SHENANDOAH TELECOMMUNICATIONS CO/VA/
Form 10-Q
August 08, 2012

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

FORM 10-Q

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

For the quarterly period ended June 30, 2012

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

For the transition period from__________ to __________

Commission File No.: 000-09881

SHENANDOAH TELECOMMUNICATIONS COMPANY
(Exact name of registrant as specified in its charter)

VIRGINIA	54-1162807
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

500 Shentel Way, Edinburg, Virginia 22824
(Address of principal executive offices) (Zip Code)

(540) 984-4141
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ 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 the definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer o Accelerated filer þ Non-accelerated filer o Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No þ

The number of shares of the registrant’s common stock outstanding on July 27, 2012 was 23,870,003.

SHENANDOAH TELECOMMUNICATIONS COMPANY
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SHENANDOAH TELECOMMUNICATIONS COMPANY AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands)

ASSETS	June 30, 2012	December 31, 2011
Current Assets		
Cash and cash equivalents	$21,312	$ 15,874
Accounts receivable, net	22,794	21,483
Income taxes receivable	-	12,495
Materials and supplies	7,520	7,469
Prepaid expenses and other	4,576	3,844
Assets held for sale	430	2,797
Deferred income taxes	155	502
Total current assets	56,787	64,464
Investments, including $1,915 and $2,160 carried at fair value	8,215	8,305
Property, plant and equipment, net	313,710	310,754
Other Assets		
Intangible assets, net	77,638	81,346
Cost in excess of net assets of businesses acquired	10,962	10,962
Deferred charges and other assets, net	4,677	4,148
Net other assets	93,277	96,456
Total assets	$471,989	$ 479,979

See accompanying notes to unaudited condensed consolidated financial statements.

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SHENANDOAH TELECOMMUNICATIONS COMPANY AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands)

LIABILITIES AND SHAREHOLDERS' EQUITY	June 30, 2012	December 31, 2011
Current Liabilities		
Current maturities of long-term debt	$21,920	$ 21,913
Accounts payable	10,314	11,708
Advanced billings and customer deposits	10,457	10,647
Accrued compensation	1,983	2,094
Liabilities held for sale	18	267
Income taxes payable	2,329	-
Accrued liabilities and other	7,562	8,950
Total current liabilities	54,583	55,579
Long-term debt, less current maturities	147,773	158,662
Other Long-Term Liabilities		
Deferred income taxes	45,289	51,675
Deferred lease payable	4,395	4,174
Asset retirement obligations	5,804	7,610
Other liabilities	5,670	4,620
Total other liabilities	61,158	68,079
Commitments and Contingencies		
Shareholders' Equity		
Common stock	22,833	22,043
Retained earnings	185,642	175,616
Total shareholders' equity	208,475	197,659
Total liabilities and shareholders' equity	$471,989	$ 479,979

See accompanying notes to unaudited condensed consolidated financial statements.

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SHENANDOAH TELECOMMUNICATIONS COMPANY AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share amounts)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Operating revenues	$ 71,378	$ 61,555	$ 140,201	$ 121,983
Operating expenses:				
Cost of goods and services, exclusive of depreciation and amortization shown separately below	29,969	25,216	58,998	51,277
Selling, general and administrative, exclusive of depreciation and amortization shown separately below	15,013	13,901	30,182	27,239
Depreciation and amortization	15,259	14,444	31,066	28,382
Total operating expenses	60,241	53,561	120,246	106,898
Operating income	11,137	7,994	19,955	15,085
Other income (expense):				
Interest expense	(1,522)	(2,846)	(3,317)	(4,665)
Gain (loss) on investments, net	132	(124)	602	(249)
Non-operating income, net	259	290	447	508
Income from continuing operations before income taxes	10,006	5,314	17,687	10,679
Income tax expense	4,284	2,276	7,558	4,581
Net income from continuing operations	5,722	3,038	10,129	6,098
Losses from discontinued operations, net of tax benefits of $106, $16, $68 and $54, respectively	(162)	(46)	(103)	(79)
Net income	$ 5,560	$ 2,992	$ 10,026	$ 6,019
Basic and diluted income (loss) per share:				
Net income from continuing operations	$ 0.24	$ 0.13	$ 0.42	$ 0.25
Losses from discontinued operations	(0.01)	-	-	-
Net income	$ 0.23	$ 0.13	$ 0.42	$ 0.25
Weighted average shares outstanding, basic	23,855	23,772	23,849	23,769
Weighted average shares, diluted	23,892	23,797	23,880	23,823

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SHENANDOAH TELECOMMUNICATIONS COMPANY AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
AND COMPREHENSIVE INCOME
(in thousands, except per share amounts)

	Shares	Common Stock	Retained Earnings	Total
Balance, December 31, 2010	23,767	$19,833	$170,472	$190,305
Net income	-	-	12,993	12,993
Dividends declared ($0.33 per share)	-	-	(7,849)	(7,849)
Dividends reinvested in common stock	51	529	-	529
Stock-based compensation	-	1,718	-	1,718
Common stock issued through exercise of incentive stock options	5	37	-	37
Common stock issued for share awards	19	-	-	-
Common stock issued	1	13	-	13
Common stock repurchased	(5)	(92)	-	(92)
Net excess tax benefit from stock options exercised and stock awards	-	5	-	5
Balance, December 31, 2011	23,838	$22,043	$175,616	$197,659
Net income	-	-	10,026	10,026
Stock-based compensation	-	996	-	996
Common stock issued for share awards	45	-	-	-
Common stock repurchased	(13)	(143)	-	(143)
Common stock issued	-	4	-	4
Net tax deficiency from stock awards	-	(67)	-	(67)
Balance, June 30, 2012	23,870	$22,833	$185,642	$208,475

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SHENANDOAH TELECOMMUNICATIONS COMPANY AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Six Months Ended June 30, 2012	2011
Cash Flows From Operating Activities		
Net income	$10,026	$6,019
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	27,347	22,333
Amortization	3,719	6,049
Provision for bad debt	1,233	1,929
Stock based compensation expense	996	902
Deferred income taxes	(6,106)	579
Net loss on disposal of equipment	12	111
Realized (gain) loss on disposal of investments	(36)	27
Unrealized gains on investments	(96)	(104)
Net (gain) loss from patronage and equity investments	(638)	173
Other	676	113
Changes in assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	(3,641)	(1,919)
Materials and supplies	(51)	(216)
Income taxes receivable	-	(843)
Increase (decrease) in:		
Accounts payable	(1,429)	(1,224)
Deferred lease payable	221	214
Income taxes payable	14,824	-
Other prepaids, deferrals and accruals	(2,581)	198
Net cash provided by operating activities	$44,476	$34,341
Cash Flows From Investing Activities		
Purchase and construction of property, plant and equipment	$(32,299)	$(31,631)
Proceeds from sale of assets	3,265	920
Proceeds from sale of equipment	156	184
Purchase of investment securities	-	(84)
Proceeds from sale of investment securities	861	386
Net cash used in investing activities	$(28,017)	$(30,225)

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SHENANDOAH TELECOMMUNICATIONS COMPANY AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Cash Flows From Financing Activities		
Principal payments on long-term debt	$(10,882)	$(6,054)
Repurchases of stock	(143)	(92)
Proceeds from exercise of incentive stock options	4	8
Net cash used in financing activities	$(11,021)	$(6,138)
Net increase (decrease) in cash and cash equivalents	$5,438	$(2,022)
Cash and cash equivalents:		
Beginning	15,874	27,453
Ending	$21,312	$25,431
Supplemental Disclosures of Cash Flow Information		
Cash payments for:		
Interest	$3,173	$3,872
Income taxes (received) paid	$(1,228)	$4,793

See accompanying notes to unaudited condensed consolidated financial statements.

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SHENANDOAH TELECOMMUNICATIONS COMPANY AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The interim condensed consolidated financial statements of Shenandoah Telecommunications Company and Subsidiaries (collectively, the “Company”) are unaudited. In the opinion of management, all adjustments necessary for a fair presentation of the interim results have been reflected therein. All such adjustments were of a normal and recurring nature. These statements should be read in conjunction with the consolidated financial statements and related notes in the Company’s Annual Report on Form 10-K for the year ended December 31, 2011. The balance sheet information at December 31, 2011 was derived from the audited December 31, 2011 consolidated balance sheet. Operating revenues and income from operations for any interim period are not necessarily indicative of results that may be expected for the entire year.

2. Discontinued Operations

In September 2008, the Company announced its intention to sell its Converged Services operation, and the related assets and liabilities were reclassified as held for sale in the consolidated balance sheet and the historical operating results were reclassified as discontinued operations. Depreciation and amortization on long-lived assets was also discontinued. As previously reported in prior years, the Company recorded impairment charges.

In several transactions during 2011, the Company sold service contracts and related equipment for Converged Services’ properties to third-party purchasers, receiving cash proceeds of $3.0 million (with an additional $2.3 million in proceeds placed in escrow). The total proceeds approximated the carrying value of the assets sold in each transaction.

During the first quarter of 2012, the Company sold service contracts and related equipment for Converged Services’ properties to third party purchasers, receiving cash proceeds of $1.1 million, with an additional $0.4 million placed in escrow. The total proceeds approximated the carrying value of the assets sold.

During the second quarter of 2012, the Company sold service contracts and related equipment for Converged Services’ properties to third party purchasers, receiving cash proceeds of $0.3 million, with an additional $0.1 million placed in escrow. The total proceeds approximated the carrying value of the assets sold. During this same quarter, the Company collected $1.8 million in cash from previously established escrow receivables.

At June 30, 2012, the Company had seven remaining properties. The Company is working with the purchasers and owners of five properties to complete negotiated sale transactions in the next 90 days and is in the process of ending its relationship with the remaining two. No additional impairments are anticipated.

Assets and liabilities held for sale consisted of the following (in thousands):

	June 30, 2012	December 31, 2011
Assets held for sale:		
Property, plant and equipment, net	$ 244	$ 2,424
Other assets	186	373
	$ 430	$ 2,797
Liabilities:		
Other liabilities	$ 18	$ 267

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Discontinued operations included the following amounts of operating revenue and income (loss) before income taxes:

(in thousands)	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011
Operating revenues	$ 200	$ 3,031
Earnings (loss) before income taxes	$ (268)	$ 62

	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Operating revenues	$ 965	$ 6,337
Earnings (loss) before income taxes	$ (171)	$ (133)

3. Property, Plant and Equipment

Property, plant and equipment consisted of the following (in thousands):

	June 30, 2012	December 31, 2011
Plant in service	$ 554,713	$ 536,267
Plant under construction	23,479	12,389
	578,192	548,656
Less accumulated amortization and depreciation	264,482	237,902
Net property, plant and equipment	$ 313,710	$ 310,754

4. Earnings per share

Basic net income (loss) per share was computed on the weighted average number of shares outstanding. Diluted net income (loss) per share was computed under the treasury stock method, assuming the conversion as of the beginning of the period, for all dilutive stock options. Of 713 thousand and 521 thousand shares and options outstanding at June 30, 2012 and 2011, respectively, 500 thousand and 210 thousand were anti-dilutive, respectively. These options have been excluded from the computations of diluted earnings per share for their respective period. There were no adjustments to net income for either period.

5. Investments Carried at Fair Value

Investments include $1.9 million and $2.2 million of investments carried at fair value as of June 30, 2012 and December 31, 2011, respectively, consisting of equity, bond and money market mutual funds. These investments were acquired under a rabbi trust arrangement related to a non-qualified supplemental retirement plan maintained by the Company. During the six months ended June 30, 2012, the Company recognized $36 thousand in net gains on dispositions of investments, recognized $25 thousand in dividend and interest income from investments, and recognized net unrealized gains of $96 thousand on these investments. The Company also received $402 thousand distributed from the rabbi trust in connection with a payout from the non-qualified supplemental retirement plan to a participant. Fair values for these investments held under the rabbi trust were determined by Level 1 quoted market prices for the underlying mutual funds.

6. Financial Instruments

Financial instruments on the consolidated balance sheets that approximate fair value include: cash and cash equivalents, receivables, investments carried at fair value, payables, accrued liabilities, interest rate swap and variable rate long-term debt.

The Company measures its interest rate swap at fair value based on information provided by the counterparty and recognizes it as a liability on the Company's condensed consolidated balance sheet. Changes in the fair value of the swap are recognized in interest expense, as the Company did not designate the swap agreement as a cash flow hedge for accounting purposes.

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7. Segment Information

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision makers. The Company has three reportable segments, which the Company operates and manages as strategic business units organized by lines of business: (1) Wireless, (2) Wireline, and (3) Cable. A fourth segment, Other, primarily includes Shenandoah Telecommunications Company, the parent holding company as well as certain general and administrative costs historically charged to Converged Services that cannot be allocated to discontinued operations.

The Wireless segment provides digital wireless service to a portion of a four-state area covering the region from Harrisburg, York and Altoona, Pennsylvania, to Harrisonburg, Virginia, as a Sprint PCS Affiliate of Sprint Nextel. This segment also owns cell site towers built on leased land, and leases space on these towers to both affiliates and non-affiliated service providers.

The Cable segment provides video, internet and voice services in Virginia, West Virginia and Maryland.

The Wireline segment provides regulated and unregulated voice services, dial-up and DSL internet access, and long distance access services throughout Shenandoah County and portions of northwestern Augusta and Rockingham Counties, Virginia, and leases fiber optic facilities throughout the northern Shenandoah Valley of Virginia, northern Virginia and adjacent areas along the Interstate 81 corridor, including portions of West Virginia and Maryland.

Selected financial data for each segment is as follows:

Three months ended June 30, 2012

(in thousands)

	Wireless	Wireline	Cable	Other	Eliminations	Consolidated Totals
External revenues						
Service revenues	$40,187	$3,664	$16,356	$-	$ -	$ 60,207
Other	3,233	5,361	2,577	-	-	11,171
Total external revenues	43,420	9,025	18,933	-	-	71,378
Internal revenues	843	4,757	79	-	(5,679)	-
Total operating revenues	44,263	13,782	19,012	-	(5,679)	71,378
Operating expenses						
Costs of goods and services, exclusive of depreciation and amortization shown separately below	16,917	6,518	11,560	7	(5,033)	29,969
Selling, general and administrative, exclusive of depreciation and amortization shown separately below	8,102	1,638	5,254	665	(646)	15,013
Depreciation and amortization	6,753	2,285	6,203	18	-	15,259
Total operating expenses	31,772	10,441	23,017	690	(5,679)	60,241
Operating income (loss)	12,491	3,341	(4,005)	(690)	-	11,137

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Three months ended June 30, 2011

(in thousands)

	Wireless	Wireline	Cable	Other	Eliminations	Consolidated Totals
External revenues						
Service revenues	$33,806	$3,660	$14,602	$-	$ -	$ 52,068
Other	2,927	4,407	2,153	-	-	9,487
Total external revenues	36,733	8,067	16,755	-	-	61,555
Internal revenues	801	4,199	79	-	(5,079)	-
Total operating revenues	37,534	12,266	16,834	-	(5,079)	61,555
Operating expenses						
Costs of goods and services, exclusive of depreciation and amortization shown separately below	13,391	4,817	11,435	30	(4,457)	25,216
Selling, general and administrative, exclusive of depreciation and amortization shown separately below	7,651	1,866	4,234	772	(622)	13,901
Depreciation and amortization	6,140	2,155	6,088	61	-	14,444
Total operating expenses	27,182	8,838	21,757	863	(5,079)	53,561
Operating income (loss)	10,352	3,428	(4,923)	(863)	-	7,994

Six months ended June 30, 2012

(in thousands)

	Wireless	Wireline	Cable	Other	Eliminations	Consolidated Totals
External revenues						
Service revenues	$78,589	$7,531	$32,410	$-	$ -	$ 118,530
Other	6,684	9,950	5,037	-	-	21,671
Total external revenues	85,273	17,481	37,447	-	-	140,201
Internal revenues	1,658	9,210	150	-	(11,018)	-
Total operating revenues	86,931	26,691	37,597	-	(11,018)	140,201
Operating expenses						
Costs of goods and services, exclusive of depreciation and amortization shown separately below	33,310	11,747	23,786	24	(9,869)	58,998
Selling, general and administrative, exclusive of depreciation and amortization shown separately below	16,096	3,354	10,301	1,580	(1,149)	30,182
Depreciation and amortization	14,510	4,458	12,055	43	-	31,066
Total operating expenses	63,916	19,559	46,142	1,647	(11,018)	120,246
Operating income (loss)	23,015	7,132	(8,545)	(1,647)	-	19,955

Six months ended June 30, 2011

(in thousands)

	Wireless	Wireline	Cable	Other	Eliminations	Consolidated Totals
External revenues						
Service revenues	$66,010	$7,245	$29,062	$-	$ -	$ 102,317
Other	6,402	9,077	4,187	-	-	19,666
Total external revenues	72,412	16,322	33,249	-	-	121,983
Internal revenues	1,590	8,028	116	-	(9,734)	-
Total operating revenues	74,002	24,350	33,365	-	(9,734)	121,983
Operating expenses						
Costs of goods and services, exclusive of depreciation and amortization shown separately below	27,004	9,350	23,359	64	(8,500)	51,277
Selling, general and administrative, exclusive of depreciation and amortization shown separately below	14,197	3,667	8,863	1,746	(1,234)	27,239
Depreciation and amortization	12,374	4,105	11,786	117	-	28,382
Total operating expenses	53,575	17,122	44,008	1,927	(9,734)	106,898
Operating income (loss)	20,427	7,228	(10,643)	(1,927)	-	15,085

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A reconciliation of the total of the reportable segments' operating income to consolidated income from continuing operations before income taxes is as follows:

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011
Total consolidated operating income	$ 11,137	$ 7,994
Interest expense	(1,522)	(2,846)
Non-operating income (expense), net	391	166
Income from continuing operations before income taxes	$ 10,006	$ 5,314

	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Total consolidated operating income	$ 19,955	$ 15,085
Interest expense	(3,317)	(4,665)
Non-operating income (expense), net	1,049	259
Income from continuing operations before income taxes	$ 17,687	$ 10,679

The Company's assets by segment are as follows:

(in thousands)

	June 30, 2012	December 31, 2011
Wireless	$ 132,272	$ 147,093
Cable	213,850	212,683
Wireline	82,833	84,456
Other (includes assets held for sale)	402,175	381,230
Combined totals	831,130	825,462
Inter-segment eliminations	(359,141)	(345,483)
Consolidated totals	$ 471,989	$ 479,979

8. Income Taxes

The Company files U.S. federal income tax returns and various state and local income tax returns. With few exceptions, years prior to 2008 are no longer subject to examination. The Company is under audit in the state of Maryland for the 2007, 2008 and 2009 tax years, and in the state of Pennsylvania for the 2009 tax year. No other state or federal income tax audits were in process as of June 30, 2012.

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9. Long-Term Debt

As of June 30, 2012 and December 31, 2011, the Company's outstanding long-term debt consisted of the following:

(in thousands)

	June 2012	December 2011
CoBank (fixed term loan)	$ 3,445	$ 4,524
CoBank Term Loan A	165,855	175,565
Other debt	393	486
	169,693	180,575
Current maturities	21,920	21,913
Total long-term debt	$ 147,773	$ 158,662

As of June 30, 2012, the Company was in compliance with the covenants in its Credit Agreement.

10. Asset Retirement Obligations

The Company records the fair value of an asset retirement obligation as a liability in the period in which it incurs a legal obligation associated with the retirement of tangible long-lived assets that results from acquisition, construction, development and/or normal use of the assets. The Company also records a corresponding asset, which is depreciated over the life of the tangible long-lived asset. Subsequent to the initial measurement of the asset retirement obligation, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation.

During the second quarter of 2012, new information became available regarding the cost to remove cell site improvements. The Company recorded a one-time adjustment to wireless segment asset retirement obligation liabilities to reflect changes in the estimated future cash flows underlying the obligation to remove cell site improvements. As a result of the adjustment, the company recorded a decrease of $2.0 million to asset retirement liabilities and a decrease of $1.1 million to asset retirement obligation asset. Additionally, the Company recognized a $0.9 million decrease in depreciation expense for the quarter. The Company expects to charge asset removal costs associated with network upgrades against the liability established for removal of cell site improvements.

Changes in the liability for asset removal obligations for the six months and twelve months ended June 30, 2012 and December 31, 2011 are summarized below (in thousands):

	June 2012	December 2011
Balance at beginning of year	$ 7,610	$ 6,542
Revisions to previous estimates	(1,973)	-
Additional liabilities accrued	-	556
Accretion expense	167	512
Balance at end of period	$ 5,804	7,610

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

This management’s discussion and analysis includes “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. When used in this report, the words “anticipate,” “believe,” “estimate,” “expect,” “intend,” “plan” and similar expressions as they relate to Shenandoah Telecommunications Company or its management are intended to identify these forward-looking statements. All statements regarding Shenandoah Telecommunications Company’s expected future financial position and operating results, business strategy, financing plans, forecasted trends relating to the markets in which Shenandoah Telecommunications Company operates and similar matters are forward-looking statements. We cannot assure you that the Company’s expectations expressed or implied in these forward-looking statements will turn out to be correct. The Company’s actual results could be materially different from its expectations because of various factors, including those discussed below and under the caption “Risk Factors” in the Company’s Annual Report on Form 10-K for its fiscal year ended December 31, 2011. The following management’s discussion and analysis should be read in conjunction with the Company’s Annual Report on Form 10-K for its fiscal year ended December 31, 2011, including the financial statements and related notes included therein.

General

Overview. Shenandoah Telecommunications Company is a diversified telecommunications company providing both regulated and unregulated telecommunications services through its wholly owned subsidiaries. These subsidiaries provide wireless personal communications services (as a Sprint PCS Affiliate of Sprint Nextel), local exchange telephone services, video, internet and data services, long distance, fiber optics facilities, and leased tower facilities. The Company has the following three reporting segments, which it operates and manages as strategic business units organized by lines of business:

* The Wireless segment provides digital wireless service to a portion of a four-state area covering the region from Harrisburg, York and Altoona, Pennsylvania, to Harrisonburg, Virginia, as a Sprint PCS Affiliate of Sprint Nextel. This segment also owns cell site towers built on leased land, and leases space on these towers to both affiliates and non-affiliated service providers.

* The Cable segment provides video, internet and voice services in franchise areas in Virginia, West Virginia and Maryland.

* The Wireline segment provides regulated and unregulated voice services, dial-up and DSL internet access, and long-distance access services throughout Shenandoah County and portions of Rockingham and Augusta Counties, Virginia, and leases fiber optic facilities, throughout the northern Shenandoah Valley of Virginia, northern Virginia and adjacent areas along the Interstate 81 corridor, including portions of West Virginia and Maryland.

* A fourth segment, Other, primarily includes Shenandoah Telecommunications Company, the parent holding company, as well as certain general and administrative costs historically charged to Converged Services that cannot be allocated to discontinued operations.

During the first quarter of 2012, the Company entered into agreements with Sprint Nextel and Alcatel-Lucent to begin updating the Company’s Wireless network. The update will use base station equipment to be acquired from Alcatel-Lucent in conjunction with Sprint Nextel’s wireless network upgrade plan known as Network Vision.

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During the second quarter of 2012, the Company upgraded its wireless switch and began replacing cell site equipment, completing replacements at ten cell sites. The Company expects to replace all of its existing cell site equipment by the end of 2013. The Company has accelerated depreciation on these assets so that net book value at time of trade-in will equal the expected value to be realized upon trade-in. Depreciation expense for the three months and six months ended June 30, 2012, included approximately $1.8 million and $4.0 million, respectively, of accelerated depreciation on Wireless segment equipment. The Company expects accelerated depreciation expense in the Wireless segment to remain at similar elevated levels through the remainder of 2012, and at lower but still elevated levels in 2013. In the three and six months ended June 30, 2012, the Company recognized a favorable one-time adjustment to Wireless segment depreciation expense related to asset retirement obligations it had previously overestimated. The Company also expects Wireless segment operating expenses to begin to increase in the near future as changes to backhaul arrangements and cell site lease agreements related to the Network Vision upgrade take effect.

In September 2008, the Company announced its intention to sell its Converged Services operation, and the related assets and liabilities were reclassified as held for sale in the consolidated balance sheet and the historical operating results were reclassified as discontinued operations. Depreciation and amortization on long-lived assets was also discontinued. During 2009, 2010 and 2011, the Company recorded impairment charges totaling $20.0 million ($12.2 million, net of tax). Most of the impairment charge was recorded in 2009.

In several transactions during 2011, the Company sold service contracts and related equipment for Converged Services’ properties to third-party purchasers, receiving cash proceeds of $3.0 million (with an additional $2.3 million in proceeds placed in escrow). The total proceeds approximated the carrying value of the assets sold in each transaction.

During the first quarter of 2012, the Company sold service contracts and related equipment for Converged Services’ properties to third party purchasers, receiving cash proceeds of $1.1 million, with an additional $0.4 million placed in escrow. The total proceeds approximated the carrying value of the assets sold.

During the second quarter of 2012, the Company sold service contracts and related equipment for Converged Services’ properties to third party purchasers, receiving cash proceeds of $0.3 million, with an additional $0.1 million placed in escrow. The total proceeds approximated the carrying value of the assets sold. The Company collected $1.8 million in cash from previously established escrow receivables.

At June 30, 2012, the Company had seven remaining properties. The Company is working with the purchasers and owners of five properties to complete negotiated sale transactions in the next 90 days and is in the process of ending its relationship with the remaining two. No additional impairments are anticipated.

Results of Operations

Three Months Ended June 30, 2012 Compared with the Three Months Ended June 30, 2011

Consolidated Results

The Company’s consolidated results from continuing operations for the second quarters of 2012 and 2011 are summarized as follows:

(in thousands)	Three Months Ended June 30,		Change	
	2012	2011	$	%

Operating revenues	$	71,378		$	61,555		$	9,823	16.0	
Operating expenses		60,241			53,561			6,680	12.5	
Operating income		11,137			7,994			3,143	39.3	
Interest expense		(1,522	)		(2,846	)		1,324	46.5	
Other income (expense)		391			166			225	135.5	
Income before taxes		10,006			5,314			4,692	88.3	
Income tax expense		4,284			2,276			(2,008)	(88.2	)
Net income from continuing operations	$	5,722		$	3,038		$	2,684	88.3	

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Operating revenues

For the three months ended June 30, 2012, operating revenues increased $9.8 million, or 16.0%. Wireless segment revenues increased $6.7 million, cable segment revenues increased $2.2 million, and wireline segment revenues increased $0.9 million after eliminations. Postpaid PCS service revenues increased $3.9 million over the second quarter of 2011, while prepaid PCS service revenues increased $2.5 million. PCS and cable segment service revenue increases reflect subscriber count increases and increases in revenue per subscriber. Wireline revenue increases resulted primarily from increases in circuits in service.

Operating expenses

For the three months ended June 30, 2012, operating expenses increased $6.7 million, or 12.5%, compared to the 2011 period. This increase included $0.7 million of additional depreciation and amortization expense, primarily due to $1.8 million of accelerated depreciation related to the Company's plans to replace its wireless cell site equipment as part of its involvement in Sprint Nextel's Network Vision upgrade plan, offset by a favorable one-time adjustment of $0.9 million related to adjustments of asset retirement costs, reflected as a reduction in depreciation expense. Costs of goods and services increased $4.8 million, due to $1.8 million in additional network and backhaul costs associated with providing wireless data capacity and expanded services in our cable segment, and to increased handset costs in the wireless segment. Postpaid handset costs increased $1.5 million while prepaid handset subsidies increased $1.0 million in the second quarter of 2012 relative to the second quarter of 2011. The increase in postpaid handset costs is largely due to the $1.1 million incremental cost of the iPhone, which the Company began selling in the fourth quarter of 2011. The increase in prepaid handset subsidies is due to an increase in the rate per handset charged by Sprint Nextel. Increases of $1.1 million in selling, general and administrative expenses largely resulted from increased sales and marketing costs in the Cable segment.

Interest expense

The decrease in interest expense resulted from four factors. During the second quarter of 2011 the Company recorded $0.6 million in interest expense, representing the change from March 31, 2011, in the fair value of the Company's interest rate swap contract. The Company also reversed $0.4 million of interest previously capitalized to plant under construction, increasing interest expense for the second quarter of 2011. During the second quarter of 2012, the Company's spread over LIBOR on its debt was reduced by 25 basis points, while the outstanding balance of long-term debt has declined by $19.4 million, contributing to lower interest expense in second quarter 2012 compared to second quarter 2011.

Net income from continuing operations

For the three months ended June 30, 2012, net income from continuing operations increased $2.7 million, reflecting growth in subscriber counts and revenue per subscriber in both the Wireless and Cable segments, increased revenues for fiber and other facilities in the Wireline segment, partially offset by increases in operating expenses incurred in support of this growth and the accelerated depreciation charges associated with the Company's participation in Sprint Nextel's wireless network upgrade program known as Network Vision, combined with lower interest expenses.

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Six Months Ended June 30, 2012 Compared with the Six Months Ended June 30, 2011

Consolidated Results

The Company's consolidated results from continuing operations for the first six months of 2012 and 2011 are summarized as follows:

(in thousands)	Six Months Ended June 30, 2012	2011	Change $	%
Operating revenues	$ 140,201	$ 121,983	$ 18,218	14.9
Operating expenses	120,246			