third quarter and \$744, or 5.2%, for the first nine months of 2017. Operations and support expenses consist of costs incurred to provide our products and services, including costs of operating and maintaining our networks and personnel expenses, such as compensation and benefits.

Decreased operations and support expenses for the third quarter were primarily due to lower volumes of wireless equipment sales and upgrades, which decreased equipment and selling and commission costs, and operational efficiencies. The nine-month period also reflects lower marketing and advertising costs resulting from the timing of scheduled ad campaigns and integrated advertising.

Depreciation expense decreased \$67, or 7.1%, in the third quarter and \$177, or 6.3%, for the first nine months of 2017. The decreases were primarily due to fully depreciated assets, partially offset by ongoing capital spending for network upgrades and expansion.

Operating income decreased \$252, or 9.8%, in the third quarter and \$581, or 7.6%, for the first nine months of 2017. Our Consumer Mobility segment operating income margin in the third quarter decreased from 31.1% in 2016 to 29.9% in 2017, and for the first nine months decreased from 30.8% in 2016 to 30.3% in 2017. Our Consumer Mobility EBITDA margin in the third quarter decreased from 42.5% in 2016 to 41.3% in 2017, and for the first nine months decreased from 42.1% in 2016 to 41.6% in 2017.

International  
Segment Results

	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Segment operating revenues						
Video entertainment	\$1,363	\$1,297	5.1 %	\$4,065	\$3,649	11.4 %
Wireless service	536	484	10.7	1,546	1,428	8.3
Wireless equipment	200	98	-	443	297	49.2
Total Segment Operating Revenues	2,099	1,879	11.7	6,054	5,374	12.7

Segment operating expenses						
Operations and support	1,937	1,640	18.1	5,468	4,951	10.4
Depreciation and amortization	304	293	3.8	905	868	4.3
Total Segment Operating Expenses	2,241	1,933	15.9	6,373	5,819	9.5
Segment Operating Income (Loss)	(142 )	(54 )	-	(319 )	(445 )	28.3
Equity in Net Income (Loss)						
of Affiliates	17	1	-	62	24	-
Segment Contribution	\$(125 )	\$(53 )	-	% \$(257 )	\$(421 )	39.0 %

32

---

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

The following tables highlight other key measures of performance for the International segment:

(in 000s)	September 30,		Percent Change
	2017	2016	
Mexican Wireless Subscribers			
Postpaid	5,316	4,733	12.3 %
Prepaid	8,231	5,665	45.3
Branded	13,547	10,398	30.3
Reseller	232	300	(22.7 )
Total Mexican Wireless Subscribers	13,779	10,698	28.8

Latin America Satellite Subscribers

PanAmericana	8,201	7,139	14.9
SKY Brazil <sup>1</sup>	5,289	5,337	(0.9 )
Total Latin America Satellite Subscribers	13,490	12,476	8.1 %

<sup>1</sup> Excludes subscribers of our International segment equity investments in SKY Mexico, in which we own a 41.3% stake. SKY Mexico had 8.0 million subscribers at June 30, 2017 and 7.9 million subscribers at September 30, 2016.

(in 000s)	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Mexican Wireless Net Additions						
Postpaid	129	163	(20.9 )%	351	444	(20.9 )%
Prepaid	585	606	(3.5 )	1,504	1,670	(9.9 )
Branded Net Additions	714	769	(7.2 )	1,855	2,114	(12.3 )
Reseller	(17 )	(26 )	34.6	(49 )	(100 )	51.0
Mexican Wireless Net Subscriber Additions	697	743	(6.2 )	1,806	2,014	(10.3 )
Latin America Satellite Net Additions <sup>1</sup>						
PanAmericana	98	(36 )	-	163	73	-
SKY Brazil	(230)	(12 )	-	(260 )	(107 )	-
Latin America Satellite Net Subscriber Additions <sup>2</sup>	(132)	(48 )	- %	(97 )	(34 )	- %

<sup>1</sup> In 2017, we updated the methodology used to account for prepaid video connections, which were reflected in beginning of period subscribers.

<sup>2</sup> Excludes SKY Mexico net subscriber losses of 13 for the six months ended June 30, 2017 and additions of 519 for the six months of June 30, 2016.

Operating Results

Our International segment consists of the Latin American operations acquired with DIRECTV as well as our Mexican wireless operations. Video entertainment services are provided to primarily residential customers using satellite technology. Our international subsidiaries conduct business in their local currency and operating results are converted to U.S. dollars using official exchange rates. Our International segment is subject to foreign currency fluctuations.

Operating revenues increased \$220, or 11.7%, in the third quarter and \$680, or 12.7%, for the first nine months of 2017. The increases include \$66 and \$416 from video services in Latin America due to price increases driven primarily by macroeconomic conditions with mixed local currencies. Mexico wireless revenues increased \$154, or 26.5%, in the third quarter and \$264, or 15.3%, for the first nine months of 2017, primarily due to growth in equipment revenues as we have increased our subscriber base, partially offset by competitive pricing for services.

33

---



AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

Operations and support expenses increased \$297, or 18.1%, in the third quarter and \$517, or 10.4%, for the first nine months of 2017. Operations and support expenses consist of costs incurred to provide our products and services, including costs of operating and maintaining our networks and providing video content and personnel expenses, such as compensation and benefits.

The increases in Latin America in the third quarter and for the first nine months were primarily due to higher programming and other operating costs. The nine-month period was partially offset by foreign currency exchange rates and our reassessment of operating tax contingencies in Brazil. The increases in Mexico for the first nine months were primarily driven by higher operational costs, including expenses associated with our network expansion and foreign currency pressures.

Depreciation expense increased \$11, or 3.8%, in the third quarter and \$37, or 4.3%, for the first nine months of 2017. The increases were primarily due to updating the estimated asset lives for video equipment in Latin America and higher capital spending in Mexico.

Operating income decreased \$88 in the third quarter and increased \$126, or 28.3%, for the first nine months of 2017, and were negatively impacted by foreign exchange pressure. Our International segment operating income margin in the third quarter decreased from (2.9)% in 2016 to (6.8)% in 2017, and for the first nine months increased from (8.3)% in 2016 to (5.3)% in 2017. Our International EBITDA margin in the third quarter decreased from 12.7% in 2016 to 7.7% in 2017, and for the first nine months increased from 7.9% in 2016 to 9.7% in 2017.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

Supplemental Operating Information

As a supplemental discussion of our operating results, for comparison purposes, we are providing a view of our combined domestic wireless operations (AT&T Mobility). See "Discussion and Reconciliation of Non-GAAP Measure" for a reconciliation of these supplemental measures to the most directly comparable financial measures calculated and presented in accordance with U.S. generally accepted accounting principles.

AT&T Mobility Results

	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Operating revenues						
Service	\$14,541	\$14,964	(2.8 )%	\$43,613	\$44,673	(2.4 )%
Equipment	2,895	3,229	(10.3 )	8,508	9,398	(9.5 )
Total Operating Revenues	17,436	18,193	(4.2 )	52,121	54,071	(3.6 )
Operating expenses						
Operations and support	10,113	10,697	(5.5 )	30,308	31,822	(4.8 )
EBITDA	7,323	7,496	(2.3 )	21,813	22,249	(2.0 )
Depreciation and amortization	2,010	2,107	(4.6 )	5,999	6,244	(3.9 )
Total Operating Expenses	12,123	12,804	(5.3 )	36,307	38,066	(4.6 )
Operating Income	\$5,313	\$5,389	(1.4 )%	\$15,814	\$16,005	(1.2 )%

The following tables highlight other key measures of performance for AT&T Mobility:

(in 000s)	September 30,		Percent Change
	2017	2016	
Wireless Subscribers <sup>1</sup>			
Postpaid smartphones	59,277	58,688	1.0 %
Postpaid feature phones and data-centric devices	18,138	18,700	(3.0 )
Postpaid	77,415	77,388	-
Prepaid <sup>3</sup>	15,136	13,035	16.1
Branded	92,551	90,423	2.4
Reseller	9,877	12,624	(21.8 )
Connected devices <sup>2, 3</sup>	36,398	30,291	20.2
Total Wireless Subscribers	138,826	133,338	4.1
Branded Smartphones	72,242	69,752	3.6
Smartphones under our installment programs at end of period	31,207	29,382	6.2 %

<sup>1</sup> Represents 100% of AT&T Mobility wireless subscribers.

<sup>2</sup> Includes data-centric devices such as session-based tablets, monitoring devices and primarily wholesale automobile systems. Excludes postpaid tablets. See (3) below.

<sup>3</sup> Beginning in July 2017, we are reporting prepaid IoT connections, which primarily consist of "connected" cars, as a component of

prepaid subscribers. The prepaid subscriber base at September 30, 2017 now includes approximately 543 subscribers that were formerly included in connected devices.

35

---

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

(in 000s)	Third Quarter			Nine-Month Period		
	2017	2016	Percent Change	2017	2016	Percent Change
Wireless Net Additions <sup>1, 4</sup>						
Postpaid	117	212	(44.8 )%	53	598	(91.1 )%
Prepaid <sup>5</sup>	324	304	6.6	873	1,169	(25.3 )
Branded Net Additions	441	516	(14.5 )	926	1,767	(47.6 )
Reseller	(392 )	(315 )	(24.4 )	(1,342 )	(1,174 )	(14.3 )
Connected devices <sup>2, 5</sup>	2,274	1,331	70.8	7,102	4,081	74.0
Wireless Net Subscriber Additions	2,323	1,532	51.6	6,686	4,674	43.0
Smartphones sold under our installment programs during period	3,491	4,283	(18.5 )%	10,575	12,378	(14.6 )%
Total Churn <sup>3, 4</sup>	1.32 %	1.45 %	(13) BP	1.35 %	1.41 %	(6) BP
Branded Churn <sup>3, 4</sup>	1.70 %	1.63 %	7 BP	1.66 %	1.57 %	9 BP
Postpaid Churn <sup>3, 4</sup>	1.07 %	1.05 %	2 BP	1.07 %	1.04 %	3 BP
Postpaid Phone Only Churn <sup>3, 4</sup>	0.84 %	0.90 %	(6) BP	0.84 %	0.90 %	(6) BP

<sup>1</sup> Excludes acquisition-related additions during the period.

<sup>2</sup> Includes data-centric devices such as session-based tablets, monitoring devices and primarily wholesale automobile systems. Excludes postpaid tablets. See (5) below.

<sup>3</sup> Calculated by dividing the aggregate number of wireless subscribers who canceled service during a month divided by the total number of wireless subscribers at the beginning of that month. The churn rate for the period is equal to the average of the churn rate for each month of that period.

<sup>4</sup> 2017 excludes the impact of the 2G shutdown and a true-up to the reseller subscriber base, which were reflected in beginning of period subscribers.

<sup>5</sup> Beginning in July 2017, we are reporting prepaid IoT connections, which primarily consist of "connected" cars, as a component of prepaid subscribers, resulting in 97 additional prepaid net adds in the quarter. Had we restated our prior periods, prepaid net adds for the comparable periods would have been 381 in the third quarter of 2016, and 1,060 and 1,324 for the first nine months of, 2017 and 2016, respectively.

Operating income decreased \$76, or 1.4%, in the third quarter and \$191, or 1.2%, for the first nine months of 2017. The third-quarter operating income margin of AT&T Mobility increased from 29.6% in 2016 to 30.5% in 2017 and for the first nine months increased from 29.6% in 2016 to 30.3% in 2017. AT&T Mobility's third-quarter EBITDA margin increased from 41.2% in 2016 to 42.0% in 2017 and for the first nine months increased from 41.1% in 2016 to 41.9% in 2017. AT&T Mobility's third-quarter EBITDA service margin increased from 50.1% in 2016 to 50.4% in 2017 and for the first nine months increased from 49.8% in 2016 to 50.0% in 2017 (EBITDA service margin is operating income before depreciation and amortization, divided by total service revenues).

**Subscriber Relationships**

As the wireless industry continues to mature, future wireless growth will become increasingly dependent on our ability to offer innovative services, plans and devices and a wireless network that has sufficient spectrum and capacity to support these innovations on as broad a geographic basis as possible. To attract and retain subscribers in a maturing market, we have launched a wide variety of plans, including unlimited, as well as equipment installment programs. Beginning in the first quarter of 2017, we expanded our unlimited wireless data plans to make them available to customers that do not subscribe to our video services.

36

---

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

ARPU

Postpaid phone-only ARPU was \$58.29 for the third quarter and \$58.23 for the first nine months of 2017, compared to \$59.64 and \$59.66 in 2016. Postpaid phone-only ARPU plus equipment installment billings was \$68.95 for the third quarter and \$68.94 for the first nine months of 2017, compared to \$69.99 and \$69.83 in 2016. ARPU has been affected by customers shifting to unlimited plans, which decreases overage revenues; however, customers are adding additional devices helping to offset that decline.

Churn

The effective management of subscriber churn is critical to our ability to maximize revenue growth and to maintain and improve margins. Total churn was lower for the third quarter and first nine months of 2017. Postpaid churn was higher for the third quarter and first nine months of 2017, driven by higher tablet churn. Postpaid phone-only churn was lower in the third quarter and first nine months of 2017, despite competitive pressure in the industry.

Branded Subscribers

Branded subscribers increased 1.1% in the third quarter of 2017 when compared to June 30, 2017 and increased 2.4% when compared to September 30, 2016. Both the sequential and year-over-year increases reflect postpaid subscribers remaining essentially flat while prepaid subscribers grew 6.7% and 16.1%, respectively. Beginning in July 2017, we are reporting prepaid IoT connections, which primarily consist of "connected" cars where customers actively subscribe for vehicle connectivity, as a component of prepaid subscribers. The prepaid subscriber base at September 30, 2017 now includes approximately 543,000 subscribers that were formerly included in connected devices.

At September 30, 2017, 92% of our postpaid phone subscriber base used smartphones, compared to 90% at September 30, 2016, with more than 95% of phone sales during both years attributable to smartphones. Virtually all of our postpaid smartphone subscribers are on plans that provide for service on multiple devices at reduced rates, and such subscribers tend to have higher retention and lower churn rates. Device connections on our Mobile Share and unlimited wireless data plans now represent 86% of our postpaid customer base, compared to 83% at September 30, 2016. Such offerings are intended to encourage existing subscribers to upgrade their current services and/or add connected devices, attract subscribers from other providers and/or minimize subscriber churn.

Our equipment installment purchase programs, including AT&T Next, allow for postpaid subscribers to purchase certain devices in installments over a period of up to 30 months. Additionally, after a specified period of time, AT&T Next subscribers also have the right to trade in the original device for a new device with a new installment plan and have the remaining unpaid balance satisfied. For installment programs, we recognize equipment revenue at the time of the sale for the amount of the customer receivable, net of the fair value of the trade-in right guarantee and imputed interest. A significant percentage of our customers choosing equipment installment programs pay a lower monthly service charge, which results in lower service revenue recorded for these subscribers. At September 30, 2017, about 53% of the postpaid smartphone base is on an equipment installment program compared to 50% at September 30, 2016. Over 90% of postpaid smartphone gross adds and upgrades for all periods presented were either equipment installment plans or Bring Your Own Device (BYOD). While BYOD customers do not generate equipment revenue or expense, the service revenue helps improve our margins.

Connected Devices

Connected Devices includes data-centric devices such as session-based tablets, monitoring devices and primarily wholesale automobile systems. Connected device subscribers increased 5.0% during the third quarter when compared

to June 30, 2017 and 20.2% when compared to September 30, 2016. During the third quarter and first nine months of 2017, we added approximately 1.5 million and 4.7 million wholesale connected cars, respectively, through agreements with various carmakers, and experienced strong growth in other IoT connections as well. We believe that these connected car agreements give us the opportunity to create future retail relationships with the car owners.

OTHER BUSINESS MATTERS

**Time Warner Inc. Acquisition** In October 2016, we announced an agreement (Merger Agreement) to acquire Time Warner in a 50% cash and 50% stock transaction for \$107.50 per share of Time Warner common stock, or approximately \$85,400 at the date of the announcement (Merger). Each share of Time Warner common stock will be exchanged for \$53.75 per share in cash and a number of shares of AT&T common stock equal to the exchange ratio. The cash portion of the purchase price will be financed with new debt and cash. The transaction remains subject to review by the U.S. Department of Justice, but is

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

expected to close before year-end 2017. See Note 7 for additional details of the transaction and "Liquidity" for a discussion of our financing arrangements.

**FirstNet** On March 30, 2017, the First Responder Network Authority (FirstNet) announced its selection of AT&T to build and manage the first nationwide broadband network dedicated to America's first responders. FirstNet will provide 20 MHz of valuable telecommunications spectrum and success-based payments of \$6,500 over the next five years to support network buildout. We expect to spend about \$40,000, in part recoverable from FirstNet, over the life of the 25-year contract to build, operate and maintain the network. AT&T will construct and operate the network and provide sustainability payments to FirstNet. Sustainability payments are required to be used for the operating expenses of FirstNet and to fund network improvements included in our \$40,000 estimate. FirstNet's operating expenses are anticipated to be in the \$75-\$100 range annually, and when adjusted for inflation, we expect to be in the \$3,000 range over the life of the 25-year contract. After FirstNet's operating expenses are paid, we anticipate that the remaining amount, expected to be in the \$15,000 range, will be reinvested into the network. As of November 2, 2017, 30 states and territories have opted-in to the program, representing 38%, or approximately \$6,900, of this total sustainability payment commitment. The actual reach of the network and our investment over the 25-year period will be determined by the number of individual states and territories electing to participate in FirstNet.

States have until December 28, 2017 to elect to opt-out of the federally funded program, after which any state that did not formally make an election will automatically be opted-in. We do not expect FirstNet to materially impact our 2017 results.

**Litigation Challenging DIRECTV's NFL SUNDAY TICKET** More than two dozen putative class actions were filed in the U.S. District Courts for the Central District of California and the Southern District of New York against DIRECTV and the National Football League (NFL). These cases were brought by residential and commercial DIRECTV subscribers that have purchased NFL SUNDAY TICKET. The plaintiffs allege that (i) the 32 NFL teams have unlawfully agreed not to compete with each other in the market for nationally televised NFL football games and instead have "pooled" their broadcasts and assigned to the NFL the exclusive right to market them; and (ii) the NFL and DIRECTV have entered into an unlawful exclusive distribution agreement that allows DIRECTV to charge "supra-competitive" prices for the NFL SUNDAY TICKET package. The complaints seek unspecified treble damages and attorneys' fees along with injunctive relief. The first complaint, *Abrahamian v. National Football League, Inc., et al.*, was served in June 2015. In December 2015, the Judicial Panel on Multidistrict Litigation transferred the cases outside the Central District of California to that court for consolidation and management of pre-trial proceedings. In June 2016, the plaintiffs filed a consolidated amended complaint. We vigorously dispute the allegations the complaints have asserted. In August 2016, DIRECTV filed a motion to compel arbitration and the NFL defendants filed a motion to dismiss the complaint. In June 2017, the court granted the NFL defendants' motion to dismiss the complaint without leave to amend, finding that: (1) the plaintiffs did not plead a viable market; (2) the plaintiffs did not plead facts supporting the contention that the exclusive agreement between the NFL and DIRECTV harms competition; (3) the claims failed to overcome the fact that the NFL and its teams must cooperate to sell broadcasts; and (4) the plaintiffs do not have standing to challenge the horizontal agreement among the NFL and the teams. In light of the order granting the motion to dismiss, the court denied DIRECTV's motion to compel arbitration as moot. In July 2017, plaintiffs filed an appeal in the U.S. Court of Appeals for the Ninth Circuit, which is pending.

**Federal Trade Commission Litigation Involving DIRECTV** In March 2015, the Federal Trade Commission (FTC) filed a civil suit in the U.S. District Court for the Northern District of California against DIRECTV seeking injunctive



relief and money damages under Section 5 of the Federal Trade Commission Act and Section 4 of the Restore Online Shoppers' Confidence Act. The FTC's allegations concern DIRECTV's advertising, marketing and sale of programming packages. The FTC alleges that DIRECTV did not adequately disclose all relevant terms. We vigorously dispute these allegations. A bench trial began on August 14, 2017, and was suspended on August 25, 2017, after the FTC rested its case, so that the court could consider DIRECTV's motion for judgment. The hearing on the motion occurred on October 25, 2017, and the judge took it under advisement.

**Unlimited Data Plan Claims** In October 2014, the FTC filed a civil suit in the U.S. District Court for the Northern District of California against AT&T Mobility, LLC seeking injunctive relief and unspecified money damages under Section 5 of the Federal Trade Commission Act. The FTC's allegations concern the application of AT&T's Maximum Bit Rate (MBR) program to customers who enrolled in our Unlimited Data Plan from 2007-2010. MBR temporarily reduces in certain instances the download speeds of a small portion of our legacy Unlimited Data Plan customers each month after the customer exceeds a designated amount of data during the customer's billing cycle. MBR is an industry-standard practice that is designed to affect only the most data-intensive applications (such as video streaming). Texts, emails, tweets, social media

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

posts, internet browsing and many other applications are typically unaffected. Contrary to the FTC's allegations, our MBR program is permitted by our customer contracts, was fully disclosed in advance to our Unlimited Data Plan customers, and was implemented to protect the network for the benefit of all customers. In March 2015, our motion to dismiss the litigation on the grounds that the FTC lacked jurisdiction to file suit was denied. In May 2015, the Court granted our motion to certify its decision for immediate appeal. The United States Court of Appeals for the Ninth Circuit subsequently granted our petition to accept the appeal, and, on August 29, 2016, issued its decision reversing the district court and finding that the FTC lacked jurisdiction to proceed with the action. The FTC asked the Court of Appeals to reconsider the decision "en banc," which the Court agreed to do. The en banc hearing was held on September 19, 2017. We do not expect a decision until early 2018. In addition to the FTC case, several class actions have been filed also challenging our MBR program. We vigorously dispute the allegations the complaints have asserted.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

**Labor Contracts** As of September 30, 2017, we employed approximately 257,000 persons. Approximately 46% of our employees are represented by the Communications Workers of America, the International Brotherhood of Electrical Workers or other unions. After expiration of the agreements, work stoppages or labor disruptions may occur in the absence of new contracts or other agreements being reached.

A summary of labor contract negotiations, by region or employee group, is as follows:

Approximately 20,000 mobility employees across the country are covered by a contract that expired in early 2017. We continue to negotiate with labor representatives. On October 30, 2017, we presented a contract that provides for, among other things, compounded annual wage increases totaling nearly 10% over the term of the contract and continued health care coverage. The contract is subject to acceptance and ratification.

Approximately 15,000 traditional wireline employees in our West region are covered by a contract that expired in April 2016. In August, these employees, along with 2,300 legacy DIRECTV non-management employees, ratified a new four-year contract that will expire in April 2020.

COMPETITIVE AND REGULATORY ENVIRONMENT

**Overview** AT&T subsidiaries operating within the United States are subject to federal and state regulatory authorities. AT&T subsidiaries operating outside the United States are subject to the jurisdiction of national and supranational regulatory authorities in the markets where service is provided.

In the Telecommunications Act of 1996 (Telecom Act), Congress established a national policy framework intended to bring the benefits of competition and investment in advanced telecommunications facilities and services to all Americans by opening all telecommunications markets to competition and reducing or eliminating regulatory burdens that harm consumer welfare. Since the Telecom Act was passed, the Federal Communications Commission (FCC) and some state regulatory commissions have maintained or expanded certain regulatory requirements that were imposed decades ago on our traditional wireline subsidiaries when they operated as legal monopolies. However, based on their public statements and written opinions, we expect the new leadership at the FCC to chart a more predictable and balanced regulatory course that will encourage long-term investment and benefit consumers. In addition, we are pursuing, at both the state and federal levels, additional legislative and regulatory measures to reduce regulatory burdens that are no longer appropriate in a competitive telecommunications market and that inhibit our ability to compete more effectively and offer services wanted and needed by our customers, including initiatives to transition services from traditional networks to all IP-based networks. At the same time, we also seek to ensure that legacy regulations are not further extended to broadband or wireless services, which are subject to vigorous competition.

On April 20, 2017, the FCC adopted an order that maintains light touch pricing regulation of packet-based services, extends such light touch pricing regulation to high-speed TDM transport services and to most of our TDM channel termination services, based on a competitive market test for such services. For those services that do not qualify for light touch regulation, the order allows companies to offer volume and term discounts, as well as contract tariffs. Several parties appealed the FCC's decision. These appeals were consolidated in the U.S. Court of Appeals for the Eighth Circuit, where they remain pending.

In October 2016, a sharply divided FCC adopted new rules governing the use of customer information by providers of broadband internet access service. Those rules were more restrictive in certain respects than those governing other participants in the internet economy, including so-called "edge" providers such as Google and Facebook. On April 3,

2017, the President signed a resolution passed by Congress repealing the new rules under the Congressional Review Act, which prohibits the issuance of a new rule that is substantially the same as a rule repealed under its provisions, or the reissuance of the repealed rule, unless the new or reissued rule is specifically authorized by a subsequent act of Congress. In June 2017, the FCC released an order clarifying that providers of broadband internet access service continue to be subject to privacy requirements under section 222 of The Communications Act of 1934 (Communications Act), but not the more restrictive rules that were adopted in October 2016.

In February 2015, the FCC released an order classifying both fixed and mobile consumer broadband internet access services as telecommunications services, subject to Title II of the Communications Act. The FCC's decision significantly expanded its authority to regulate the provision of fixed and mobile broadband internet access services. AT&T and other providers of

40

---

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued  
Dollars in millions except per share and per subscriber amounts

broadband internet access services challenged the FCC's decision before the U.S. Court of Appeals for the D.C. Circuit. In June 2016, a panel of the Court of Appeals upheld the FCC's classification of broadband internet access and the attendant rules by a 2-1 vote. On May 1, 2017, the Court of Appeals denied requests for rehearing filed by AT&T and several other parties. In May 2017, the FCC initiated a proceeding to reverse its 2015 decision to classify broadband internet access services as telecommunications services. AT&T fully supports an open internet and believes that Congress should pass bipartisan legislation that codifies core principles of net neutrality while maintaining a stable regulatory environment conducive to investment, future innovation and economic growth. On September 28, 2017, AT&T and other parties filed with the United States Supreme Court petitions for certiorari to review the Court of Appeals decision.

We provide satellite video service through our subsidiary DIRECTV, whose satellites are licensed by the FCC. The Communications Act of 1934 and other related acts give the FCC broad authority to regulate the U.S. operations of DIRECTV. In addition, states representing a majority of our local service access lines have adopted legislation that enables us to provide IP-based service through a single statewide or state-approved franchise (as opposed to the need to acquire hundreds or even thousands of municipal-approved franchises) to offer a competitive video product. We also are supporting efforts to update and improve regulatory treatment for our services. Regulatory reform and passage of legislation is uncertain and depends on many factors.

We provide wireless services in robustly competitive markets, but are subject to substantial governmental regulation. Wireless communications providers must obtain licenses from the FCC to provide communications services at specified spectrum frequencies within specified geographic areas and must comply with the FCC rules and policies governing the use of the spectrum. While wireless communications providers' prices and offerings are generally not subject to state or local regulation, states sometimes attempt to regulate or legislate various aspects of wireless services, such as in the areas of consumer protection and the deployment of cell sites and equipment. The anticipated industry-wide deployment of 5G technology, which is needed to satisfy extensive demand for video and internet access, will involve significant deployment of "small cell" equipment and therefore increase the need for a quick permitting process.

The FCC has recognized that the explosive growth of bandwidth-intensive wireless data services requires the U.S. government to make more spectrum available. The FCC finished its most recent auction in April 2017 of certain spectrum that is currently used by broadcast television licensees (the "600 MHz Auction").

In May 2014, the FCC issued an order revising its policies governing mobile spectrum holdings. The FCC rejected the imposition of caps on the amount of spectrum any carrier could acquire, retaining its case-by-case review policy. Moreover, it increased the amount of spectrum that could be acquired before exceeding an aggregation "screen" that would automatically trigger closer scrutiny of a proposed transaction. On the other hand, it indicated that it will separately consider an acquisition of "low band" spectrum that exceeds one-third of the available low band spectrum as presumptively harmful to competition. The spectrum screen (including the low band screen) recently increased by 23 MHz. On balance, the order and the spectrum screen should allow AT&T to obtain additional spectrum to meet our customers' needs.

As the wireless industry continues to mature, future wireless growth will become increasingly dependent on our ability to offer innovative video and data services and a wireless network that has sufficient spectrum and capacity to support these innovations. We continue to invest significant capital in expanding our network capacity, as well as to

secure and utilize spectrum that meets our long-term needs. To that end, we have:

Submitted winning bids for 251 Advanced Wireless Services (AWS) spectrum licenses for a near-nationwide contiguous block of high-quality spectrum in the AWS-3 Auction.

Redeployed spectrum previously used for basic 2G services to support more advanced mobile internet services on our 3G and 4G networks.

Secured the FirstNet contract, which provides us with access to a nationwide low band 20 MHz of spectrum, assuming all states opt-in.

Invested in 5G and millimeter-wave technologies with our in-process acquisition of Fiber-Tower Corporation, which holds significant amounts of spectrum in the millimeter wave bands (28 GHz and 39 GHz) that the FCC recently reallocated for mobile broadband services. These bands will help to accelerate our entry into 5G services.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

Tax Reform On November 2, 2017, the Tax Cuts and Jobs Act was introduced in the U.S. House of Representatives. If enacted, we expect it would stimulate investment, job creation and economic growth which would result in a positive impact on demand for our services. As written, we anticipate the legislation will have a positive impact on our consolidated operations and cash flows.

LIQUIDITY AND CAPITAL RESOURCES

In anticipation of the Time Warner transaction, we had \$48,499 in cash and cash equivalents available at September 30, 2017. Cash and cash equivalents included cash of \$3,707 and money market funds and other cash equivalents of \$44,792. Approximately \$888 of our cash and cash equivalents resided in foreign jurisdictions and were primarily in foreign currencies; these funds are primarily used to meet working capital requirements of foreign operations.

Cash and cash equivalents increased \$42,711 since December 31, 2016. In the first nine months of 2017, cash inflows were primarily provided by the issuance of long-term debt, and cash receipts from operations, including cash from our sale and transfer of certain wireless equipment installment receivables to third parties. We also received a \$1,438 deposit refund from the FCC. These inflows were offset by cash used to meet the needs of the business, including, but not limited to, payment of operating expenses, funding capital expenditures, debt repayments, dividends to stockholders, and the acquisition of wireless spectrum and other operations. We discuss many of these factors in detail below.

Cash Provided by or Used in Operating Activities

During the first nine months of 2017, cash provided by operating activities was \$29,274, compared to \$29,202 for the first nine months of 2016. Higher operating cash flows in 2017 were primarily due to higher receipts from our sale of AT&T Next receivables and working capital improvements.

Cash Used in or Provided by Investing Activities

For the first nine months of 2017, cash used in investing activities totaled \$15,266 and consisted primarily of \$15,756 for capital expenditures, excluding interest during construction.

Investing activities also include a refund from the FCC in the amount of \$1,438 in April 2017, resulting from the conclusion of the FCC's 600 MHz Auction. We submitted winning bids to purchase spectrum licenses in 18 markets for which we paid \$910.

The majority of our capital expenditures are spent on our networks, our video services and related support systems. Capital expenditures, excluding interest during construction, increased \$473 in the first nine months. The increase was primarily due to our continued fiber buildout and timing of build schedules in 2017 compared with 2016.

Additionally, in connection with capital improvements, we negotiate favorable payment terms (referred to as vendor financing). For the first nine months of 2017, vendor financing related to capital investments was \$897. We do not report capital expenditures at the segment level.

We continue to expect our 2017 capital expenditures to be in the \$22,000 range, and we expect our capital expenditures to be in the 15% range of service revenues or lower for each of the years 2017 through 2019. The amount of capital expenditures is influenced by demand for services and products, capacity needs and network enhancements. Our capital spending takes into account existing tax law and does not reflect anticipated tax reform. We continue to

focus on ensuring DIRECTV merger commitments are met.

#### Cash Provided by or Used in Financing Activities

For the first nine months of 2017, cash provided by financing activities totaled \$28,703 and included net proceeds of \$46,761 primarily from the following long-term debt issuances:

- February issuance of \$1,250 of 3.200% global notes due 2022.
- February issuance of \$750 of 3.800% global notes due 2024.
- February issuance of \$2,000 of 4.250% global notes due 2027.
- February issuance of \$3,000 of 5.250% global notes due 2037.
- February issuance of \$2,000 of 5.450% global notes due 2047.
- February issuance of \$1,000 of 5.700% global notes due 2057.
- March issuance of \$1,430 of 5.500% global notes due 2047.

·March issuance of \$800 floating rate global notes due 2020. The floating rate for the notes is based upon the three-month London Interbank Offered Rate (LIBOR), reset quarterly, plus 65 basis points.

·March draw of \$300 on a private financing agreement with Banco Nacional de Mexico, S.A. due March 2019. The agreement contains terms similar to that provided under our syndicated credit arrangements; the interest rate is a market rate.



AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

May issuance of \$1,500 floating rate global notes due 2021. The floating rate for the notes is based upon the three-month LIBOR, reset quarterly, plus 95 basis points.

May issuance of CAD\$600 of 2.850% global notes due 2024 and CAD\$750 of 4.850% global notes due 2047 (together, equivalent to \$994, when issued).

June issuance of £1,000 of 3.550% global notes due 2037, subject to mandatory redemption (equivalent to \$1,282 when issued).

June issuance of €750 of 1.050% global notes due 2023, €1,750 of 1.800% global notes due 2026, €1,500 of 2.350% global notes due 2029, €1,750 of 3.150% global notes due 2036 and €1,250 of floating rate global notes due 2023. All except the 2036 global notes are subject to mandatory redemption (together, equivalent to \$7,883, when issued).

August issuance of \$750 of floating rate notes due 2023, \$1,750 of 2.85% global notes due 2023, \$3,000 of 3.40% global notes due 2024, \$5,000 of 3.90% global notes due 2027, \$4,500 of 4.90% global notes due 2037, \$5,000 of 5.15% global notes due 2050 and \$2,500 of 5.30% global notes due 2058. All are subject to mandatory redemption.

For notes subject to mandatory redemption (\$29,801), if we do not consummate the Time Warner acquisition pursuant to the merger agreement, on or prior to April 22, 2018, or, if prior to such date, the merger agreement is terminated, then in either case we must redeem certain of the notes at a redemption price equal to 101% of the principal amount of the notes, plus accrued but unpaid interest.

On October 27, 2017, we issued \$1,150 of 5.35% global notes due 2066. The underwriters have an option to purchase up to an additional \$173 aggregate principal amount within 30 days of the offering.

On October 30, 2017, we launched an exchange offer covering approximately \$24,000 of notes issued by AT&T Inc., DIRECTV Holdings LLC and DIRECTV Financing Co., Inc. due between 2020 and 2023. We may issue up to \$8,000 of new AT&T Inc. notes, subject to increase, due 2028 and 2030. Also on October 30, 2017, we offered to exchange approximately \$9,000 of high-coupon existing AT&T Inc. notes and existing subsidiary notes for new AT&T Inc. notes. The notes covered in the exchange have coupons ranging from 5.85% to 8.75% and maturities from 2022 to 2097. The existing AT&T Inc. notes may be exchanged for new AT&T Inc. notes due 2046 and the subsidiary bonds may be exchanged for new AT&T Inc. notes due 2046 or new AT&T Inc. notes with identical coupon and maturity as the existing subsidiary notes. We are also seeking consent of bondholders to modify the covenants of the subsidiary indentures to generally conform to AT&T Inc.'s indenture. The exchange offers will expire on November 28, 2017.

During the first nine months of 2017, we redeemed or repaid \$10,309 of debt, primarily consisting of the following:

- \$1,142 of 2.400% global notes due 2017.
- \$1,000 of 1.600% global notes due 2017.
- \$500 of floating rate notes due 2017.
- £750 of 5.875% global notes due 2017.
- \$750 repayment of a private financing agreement with Export Development Canada due 2017.
- \$1,150 of 1.700% global notes due 2017.
- \$4,155 repayment of amounts outstanding under our syndicated credit agreement.

Our weighted average interest rate of our entire long-term debt portfolio, including the impact of derivatives, was approximately 4.4% as of September 30, 2017, compared to 4.2% as of December 31, 2016. We had \$162,450 of total notes and debentures outstanding at September 30, 2017, which included Euro, British pound sterling, Swiss franc, Brazilian real, Mexican peso and Canadian dollar denominated debt that totaled approximately \$37,260.

As of September 30, 2017, we had approximately 388 million shares remaining from 2013 and 2014 authorizations from our Board of Directors to repurchase shares of our common stock. During the first nine months of 2017, we repurchased approximately 7 million shares totaling \$279 under these authorizations. In 2017, we intend to use free cash flow (operating cash flows less construction and capital expenditures) after dividends primarily to pay down debt.

We paid dividends of \$9,030 during the first nine months of 2017, compared with \$8,850 for the first nine months of 2016, primarily reflecting the increase in the quarterly dividend approved by our Board of Directors in October 2016. Dividends declared by our Board of Directors totaled \$0.49 per share in the third quarter and \$1.47 per share in the first nine months of 2017 and \$0.48 per share in the third quarter and \$1.44 for the first nine months of 2016. Our dividend policy considers the

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

expectations and requirements of stockholders, capital funding requirements of AT&T and long-term growth opportunities. It is our intent to provide the financial flexibility to allow our Board of Directors to consider dividend growth and to recommend an increase in dividends to be paid in future periods. All dividends remain subject to declaration by our Board of Directors.

At September 30, 2017, we had \$8,551 of debt maturing within one year, \$8,379 of which was related to long-term debt issuances. Debt maturing within one year includes the following notes that may be put back to us by the holders: \$1,000 of annual put reset securities issued by BellSouth that may be put back to us each April until maturity in 2021. An accreting zero-coupon note that may be redeemed each May until maturity in 2022. In May 2017, \$1 was redeemed by the holder for \$1. If the remainder of the zero-coupon note (issued for principal of \$500 in 2007) is held to maturity, the redemption amount will be \$1,029.

Credit Facilities

The following summary of our various credit and loan agreements does not purport to be complete and is qualified in its entirety by reference to each agreement filed as exhibits to our Annual Report on Form 10-K.

We use credit facilities as a tool in managing our liquidity status. In December 2015, we entered into a five-year \$12,000 revolving credit agreement of which no amounts are outstanding as of September 30, 2017. On September 5, 2017 we repaid all of the amounts outstanding under our \$9,155 syndicated credit agreement and terminated the facility. On September 29, 2017, we entered into a five-year \$2,250 syndicated term loan credit agreement containing (i) a \$750 term loan facility (the "Tranche A Facility"), (ii) a \$750 term loan facility (the "Tranche B Facility") and (iii) a \$750 term loan facility (the "Tranche C Facility"), with certain investment and commercial banks and The Bank of Nova Scotia, as administrative agent. No amounts are outstanding under the Tranche A Facility, the Tranche B Facility or the Tranche C Facility as of September 30, 2017.

We also enter into various credit arrangements supported by government agencies to support network equipment purchases.

In connection with our pending Merger with Time Warner, we entered into a \$30,000 bridge loan credit agreement ("Bridge Loan") and a \$10,000 term loan agreement ("Term Loan"). Following the August issuances of \$22,500 of global notes, we reduced the commitments under the Bridge Loan to \$0 and terminated the facility. No amounts will be borrowed under the Term Loan prior to the closing of the Merger. Borrowings under the Term Loan will be used solely to finance a portion of the cash to be paid in the Merger, the refinancing of debt of Time Warner and its subsidiaries and the payment of related expenses.

Each of our credit and loan agreements contains covenants that are customary for an issuer with an investment grade senior debt credit rating as well as a net debt-to-EBITDA financial ratio covenant requiring AT&T to maintain, as of the last day of each fiscal quarter, a ratio of not more than 3.5-to-1. As of September 30, 2017, we were in compliance with the covenants for our credit facilities.

Collateral Arrangements

During the first nine months of 2017, we received \$2,743 of additional cash collateral, on a net basis, from banks and other participants in our derivative arrangements. Cash postings under these arrangements vary with changes in credit ratings and netting agreements. At September 30, 2017, we had posted collateral assets of \$837 and received collateral

liabilities of \$338, compared to December 31, 2016, posted collateral assets of \$3,242 and no collateral liabilities. (See Note 6)

Other

Our total capital consists of debt (long-term debt and debt maturing within one year) and stockholders' equity. Our capital structure does not include debt issued by our equity method investments. At September 30, 2017, our debt ratio was 56.4%, compared to 50.1% at September 30, 2016, and 49.9% at December 31, 2016. Our net debt ratio was 39.7% at September 30, 2017, compared to 47.8% at September 30, 2016 and 47.5% at December 31, 2016. The debt ratio is affected by the same factors that affect total capital, and reflects our recent debt issuances and repayments.

During the first nine months of 2017, we received \$4,217 from the monetization of various assets, primarily the sale of certain equipment installment receivables. We plan to continue to explore similar opportunities.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued  
Dollars in millions except per share and per subscriber amounts

In 2013, we made a voluntary contribution of a preferred equity interest in AT&T Mobility II LLC (Mobility), the holding company for our U.S. wireless operations, to the pension trust used to pay benefits under our qualified pension plans. The preferred equity interest had a value of \$9,354 as of September 30, 2017, and \$8,477 as of December 31, 2016, does not have any voting rights and has a liquidation value of \$8,000. The trust is entitled to receive cumulative cash distributions of \$560 per annum, which are distributed quarterly in equal amounts. Mobility II distributed \$420 to the trust during the first nine months of 2017. So long as those distributions are made, the terms of the preferred equity interest will not impose any limitations on our ability to declare a dividend or repurchase shares.

During the third quarter, AT&T notified the trust and the fiduciary of the preferred interest that AT&T would not exercise its call option of the preferred interest until at least September 9, 2022, which raised the valuation of the preferred interest by approximately \$1,245.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

DISCUSSION AND RECONCILIATION OF NON-GAAP MEASURE

We believe the following measure is relevant and useful information to investors as it is used by management as a method of comparing performance with that of many of our competitors. This supplemental measure should be considered in addition to, but not as a substitute of, our consolidated and segment financial information.

Supplemental Operational Measure

We provide a supplemental discussion of our domestic wireless operations that is calculated by combining our Consumer Mobility and Business Solutions segments, and then adjusting to remove non-wireless operations. The following table presents a reconciliation of our supplemental AT&T Mobility results.

	Three Months Ended				September 30, 2016			
	September 30, 2017				September 30, 2016			
	Consumer	Business	Adjustments <sup>1</sup>	AT&T	Consumer	Business	Adjustments <sup>1</sup>	AT&T
	Mobility	Solutions		Mobility	Mobility	Solutions		Mobility
Operating Revenues								
Wireless service	\$6,507	\$8,034	\$ -	\$14,541	\$6,914	\$8,050	\$ -	\$14,964
Fixed strategic services	-	3,087	(3,087)	-	-	2,913	(2,913)	-
Legacy voice and data services	-	3,434	(3,434)	-	-	4,042	(4,042)	-
Other service and equipment	-	852	(852)	-	-	886	(886)	-
Wireless equipment	1,241	1,654	-	2,895	1,353	1,876	-	3,229
Total Operating Revenues	7,748	17,061	(7,373)	17,436	8,267	17,767	(7,841)	18,193
Operating Expenses								
Operations and support	4,551	10,233	(4,671)	10,113	4,751	10,925	(4,979)	10,697
EBITDA	3,197	6,828	(2,702)	7,323	3,516	6,842	(2,862)	7,496
Depreciation and amortization	877	2,325	(1,192)	2,010	944	2,539	(1,376)	2,107
Total Operating Expense	5,428	12,558	(5,863)	12,123	5,695	13,464	(6,355)	12,804
Operating Income	\$2,320	\$4,503	\$ (1,510)	\$5,313	\$2,572	\$4,303	\$ (1,486)	\$5,389

<sup>1</sup> Non-wireless (fixed) operations reported in Business Solutions segment.

AT&T INC.  
SEPTEMBER 30, 2017

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations - Continued

Dollars in millions except per share and per subscriber amounts

	Nine Months Ended September 30, 2017			AT&T Mobility	September 30, 2016			AT&T Mobility
	Consumer Mobility	Business Solutions	Adjustments <sup>1</sup>		Consumer Mobility	Business Solutions	Adjustments <sup>1</sup>	
<b>Operating Revenues</b>								
Wireless service	\$19,644	\$23,969	\$ -	\$43,613	\$20,805	\$23,868	\$ -	\$44,673
Fixed strategic services	-	9,089	(9,089 )	-	-	8,469	(8,469 )	-
Legacy voice and data services	-	10,572	(10,572 )	-	-	12,577	(12,577 )	-
Other service and equipment	-	2,513	(2,513 )	-	-	2,619	(2,619 )	-
Wireless equipment	3,635	4,873	-	8,508	3,976	5,422	-	9,398
<b>Total Operating Revenues</b>	<b>23,279</b>	<b>51,016</b>	<b>(22,174 )</b>	<b>52,121</b>	<b>24,781</b>	<b>52,955</b>	<b>(23,665 )</b>	<b>54,071</b>
<b>Operating Expenses</b>								
Operations and support	13,599	30,722	(14,013 )	30,308	14,343	32,584	(15,105 )	31,822
<b>EBITDA</b>	<b>9,680</b>	<b>20,294</b>	<b>(8,161 )</b>	<b>21,813</b>	<b>10,438</b>	<b>20,371</b>	<b>(8,560 )</b>	<b>22,249</b>
Depreciation and amortization	2,621	6,972	(3,594 )	5,999	2,798	7,568	(4,122 )	6,244
<b>Total Operating Expense</b>	<b>16,220</b>	<b>37,694</b>	<b>(17,607 )</b>	<b>36,307</b>	<b>17,141</b>	<b>40,152</b>	<b>(19,227 )</b>	<b>38,066</b>
<b>Operating Income</b>	<b>\$7,059</b>	<b>\$13,322</b>	<b>\$(4,567 )</b>	<b>\$15,814</b>	<b>\$7,640</b>	<b>\$12,803</b>	<b>\$(4,438 )</b>	<b>\$16,005</b>

<sup>1</sup> Non-wireless (fixed) operations reported in Business Solutions segment.

AT&T INC.  
SEPTEMBER 30, 2017

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Dollars in millions except per share amounts

At September 30, 2017, we had interest rate swaps with a notional value of \$10,775 and a fair value of \$11.

We have fixed-to-fixed and floating-to-fixed cross-currency swaps on foreign currency-denominated debt instruments with a U.S. dollar notional value of \$38,694 to hedge our exposure to changes in foreign currency exchange rates. These derivatives have been designated at inception and qualify as cash flow hedges with a net fair value of \$(842) at September 30, 2017.

Item 4. Controls and Procedures

The registrant maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed by the registrant is recorded, processed, summarized, accumulated and communicated to its management, including its principal executive and principal financial officers, to allow timely decisions regarding required disclosure, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. The chief executive officer and chief financial officer have performed an evaluation of the effectiveness of the design and operation of the registrant's disclosure controls and procedures as of September 30, 2017. Based on that evaluation, the chief executive officer and chief financial officer concluded that the registrant's disclosure controls and procedures were effective as of September 30, 2017.



AT&T INC.  
SEPTEMBER 30, 2017

CAUTIONARY LANGUAGE CONCERNING FORWARD-LOOKING STATEMENTS

Information set forth in this report contains forward-looking statements that are subject to risks and uncertainties, and actual results could differ materially. Many of these factors are discussed in more detail in the "Risk Factors" section. We claim the protection of the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995.

The following factors could cause our future results to differ materially from those expressed in the forward-looking statements:

Adverse economic and/or capital access changes in the markets served by us or in countries in which we have significant investments, including the impact on customer demand and our ability and our suppliers' ability to access financial markets at favorable rates and terms.

Changes in available technology and the effects of such changes, including product substitutions and deployment costs.

Increases in our benefit plans' costs, including increases due to adverse changes in the United States and foreign securities markets, resulting in worse-than-assumed investment returns and discount rates; adverse changes in mortality assumptions; adverse medical cost trends; and unfavorable or delayed implementation or repeal of healthcare legislation, regulations or related court decisions.

The final outcome of FCC and other federal, state or foreign government agency proceedings (including judicial review, if any, of such proceedings) involving issues that are important to our business, including, without limitation, special access and business data services; intercarrier compensation; interconnection obligations; pending Notices of Apparent Liability; the transition from legacy technologies to IP-based infrastructure, including the withdrawal of legacy TDM-based services; universal service; broadband deployment; wireless equipment siting regulations; E911 services; competition policy; privacy; net neutrality, including the FCC's order classifying broadband as Title II services subject to much more comprehensive regulation; unbundled network elements and other wholesale obligations; multi-channel video programming distributor services and equipment; availability of new spectrum, on fair and balanced terms; and wireless and satellite license awards and renewals.

The final outcome of state and federal legislative efforts involving issues that are important to our business, including deregulation of IP-based services, relief from Carrier of Last Resort obligations and elimination of state commission review of the withdrawal of services.

Enactment of additional state, local, federal and/or foreign regulatory and tax laws and regulations, or changes to existing standards and actions by tax agencies and judicial authorities including the resolution of disputes with any taxing jurisdictions, pertaining to our subsidiaries and foreign investments, including laws and regulations that reduce our incentive to invest in our networks, resulting in lower revenue growth and/or higher operating costs.

Our ability to absorb revenue losses caused by increasing competition, including offerings that use alternative technologies or delivery methods (e.g., cable, wireless, VoIP and over-the-top video service), subscriber reluctance to purchase new wireless handsets, and our ability to maintain capital expenditures.

The extent of competition including from governmental networks and other providers and the resulting pressure on customer totals and segment operating margins.

Our ability to develop attractive and profitable product/service offerings to offset increasing competition.

The ability of our competitors to offer product/service offerings at lower prices due to lower cost structures and regulatory and legislative actions adverse to us, including state regulatory proceedings relating to unbundled network elements and non-regulation of comparable alternative technologies (e.g., VoIP).

The continued development and delivery of attractive and profitable video and broadband offerings; the extent to which regulatory and build-out requirements apply to our offerings; our ability to match speeds offered by our competitors and the availability, cost and/or reliability of the various technologies and/or content required to provide such offerings.

Our continued ability to maintain margins, attract and offer a diverse portfolio of video, wireless service and devices and device financing plans.

The availability and cost of additional wireless spectrum and regulations and conditions relating to spectrum use, licensing, obtaining additional spectrum, technical standards and deployment and usage, including network management rules.

Our ability to manage growth in wireless video and data services, including network quality and acquisition of adequate spectrum at reasonable costs and terms.

The outcome of pending, threatened or potential litigation (which includes arbitrations), including, without limitation, patent and product safety claims by or against third parties.

The impact from major equipment failures on our networks, including satellites operated by DIRECTV; the effect of security breaches related to the network or customer information; our inability to obtain handsets, equipment/software or have handsets, equipment/software serviced in a timely and cost-effective manner from suppliers; and in the case of satellites launched, timely provisioning of services from vendors; or severe weather conditions, natural disasters, pandemics, energy shortages, wars or terrorist attacks.

The issuance by the Financial Accounting Standards Board or other accounting oversight bodies of new accounting standards or changes to existing standards.

Our ability to integrate our acquisition of DIRECTV.

Our ability to close our pending acquisition of Time Warner Inc. and successfully reorganize our operations, including the ability to manage various businesses in widely dispersed business locations and with decentralized management.

Our ability to adequately fund our wireless operations, including payment for additional spectrum, network upgrades and technological advancements.

Our increased exposure to video competition and foreign economies, including foreign exchange fluctuations as well as regulatory and political uncertainty.

Changes in our corporate strategies, such as changing network-related requirements or acquisitions and dispositions, which may require significant amounts of cash or stock, to respond to competition and regulatory, legislative and technological developments.

The uncertainty surrounding further congressional action to address spending reductions, which may result in a significant decrease in government spending and reluctance of businesses and consumers to spend in general.

The uncertainty and impact of anticipated regulatory and corporate tax reform, which may impact the overall economy and incentives for business investments.

Readers are cautioned that other factors discussed in this report, although not enumerated here, also could materially affect our future earnings.

AT&T INC.  
SEPTEMBER 30, 2017

PART II – OTHER INFORMATION

Dollars in millions except per share amounts

Item 1A. Risk Factors

We discuss in our Annual Report on Form 10-K various risks that may materially affect our business. We use this section to update this discussion to reflect material developments since our Form 10-K was filed. For the third quarter 2017, there were no such material developments.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(c) A summary of our repurchases of common stock during the third quarter of 2017 is as follows:

(a) Total Number of Shares (or Units) Purchased <sup>1, 2, 3</sup>	(b) Average Price Paid Per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs <sup>1</sup>	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) That May Yet Be Purchased Under The Plans or Programs
July 1, 2017 - 19,060	\$ 37.45	-	388,296,000
July 31, 2017 August 1, 2017 - 16,379	38.88	-	388,296,000
August 31, 2017 September 1, 2017 - 618,928	38.08	-	388,296,000
September 30, 2017 Total, 2017 - 654,367	\$ 38.10	-	

<sup>1</sup> In March 2014, our Board of Directors approved an additional authorization to repurchase up to 300 million shares of our common stock. In March 2013, our Board of Directors authorized the repurchase of up to an additional 300 million shares of our common stock.

The authorizations have no expiration date.

<sup>2</sup> Of the shares repurchased, 63,861 shares were acquired through the withholding of taxes on the vesting of restricted stock

and performance shares or on the exercise price of options.

<sup>3</sup> Of the shares repurchased, 590,506 shares were acquired through reimbursements from AT&T maintained Voluntary Employee Benefit

Association (VEBA) trusts.

AT&T INC.  
SEPTEMBER 30, 2017

Item 6. Exhibits

The following exhibits are filed or incorporated by reference as a part of this report:

Exhibit Number	Exhibit Description	Filed Herewith	Incorporated by Reference Form	Period Ending	Exhibit	Filing Date
<u>10-a</u>	<u>Resolution Regarding John Donovan</u>	x				
<u>10-b</u>	<u>Resolution Regarding John Stankey</u>	x				
<u>10-c</u>	<u>Resolution Regarding John Stephens</u>	x				
<u>10-d</u>	<u>AT&amp;T Health Plan 2005 Supplemental</u>	x				
<u>10-e</u>	<u>Employee Retirement Plan</u>		8-K		10.1	10/4/2017
<u>10-f</u>	<u>Term Loan Credit Agreement</u>	x				
<u>12</u>	<u>Computation of Ratios of Earnings to Fixed Charges</u>	x				
31	13a-14(a)/15d-14(a) Certifications					
	<u>31.1 Certification of Principal Executive Officer</u>	x				
	<u>31.2 Certification of Principal Financial Officer</u>	x				
<u>32</u>	<u>Section 1350 Certifications</u>	x				
101	XBRL Instance Document	x				

SIGNATURE

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

AT&T Inc.

/s/ John J. Stephens

November 3, 2017

John J. Stephens  
Senior Executive Vice President  
and Chief Financial Officer