ALASKA COMMUNICATIONS SYSTEMS GROUP INC

FORM 10-Q
(Quarterly Report)

Filed 08/04/17 for the Period Ending 06/30/17

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

OR

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

For the transition period from ____________to ____________.

Commission File Number: 000-28167

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
(Exact name of registrant as specified in its charter)

Delaware	**52-2126573**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

600 Telephone Avenue, Anchorage, Alaska 99503-6091
(Address of principal executive offices) (Zip Code)

(907) 297-3000
(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 ☒ 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 ☒ No ☐

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

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 check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

As of July 25, 2017, there were outstanding 52,433,202 shares of Common Stock, $.01 par value, of the registrant.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Condensed Consolidated Balance Sheets
(Unaudited, In Thousands Except Per Share Amounts)

	June 30, 2017	December 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	$ 12,982	$ 21,228
Restricted cash	11,924	1,917
Accounts receivable, net of allowance of $2,365 and $1,115	22,240	25,062
Materials and supplies	5,577	4,917
Prepayments and other current assets	7,340	5,995
Total current assets	60,063	59,119
Property, plant and equipment	1,357,723	1,349,899
Less: accumulated depreciation and amortization	(996,459)	(983,050)
Property, plant and equipment, net	361,264	366,849
Deferred income taxes	16,266	14,718
Other assets	1,773	1,674
Total assets	$ 439,366	$ 442,360
Liabilities and Stockholders' Equity		
Current liabilities:		
Current portion of long-term obligations	$ 15,958	$ 1,973
Accounts payable, accrued and other current liabilities	30,917	38,180
Advance billings and customer deposits	4,351	4,167
Total current liabilities	51,226	44,320
Long-term obligations, net of current portion	171,708	177,626
Other long-term liabilities, net of current portion	60,949	61,538
Total liabilities	283,883	283,484
Commitments and contingencies		
Alaska Communications stockholders' equity:		
Common stock, $.01 par value; 145,000 authorized; 52,435 issued and outstanding at June 30, 2017; 51,477 issued and outstanding at December 31, 2016	524	515
Additional paid in capital	157,929	159,474
(Accumulated deficit) retained earnings	(1,377)	752
Accumulated other comprehensive loss	(2,574)	(2,910)
Total Alaska Communications stockholders' equity	154,502	157,831
Noncontrolling interest	981	1,045
Total stockholders' equity	155,483	158,876
Total liabilities and stockholders' equity	$ 439,366	$ 442,360

See Notes to Condensed Consolidated Financial Statements

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Condensed Consolidated Statements of Comprehensive (Loss) Income
(Unaudited, In Thousands Except Per Share Amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Operating revenues	$58,536	$56,262	$115,267	$112,590
Operating expenses:				
Cost of services and sales (excluding depreciation and amortization)	26,454	25,543	51,596	51,671
Selling, general and administrative	17,438	17,586	35,531	34,926
Depreciation and amortization	9,028	8,640	17,931	17,160
Loss on disposal of assets, net	14	128	33	152
Total operating expenses	52,934	51,897	105,091	103,909
Operating income	5,602	4,365	10,176	8,681
Other income and (expense):				
Interest expense	(3,913)	(3,852)	(7,758)	(7,721)
Loss on extinguishment of debt	(5,158)	—	(7,434)	(336)
Interest income	7	6	14	11
Total other income and (expense)	(9,064)	(3,846)	(15,178)	(8,046)
(Loss) income before income tax benefit (expense)	(3,462)	519	(5,002)	635
Income tax benefit (expense)	632	(236)	1,464	(299)
Net (loss) income	(2,830)	283	(3,538)	336
Less net loss attributable to noncontrolling interest	(32)	(34)	(64)	(67)
Net (loss) income attributable to Alaska Communications	(2,798)	317	(3,474)	403
Other comprehensive income (loss):				
Minimum pension liability adjustment	29	14	58	28
Income tax effect	(12)	(6)	(24)	(15)
Amortization of defined benefit plan loss	154	217	308	434
Income tax effect	(63)	(89)	(126)	(178)
Interest rate swap marked to fair value	131	(49)	156	(174)
Income tax effect	(54)	20	(65)	71
Reclassification to interest expense	24	26	49	53
Income tax effect	(10)	(11)	(20)	(22)
Total other comprehensive income	199	122	336	197
Total comprehensive (loss) income attributable to Alaska Communications	(2,599)	439	(3,138)	600
Net loss attributable to noncontrolling interest	(32)	(34)	(64)	(67)
Total other comprehensive income attributable to noncontrolling interest	—	—	—	—
Total comprehensive loss attributable to noncontrolling interest	(32)	(34)	(64)	(67)
Total comprehensive (loss) income	$ (2,631)	$ 405	$ (3,202)	$ 533
Net (loss) income per share attributable to Alaska Communications:				
Basic and Diluted	$ (0.05)	$ 0.01	$ (0.07)	$ 0.01
Weighted average shares outstanding:				
Basic	52,341	51,231	52,177	50,986
Diluted	52,341	52,138	52,177	52,006

See Notes to Condensed Consolidated Financial Statements

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Condensed Consolidated Statement of Stockholders' Equity
Six Months Ended June 30, 2017
(Unaudited, In Thousands Except Per Share Amounts)

	Alaska Communications Stockholders' Equity						
	Shares	Common Stock	Additional Paid in Capital	(Accumulated Deficit) Retained Earnings	Accumulated Other Comprehensive Loss	Noncontrolling Interest	Stockholders' Equity
Balance at December 31, 2016	51,477	$ 515	$ 159,474	$ 752	$ (2,910)	$ 1,045	$ 158,876
Total comprehensive (loss) income	—	—	—	(3,474)	336	(64)	(3,202)
Cumulative effect of new accounting principles adopted	—	—	(1,278)	1,345	—	—	67
Stock compensation	—	—	581	—	—	—	581
Extinguishment of convertible note options, net of tax	—	—	(359)	—	—	—	(359)
Surrender of shares to cover minimum withholding taxes on stock-based compensation	—	—	(599)	—	—	—	(599)
Issuance of common stock, pursuant to stock plans, $.01 par	958	9	110	—	—	—	119
Balance at June 30, 2017	52,435	$ 524	$ 157,929	$ (1,377)	$ (2,574)	$ 981	$ 155,483

See Notes to Condensed Consolidated Financial Statements

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Condensed Consolidated Statements of Cash Flows
(Unaudited, In Thousands)

	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
Cash Flows from Operating Activities:		
Net (loss) income	$ (3,538)	$ 336
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	17,931	17,160
Loss on disposal of assets, net	33	152
Amortization of debt issuance costs and debt discount	1,537	2,021
Loss on extinguishment of debt	7,434	336
Amortization of deferred capacity revenue	(1,717)	(1,702)
Stock-based compensation	581	1,447
Deferred income tax (benefit) expense	(1,466)	495
Tax deficiencies from share-based payments	—	(51)
Charge for uncollectible accounts	1,633	77
Other non-cash expense, net	288	414
Income taxes payable (receivable)	574	(722)
Changes in operating assets and liabilities	(6,225)	(1,077)
Net cash provided by operating activities	17,065	18,886
Cash Flows from Investing Activities:		
Capital expenditures	(10,522)	(13,662)
Capitalized interest	(463)	(548)
Change in unsettled capital expenditures	(2,043)	(9,156)
Proceeds on sale of assets	4	2,663
Net cash used by investing activities	(13,024)	(20,703)
Cash Flows from Financing Activities:		
Repayments of long-term debt	(174,013)	(11,486)
Proceeds from the issuance of long-term debt	183,000	—
Debt issuance costs and discounts	(5,508)	(44)
Cash paid for debt extinguishment	(5,279)	(150)
Cash proceeds from noncontrolling interest	—	75
Payment of withholding taxes on stock-based compensation	(599)	(472)
Proceeds from the issuance of common stock	119	128
Net cash used by financing activities	(2,280)	(11,949)
Change in cash, cash equivalents and restricted cash	1,761	(13,766)
Cash, cash equivalents and restricted cash, beginning of period	23,145	37,825
Cash, cash equivalents and restricted cash, end of period	$ 24,906	$ 24,059
Supplemental Cash Flow Data:		
Interest paid	$ 7,595	$ 6,359
Income taxes (refunded) paid, net	$ (572)	$ 577

See Notes to Condensed Consolidated Financial Statements

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited, In Thousands Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Alaska Communications Systems Group, Inc. (“we”, “our”, “us”, the “Company” and “Alaska Communications”), a Delaware corporation, through its operating subsidiaries, provides broadband telecommunication and managed information technology (“IT”) services to customers in the State of Alaska and beyond using its telecommunications network.

The accompanying unaudited condensed consolidated financial statements represent the consolidated financial position, comprehensive income and cash flows of Alaska Communications Systems Group, Inc. and the following wholly-owned subsidiaries:

- Alaska Communications Systems Holdings, Inc. (“ACS Holdings”)
- ACS of Alaska, LLC (“ACSAK”)
- ACS of the Northland, LLC (“ACSN”)
- ACS of Fairbanks, LLC (“ACSF”)
- ACS of Anchorage, LLC (“ACSA”)
- ACS Wireless, Inc. (“ACSW”)
- ACS Long Distance, LLC (“ACSLD”)
- Alaska Communications Internet, LLC (“ACSI”)
- ACS Messaging, Inc. (“ACSM”)
- ACS Cable Systems, LLC (“ACSC”)
- Crest Communications Corporation
- WCI Cable, Inc.
- WCIC Hillsboro, LLC
- Alaska Northstar Communications, LLC
- WCI LightPoint, LLC
- WorldNet Communications, Inc.
- Alaska Fiber Star, LLC
- TekMate, LLC (“TekMate”)

In addition to the wholly-owned subsidiaries, the Company has a fifty percent interest in ACS-Quintillion JV, LLC, a joint venture formed by its wholly-owned subsidiary ACS Cable Systems, LLC and Quintillion Holdings, LLC (“QHL”) in connection with the North Slope fiber optic network. See Note 2 “ *Joint Venture* ” for additional information.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements and notes included in this Quarterly Report on Form 10-Q have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016. Certain information and note disclosures normally included in financial statements prepared in accordance with Generally Accepted Accounting Principles in the United States of America (“GAAP”) have been condensed or omitted pursuant to the rules and regulations of the SEC. The Company believes the disclosures made are adequate to make the information presented not misleading.

The Company has consolidated the financial results of the joint venture with QHL based on its determination that, for accounting purposes, it holds a controlling financial interest in the joint venture and is the primary beneficiary of this variable interest entity. The Company has accounted for and reported QHL’s 50 percent ownership interest in the joint venture as a noncontrolling interest. See Note 2 “ *Joint Venture* ” for additional information.

In the opinion of management, the unaudited condensed consolidated financial statements contain all normal, recurring adjustments necessary to present fairly the consolidated financial position, comprehensive (loss) income and cash flows for all periods presented. Comprehensive loss for the three and six months ended June 30, 2017, is not necessarily indicative of comprehensive (loss) income which might be expected for the entire year or any other interim periods. The balance sheet at December 31, 2016 has been derived from the audited financial statements as of that date but does not include all information and notes required by GAAP for complete financial statements. Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation.

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the Company’s consolidated financial statements and the accompanying notes, including estimates of probable losses and expenses. Actual results could differ materially from those estimates.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited, In Thousands Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Recently Adopted Accounting Pronouncements

In the first quarter of 2017, the Company adopted ASU No. 2016-09, " *Compensation – Stock Compensation (Topic 718), Improvements to Employee Share-Based Payment Accounting* " ("ASU 2016-09"). The amendments in ASU 2016-09 simplify several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The relevant provisions of ASU 2016-09 and the effect of adoption on the Company's financial statements and related disclosures are summarized as follows: (i) The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. Excess tax benefits should be recognized regardless of whether the benefit reduces taxes payable in the current period. Excess tax benefits and tax deficiencies should be recognized as income tax expense or benefit in the income statement. The Company adopted these provisions on a modified retrospective basis. Excess tax benefits and tax deficiencies are included in the income tax provision beginning in the first quarter of 2017. A cumulative-effect adjustment was recorded in the first quarter of 2017 to reclassify $1,441 from additional paid in capital to retained earnings for excess tax benefits and deficiencies recorded to additional paid in capital prior to 2017. (ii) Excess tax benefits and tax deficiencies should be classified as an operating activity in the statement of cash flows. The Company adopted this provision on a retrospective basis. Tax deficiencies from share-based payments of $51 classified as a financing activity on the statement of cash flows in the six-month period of 2016 were reclassified to operating activities. See the condensed consolidated statement of cash flows. (iii) An entity may make an accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. Prior to 2017, the Company's stock-based compensation expense reflected an estimate of the number of awards that were expected to vest, including an estimate of forfeitures. Effective in the first quarter 2017, the Company elected to account for forfeitures when they occur. This provision was adopted on a modified retrospective basis, and a cumulative-effect adjustment was recorded in the first quarter of 2017 to reclassify $163 from additional paid in capital to retained earnings for the effect of this accounting change on periods prior to 2017. Retained earnings was charged $96 net of the income tax effect of $67. (iv) The threshold to qualify for equity classification permits withholding up to the maximum statutory tax rates. The Company has historically withheld taxes at the minimum statutory rate. Adoption of this provision is not expected to have a material effect on the Company's financial statements. (vii) Cash paid by an employer when directly withholding shares for tax withholding purposes should be classified as a financing activity. This classification is consistent with the Company's historical practice. See the consolidated statement of stockholders' equity, Note 9 " *Stock Incentive Plans* " and Note 10 " *Income Taxes* " for additional information.

In August 2016, the Financial Accounting Standards Board ("FASB") issued ASU No. 2016-15, " *Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments* " ("ASU 2016-15"). The amendments in this update address eight specific cash flow classification issues for which current GAAP either is unclear or does not include specific guidance, and for which there exists diversity in practice: Debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, and interim periods within those years, and early adoption is permitted. The Company adopted ASU 2016-15 effective in the first quarter of 2017 on a modified retrospective basis as required by the standard. The Company's cash flow classifications for the eight issues addressed in ASU 2016-15, where applicable, were generally consistent with the new guidance. Accordingly, adoption of ASU 2016-15 did not have a material effect on the Company's financial statements.

In November 2016, the FASB issued ASU No. 2016-18, " *Statement of Cash Flows (Topic 230), Restricted Cash* " ("ASU 2016-18"). ASU 2016-18 requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited, In Thousands Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

cash equivalents. ASU 2016-18 is effective for fiscal years beginning after December 15, 2017, and was adopted by the Company effective in the first quarter of 2017 as permitted. The Company adopted ASU 2016-18 on a retrospective basis as required by the standard. See Note 13 " *Supplemental Cash Flow Information* " for additional information.

Accounting Pronouncements Issued Not Yet Adopted

In May 2014, the FASB issued ASU No. 2014-09, " *Revenue from Contracts with Customers (Topic 606)* " ("ASU 2014-09"). The amendments in ASU 2014-09 and subsequent updates require that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Adoption of the new standard is to be applied on a full retrospective basis or modified retrospective basis. The Company's assessment of ASU 2014-09 and subsequent updates is nearing completion and is currently expected to be completed during the third quarter of 2017. This assessment includes determining the effect of the new standard on the Company's financial statements, accounting systems, business processes, and internal controls. Based on its assessment to date, the Company does not currently expect adoption to have a material effect on its consolidated revenues. It is currently expected that adoption of the new standard will result in the deferral of certain contract fulfillment and other costs, including certain sales commissions, connection costs and modems, which are currently expensed as incurred. Such deferred costs will be amortized over the period that the associated revenue is recognized. The Company is in the early stages of implementation, which will require changes to the Company's accounting systems, business processes and internal controls. The Company will adopt ASU 2014-09 effective January 1, 2018 and has not yet selected an adoption method.

In February 2016, the FASB issued ASU No. 2016-02, " *Leases (Topic 842)* " ("ASU 2016-02"). The primary change in GAAP addressed by ASU 2016-02 is the requirement for a lessee to recognize on the balance sheet a liability to make lease payments ("lease liability") and a right-of-use asset representing its right to use the underlying asset for the lease term. The accounting applied by a lessor is largely unchanged from that applied under previous GAAP. ASU 2016-02 also requires qualitative and quantitative disclosures to enable users of the financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those years. Lessees must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The Company is evaluating the effect that ASU 2016-02 will have on its consolidated financial statements and related disclosures.

In March 2017, the FASB issued ASU No. 2017-07, " *Compensation – Retirement Benefits (Topic 715)* " ("ASU 2017-07"). The amendments in ASU 2017-07 require that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees. The other components of net benefit costs are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. If a separate line item or items are used to present the other components of net benefit costs, that line item or items must be appropriately described. If a separate line item or items are not used, the line item or items used in the income statement to present the other components of net benefit cost must be disclosed. ASU 2017-07 also requires that only the service cost component is eligible for capitalization when applicable. ASU 2017-07 is effective for fiscal years beginning after December 15, 2017. The Company does not currently expect that adoption of ASU 2017-07 will have a material effect on its consolidated financial statements and related disclosures.

In May 2017, the FASB issued ASU No. 2017-09, " *Compensation – Stock Compensation (Topic 718)* " ("ASU 2017-09"). The amendments in ASU 2017-09 are intended to provide clarity, and reduce diversity in practice and the cost and complexity of applying the guidance in Topic 718. The primary provision of ASU 2017-09 is to provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting. An entity should account for the effects of a change as a modification unless all the following conditions are met: (i) The fair value of the modified award is the same as the fair value of the original award immediately before the original award is modified. If the modification does not affect any of the inputs to the valuation technique that the entity uses to value the award, the entity is not required to estimate the value immediately before and after the modification. (ii) The vesting conditions of the modified award are the same as the vesting conditions of the original award immediately before the original award is modified. (iii) The

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited, In Thousands Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

classification of the modified award as an equity instrument or a liability instrument is the same as the classification of the original award immediately before the original award is modified. ASU 2017-09 is effective for fiscal years beginning after December 15, 2017. Early adoption is permitted, including adoption in any interim period. The amendments in this update should be applied prospectively to awards modified on or after the adoption date. The effect of the adoption of ASU 2017-09 on the Company's financial statements and related disclosures will be dependent on the frequency and types of changes made to its share-based payment awards.

2. JOINT VENTURE

In the second quarter of 2015, the Company entered into a series of transactions including the acquisition of a fiber optic network on the North Slope of Alaska and the establishment of a joint venture with QHL. The network enables commercially-available, high-speed connectivity where only high-cost microwave and satellite communications was previously available. Through the Alaska Communications and QHL joint venture, this network has been made available to other telecom carriers in the market.

Acquisition of Fiber Optic Network

The Company, through its wholly-owned subsidiary ACS Cable Systems, LLC, acquired a fiber optic cable system (including conduit, licenses, permits and right-of-ways) running from the Kuparuk Operating Center to the Trans-Alaska Pipeline System Pump Station #1 (the "Fiber Optic System"). The purchase price was $11,000, $5,500 of which was paid by the Company at closing and the balance of which was paid on April 7, 2016. The Company sold to the previous owner a 30 year IRU on certain fibers from the Fiber Optic System. The sales price was $400, all of which was paid at closing. The Company also entered into agreements for the exchange of IRUs, pipeline access, conduit and future capacity, and the prepayment of certain fees and services.

Transactions with QHL

The Company sold certain fiber strands from the Fiber Optic System to QHL for $5,300, $2,650 of which was paid to the Company by QHL at closing and the balance of which was paid on March 31, 2016. The Company and QHL also exchanged 30 year IRU agreements.

Formation of Joint Venture

On April 2, 2015, the Company, through its wholly-owned subsidiary ACS Cable Systems, LLC, entered into a joint venture agreement with QHL to form ACS-Quintillion JV, LLC (the "Joint Venture") for the purpose of expanding the fiber optic network, and making the network available to other telecom carriers. The Joint Venture may also participate in and facilitate other capital and service initiatives in the telecom industry. The Company and QHL each contributed to the Joint Venture IRUs with a combined value of $1,844 ($922 by each party). Each party also contributed cash of $250. The Company contributed an additional IRU with a value of $461. In the first quarter of 2016, the Company and QHL executed an amendment to the operating agreement which provides the Company access to 50 percent of the Joint Venture's initial in-field lit capacity in compensation for the Company's contribution of the additional IRU at the Joint Venture's formation. This amendment is effective as of the establishment date of the Joint Venture on April 2, 2015. In the second quarter of 2016, the Company and QHL each made an additional $75 capital contribution to the Joint Venture. The Company and QHL each hold a 50 percent voting interest in the Joint Venture.

The Company determined that the Joint Venture is a Variable Interest Entity as defined in ASC 810, " *Consolidation* ." The Company consolidates the financial results of the Joint Venture based on its determination that, the 50 percent voting interest of each party notwithstanding, for accounting purposes it holds a controlling financial interest in, and is the primary beneficiary of, the Joint Venture. This determination was based on (i) the Company's expected future utilization of certain assets of the Joint Venture in the operation of the Company's business; (ii) the Company' engineering, design, installation, service and maintenance expertise in the telecom industry and its existing relationships and presence in the Alaska telecom market are expected to be significant factors in the successful operation of the Joint Venture; and (iii) the Company's role as Joint Venture manager and its right to a management fee equal to a percentage of the Joint Venture's collected gross revenue. There was no gain or loss recognized by the Company on the initial consolidation of the Joint Venture. The Company has accounted for and reported QHL's 50 percent ownership interest in the Joint Venture as a noncontrolling interest.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited, In Thousands Except Per Share Amounts)

2. JOINT VENTURE (Continued)

The table below provides certain financial information about the Joint Venture included on the Company's consolidated balance sheet at June 30, 2017 and December 31, 2016. Cash may be utilized only to settle obligations of the Joint Venture. Because the Joint Venture is an LLC, its creditors do not have recourse to the general credit of the Company.

	2017	2016
Cash	$ 67	$ 67
Fiber and IRUs, net of accumulated depreciation of $161 and $112	$1,980	$2,029

The operating results and cash flows of the Joint Venture in the three and six-month periods of 2017 and 2016 were not material to the Company's consolidated financial results.

3. FAIR VALUE MEASUREMENTS AND DERIVATIVE FINANCIAL INSTRUMENTS

Fair Value Measurements

The Company has developed valuation techniques based upon observable and unobservable inputs to calculate the fair value of non-current monetary assets and liabilities. Observable inputs reflect market data obtained from independent sources and unobservable inputs reflect internal market assumptions. These two types of inputs create the following fair value hierarchy:

- Level 1- Quoted prices for identical instruments in active markets.
- Level 2- Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-derived valuations whose inputs are observable or whose significant value drivers are observable.
- Level 3- Significant inputs to the valuation model are unobservable.

Financial assets and liabilities are classified within the fair value hierarchy in their entirety based on the lowest level of input that is significant to the fair value measurements. The Company's assessment of the significance of a particular input to the fair value measurements requires judgment and may affect the valuation of the assets and liabilities being measured, as well as their level within the fair value hierarchy.

The fair values of cash equivalents, restricted cash, other short-term monetary assets and liabilities and capital leases approximate carrying values due to their nature. The estimated fair value of the Company's 6.25% Convertible Notes due 2018 ("6.25% Notes") Notes of $9,913 at June 30, 2017, was estimated based on quoted market prices for identical instruments on dates different from the market trade date value (Level 2). The carrying value of the 6.25% Notes at June 30, 2017 was $9,913. The estimated fair value and carrying value of the Company's 6.25% Notes was $91,729 at December 31, 2016. The carrying values of the Company's senior credit facilities and other long-term obligations of $180,956 and $90,075 at June 30, 2017 and December 31, 2016, respectively, approximate fair value primarily as a result of the stated interest rates of the 2017 Senior Credit Facility and 2015 Senior Credit Facilities approximating current market rates (Level 2).

The following table presents the Company's financial liabilities measured at fair value on a recurring basis as of June 30, 2017 and December 31, 2016, at each hierarchical level:

	June 30, 2017				December 31, 2016			
	Total	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3
Other assets:								
Interest rate swaps	$126	$ —	$ 126	$ —	$—	$ —	$ —	$ —
Other long-term liabilities:								
Interest rate swaps	$—	$ —	$ —	$ —	$100	$ —	$ 100	$ —

Derivative Financial Instruments

The Company currently uses interest rate swaps to manage variable interest rate risk. At low LIBOR rates, payments under the swaps increase the Company's cash interest expense.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited, In Thousands Except Per Share Amounts)

3. FAIR VALUE MEASUREMENTS AND DERIVATIVE FINANCIAL INSTRUMENTS (Continued)

The outstanding amount of the swaps as of a period end are reported on the balance sheet at fair value, represented by the estimated amount the Company would receive or pay to terminate the swaps, and are valued using models based on readily observable market parameters for all substantial terms of the contracts.

Under the terms of the 2017 Senior Credit Facility, the Company was required enter into or obtain an interest rate hedge sufficient to effectively fix or limit the interest rate on borrowings under the Agreement of a minimum of $90,000 with a weighted average life of at least two years within ninety days of March 28, 2017. Subsequent to repayment of the principal amounts outstanding under its 2015 Senior Credit Facilities on March 28, 2017, the Company redesignated its existing pay-fixed, receive-floating interest rate swap with a remaining notional amount of $42,058 at March 31, 2017 and an interest rate of 6.333%, inclusive of a 5.0% LIBOR spread, as a hedge of variable interest rate payments under its 2017 Senior Credit Facility. The notional amount of this swap, which terminates on December 31, 2017, was $41,365 at June 30, 2017. On June 14, 2017, the Company entered into an additional pay-fixed, receive-floating interest rate swap in the initial notional amount of $48,635, increasing to $90,000 on December 29, 2017, with an interest rate of 6.49425%, inclusive of a 5.0% LIBOR spread, and a maturity date of June 28, 2019. Changes in fair value of these interest rate swaps are recorded to accumulated other comprehensive loss and are reclassified to interest expense when the hedged transaction is recognized in earnings. See Note 6 " *Long-Term Obligations* " and Note 8 " *Accumulated Other Comprehensive Loss.* "

The Company's two interest rate swaps at June 30, 2017 are with the same counterparty, are hedges of the same variable rate borrowing instrument and are subject to a master netting arrangement. The fair value of the two derivatives has been reported on a net basis on the balance sheet at June 30, 2017. The following table provides a gross presentation, the effects of offsetting, and the net presentation of these derivative instruments as of June 30,2017. The net amount of the derivative asset can be reconciled to the fair value disclosures.

	Gross Amount Recognized	Gross Amount Offset on the Balance Sheet	Net Amount Presented on the Balance Sheet
Other assets	$ 137	$ (11)	$ 126
Other long-term liabilities	$ 11	$ (11)	$ —

The following table presents the notional amount, fair value and balance sheet classification of the Company's derivative financial instruments designated as cash flow hedges as of June 30, 2017 and December, 31, 2016:

	Balance Sheet Location	Notional Amount	Fair Value
At June 30, 2017:			
Interest rate swaps	Other assets	$90,000	$ 126
At December 31, 2016:			
Interest rate swaps	Other long-term liabilities	$42,750	$ 100

The following table presents gains and losses before income taxes on the Company's interest rate swaps designated as cash flow hedges for the three and six-month periods ending June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Gain (loss) recognized in accumulated other comprehensive loss	$ 131	$ (49)	$ 156	$ (174)
Loss reclassified from accumulated other comprehensive loss	(24)	(26)	(49)	(53)
Gain recognized in interest expense (ineffective portion and amount excluded from effectiveness testing)	—	—	—	—

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4. ACCOUNTS RECEIVABLE

Accounts receivable, net, consists of the following at June 30, 2017 and December 31, 2016:

	2017	2016
Retail customers	$15,210	$17,511
Wholesale carriers	5,086	4,293
Other	4,309	4,373
	24,605	26,177
Less: allowance for doubtful accounts	(2,365)	(1,115)
Accounts receivable, net	$22,240	$25,062

The following table summarizes the change in the allowance for doubtful accounts for the six-month period ended June 30, 2017:

	2017
Balance at January 1	$1,115
Provision for uncollectible accounts	1,633
Charged to other accounts	—
Deductions	(383)
Balance at June 30	$2,365

On April 10, 2017, the Universal Service Administrative Company ("USAC"), which administers the Federal Communications Commission's ("FCC") rural health care universal service support mechanism, confirmed that demand for rural health care support had exceeded the program's $400 million annual cap in Funding Year 2016, which began July 1, 2016 and ended on June 30, 2017. As a result, USAC announced that applicants that filed successful funding requests between September 1 and November 30, 2016 would receive 92.5 percent of the funding for which they were otherwise eligible. On June 30, 2017, the FCC issued an order to Alaskan health care providers impacted by the Rural Health Care Program pro-ration, allowing customers unable to fund the shortfall to remain in regulatory compliance with the program. The Company subsequently notified this subset of customers that, subject to certain terms and conditions, it would suspend collection of the funding shortfall for Funding Year 2016. In the second quarter of 2017, the Company recorded a charge of $1,102 to fully reserve the effect of the funding shortfall for Funding Year 2016 on its rural health care customers. At June 30, 2017, the Company's accounts receivable balance included $4,233, net of the allowance for doubtful accounts including the above referenced charge, associated with these customers. Rural health care accounts are a component of the Retail Customers category in the above table. The Company will continue to evaluate the impact of potential shortfalls in Funding Year 2016 on its accounts receivable.

5. CURRENT LIABILITIES

Accounts payable, accrued and other current liabilities consist of the following at June 30, 2017 and December 31, 2016:

	2017	2016
Accrued payroll, benefits, and related liabilities	$10,836	$14,395
Accounts payable - trade	9,940	13,782
Deferred capacity and other revenue	5,432	4,502
Accrued interest on long-term obligations	160	1,026
Other	4,549	4,475
	$30,917	$38,180

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
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5. CURRENT LIABILITIES (Continued)

Advance billings and customer deposits consist of the following at June 30, 2017 and December 31, 2016:

	2017	2016
Advance billings	$4,319	$4,136
Customer deposits	32	31
	$4,351	$4,167

6. LONG-TERM OBLIGATIONS

Long-term obligations consist of the following at June 30, 2017 and December 31, 2016:

	2017	2016
2017 senior secured credit facility due 2023	$180,000	$ —
Debt discount	(3,000)	—
Debt issuance costs	(3,176)	—
2015 senior secured credit facilities due 2018	—	86,750
Debt issuance costs	—	(1,738)
6.25% convertible notes due 2018	10,044	94,000
Debt discount	(131)	(2,271)
Debt issuance costs	(27)	(467)
Capital leases and other long-term obligations	3,956	3,325
	187,666	179,599
Less current portion	(15,958)	(1,973)
Long-term obligations, net of current portion	$171,708	$177,626

As of June 30, 2017, the aggregate maturities of long-term obligations were as follows:

2017 (July 1 - December 31)	$ 2,602
2018 (January 1 - December 31)	16,880
2019 (January 1 - December 31)	6,639
2020 (January 1 - December 31)	8,902
2021 (January 1 - December 31)	16,267
2022 (January 1 - December 31)	86,483
Thereafter	56,227
	$194,000

As of June 30, 2017, the Company had no amounts outstanding under the $15,000 revolving facility component of its 2017 Senior Credit Facility.

2017 Senior Credit Facility

On March 13, 2017 (the "Closing Date"), the Company entered into a new senior credit facility consisting of a Term A-1 Facility of $120,000, a Term A-2 Facility of $60,000 and a revolving facility of $15,000 (the "2017 Senior Credit Facility" or "Agreement"). Upon the satisfaction of certain conditions, on March 28, 2017 (the "Funding Date"), the 2017 Senior Credit Facility was funded. Gross cash proceeds totaling $176,828, net of discounts of $3,172, and cash on hand of $8,955 were utilized as follows: (i) repayment of the Company's 2015 Senior Credit Facility due 2018 totaling $88,135, including principal, accrued interest and fees; (ii) placement of $94,000 in restricted cash to fund the purchase or repayment at maturity of its 6.25% Convertible Notes due 2018 ("6.25% Notes"); (iii) fund fees associated with tender of the 6.25% Notes of $197; and (iv) fund fees and other expenses associated with the transaction totaling $3,451. Discounts, fees and expenses associated with the 2017 Senior Credit Facility, including amounts paid in 2016, totaling $6,528 were deferred and will be charged to interest expense over the terms of the Agreement.

6. LONG-TERM OBLIGATIONS (Continued)

The Term A-1 Facility in the principal amount of $120,000 bears interest at LIBOR plus 5.0% per annum, with a LIBOR minimum of 1.0%. Quarterly principal payments are $1,500 beginning in the fourth quarter of 2017 through the first quarter of 2020; $2,250 in the second quarter of 2020 through the first quarter of 2021; and $4,000 in the second quarter of 2021 through the fourth quarter of 2021. The remaining outstanding principal balance is due on March 13, 2022.

The Term A-2 Facility in the principal amount of $60,000 bears interest at LIBOR plus 7.0% per annum, with a LIBOR minimum of 1.0%. Quarterly principal payments are $150 beginning in the fourth quarter of 2017 through the first quarter of 2021; and $600 in the second quarter of 2021 through the fourth quarter of 2022. The remaining outstanding principal balance is due on March 13, 2023.

The Company may, at its option, designate a portion of the borrowings under the Term A-1 Facility and Term A-2 Facility to bear interest at an Alternative Base Rate, which is defined as the highest of (i) the Prime Rate; (ii) the Federal Funds Effective Rate plus 0.50% per annum; and (iii) the Adjusted LIBOR Rate for an Interest Period of one month plus 1.0% per annum. If the LIBOR Rate is no longer available for such interest period, the Adjusted LIBOR Rate shall be calculated as the Administrative Agent shall select in its sole discretion. The Alternative Base Rate shall not be less than zero.

The revolving facility provides for borrowings in an aggregate amount outstanding at any one time not to exceed $15,000, including a letter of credit subfacility and swingline subfacility with commitment limitations based on amounts drawn under the revolving facility (collectively the “Revolving Facility”). The Revolving Facility bears interest at LIBOR plus 5.0% per annum, with a LIBOR minimum of 1.0%.

The obligations under the 2017 Senior Credit Facility are secured by substantially all of the personal property and certain material real property owned by the Company and its wholly-owned subsidiaries, with certain exceptions. The 2017 Senior Credit Facility contains customary representations, warranties and covenants, including covenants limiting the incurrence of debt, declaring dividends, repurchase of the Company’s common stock, making investments, dispositions, and entering into mergers and acquisitions. Financial covenants (i) impose a maximum net total leverage to consolidated EBITDA ratio; and (ii) require a minimum consolidated EBITDA to fixed charge coverage ratio. The 2017 Senior Credit Facility provides for events of default customary for credit facilities of this type, including non-payment under the agreement, breach of warranty, breach of covenants, defaults on other debt, incurrence of liens on collateral, change of control and insolvency, all as defined in the Agreement. Consequences of an event of default are defined in the Agreement.

As required under the terms of the 2017 Senior Credit Facility, the Company has entered into interest rate hedges sufficient to effectively fix or limit the interest rate on borrowings under the Agreement of a minimum of $90,000 with a weighted average life of at least two years. See Note 3 “ *Fair Value Measurements and Derivative Financial Instruments* ” for additional information.

2015 Senior Credit Facilities

On March 28, 2017, the Company utilized proceeds from the 2017 Senior Credit Facility and cash on hand to repay, in full, the outstanding principal balance of its 2015 Senior Credit Facilities in the amount of $86,750 and accrued interest and fees totaling $1,385. The Company recorded a loss of $2,274 on the extinguishment of debt associated with this transaction, including the write-off of debt issuance costs and third-party fees. Principal payments under the 2015 Senior Credit Facility were due in 2017 and 2018.

6.25% Convertible Notes Due 2018

On March 17, 2017, the Company issued a tender offer to purchase any and all of its outstanding 6.25% Notes for cash in an amount equal to one thousand twenty-five dollars per one thousand dollars principal amount (the “Tender Offer”). The Tender Offer was subsequently amended to one thousand thirty-seven dollars and fifty cents per one thousand dollars principal amount. Under the terms of the Agreement, proceeds from the Company’s 2017 Senior Credit Facility in the amount of $94,000 must be utilized to fund the Tender Offer, the repurchase, or repayment at maturity of, the 6.25% Notes. The Tender Offer expired on April 14, 2017 and was settled on April 17, 2017. As of the expiration date, $83,956 aggregate principal amount of the 6.25% Notes were validly tendered and not validly withdrawn pursuant to the Tender Offer, and were accepted for purchase by the Company at a purchase price equal to one thousand thirty-seven dollars and fifty cents per one thousand dollars principal amount. The Company settled the Tender Offer on April 17, 2017 for a total of $90,011, including principal of $83,956, accrued interest of $2,420, the premium of $3,148 and fees of $487. Settlement was funded with restricted cash of $83,956 and other cash on hand of $6,055. The Company recorded a loss on the extinguishment of this debt of $5,160 in the second quarter of 2017. Following settlement, 6.25% Notes in the aggregate principal amount of $10,044 remained outstanding. The purchase or settlement at maturity of the remaining 6.25% Notes will be funded, in part, with restricted cash of $10,044 designated for this purpose.

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7. OTHER LONG-TERM LIABILITIES

Other long-term liabilities consist of the following at June 30, 2017 and December 31, 2016:

	2017	2016
Deferred GCI capacity revenue, net of current portion	$34,228	$35,255
Other deferred IRU capacity revenue, net of current portion	17,274	15,697
Other deferred revenue, net of current portion	1,346	2,202
Other	8,101	8,384
	$60,949	$61,538

8. ACCUMULATED OTHER COMPREHENSIVE LOSS

The following table summarizes the activity in accumulated other comprehensive loss for the six-month period ended June 30, 2017:

	Defined Benefit Pension Plan	Interest Rate Swaps	Total
Balance at December 31, 2016	$(2,875)	$ (35)	$(2,910)
Other comprehensive income before reclassifications	34	91	125
Reclassifications from accumulated comprehensive loss to net income	182	29	211
Net other comprehensive income	216	120	336
Balance at June 30, 2017	$(2,659)	$ 85	$(2,574)

The following table summarizes the reclassifications from accumulated other comprehensive loss to net (loss) income for the three and six-month periods ended June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Amortization of defined benefit plan pension items:				
Amortization of loss	$ 154	$ 217	$ 308	$ 434
Income tax effect	(63)	(89)	(126)	(178)
After tax	91	128	182	256
Amortization of loss on interest rate swap:				
Reclassification to interest expense	24	26	49	53
Income tax effect	(10)	(11)	(20)	(22)
After tax	14	15	29	31
Total reclassifications, net of income tax	$ 105	$ 143	$ 211	$ 287

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8. ACCUMULATED OTHER COMPREHENSIVE LOSS (Continued)

Amounts reclassified to net (loss) income from our defined benefit pension plan and interest rate swaps have been presented within “Selling, general and administrative expenses” and “Interest expense,” respectively, in the Condensed Consolidated Statements of Comprehensive (Loss) Income. The estimated amount of accumulated other comprehensive loss to be reclassified to interest expense within the next twelve months is $62. See Note 3 “ *Fair Value Measurements and Derivative Financial Instruments* .”

9. STOCK INCENTIVE PLANS

Under the Company’s stock incentive plan, stock options, restricted stock, stock-settled stock appreciation rights, performance share units and other awards may be granted to officers, employees, consultants, and non-employee directors.

Prior to 2017, the Company’s stock-based compensation expense reflected an estimate of forfeited share-based awards. Upon the adoption of ASU 2016-09 effective January 1, 2017, the Company elected to account for forfeitures when they occur. This standard was adopted on a modified retrospective basis and stock-based compensation expense for the three and six-month periods ended June 30, 2016 have not be restated for this change. Adoption did not have a material effect on the Company’s stock-based compensation expense. See Note 1 “ *Summary of Significant Accounting Policies* ” for additional information.

The following table summarizes the restricted stock unit, long-term incentive award and non-employee director stock compensation activity for the six-month period ended June 30, 2017:

	Number of Shares	Weighted Average Grant Date Fair Value
Nonvested at December 31, 2016	1,414	$ 1.79
Granted	70	2.01
Vested	(737)	1.83
Canceled or expired	—	—
Nonvested at June 30, 2017	747	$ 1.77

The following table summarizes the performance share unit activity for the six-month period ended June 30, 2017:

	Number of Shares	Weighted Average Grant Date Fair Value
Nonvested at December 31, 2016	1,334	$ 1.77
Granted	—	—
Vested	(532)	1.78
Canceled or expired	(19)	1.81
Nonvested at June 30, 2017	783	$ 1.76

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
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9. STOCK INCENTIVE PLANS (Continued)

The following table provides selected information about the Company's share-based compensation as of and for the three and six-month periods ended June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Total compensation cost for share-based payments	$ (29)	$ 642	$ 581	$1,447
Weighted average grant-date fair value of equity instruments granted (per share)	$ 2.20	$ 1.70	$ 1.81	$ 1.74
Total fair value of shares vested during the period	$ 140	$ 70	$2,286	$1,884
At June 30:				
Unamortized share-based payments			$ 807	$2,586
Weighted average period (in years) to be recognized as expense			1.3	1.6

10. INCOME TAXES

The Company adopted ASU 2016-09 effective January 1, 2017. As required by ASU 2016-09, the Company recorded a tax deficiency from share-based payments of $29 in the provision for income taxes in the six-month period ended June 30, 2017, which decreased net income by the same amount. A tax deficiency from share-based payments of $51 in the six-month period ended June 30, 2016 was charged to additional paid-in capital in that period. ASU 2016-09 was adopted on a modified retrospective basis and the income tax provision reported for the three and six-month periods ended June 30, 2016 were not adjusted for this change. See Note 1 " *Summary of Significant Accounting Policies* " for additional information.

The Company's income tax benefit of $632 and $1,464 and effective income tax rate of 18.3% and 29.3% in the three and six-month periods ended June 30, 2017 reflect the impact of permanent book to tax differences.

11. EARNINGS PER SHARE

Earnings per share are based on the weighted average number of shares of common stock and dilutive potential common share equivalents outstanding. Basic earnings per share assumes no dilution and is computed by dividing net income attributable to Alaska Communications by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution of securities that could share in the earnings of the Company. Potential common share equivalents include restricted stock granted to employees and deferred shares granted to directors. The Company includes dilutive stock options based on the "treasury stock method."

Effective in 2015, the Company discontinued use of the "if converted" method in calculating diluted earnings per share in connection with its contingently convertible debt. Accordingly, 2,502 and 5,714 shares related to the 6.25% Notes have been excluded from the calculation of diluted earnings per share for the three and six-month periods ended June 30, 2017, respectively, and 9,143 and 9,298 shares were excluded from the calculation of diluted earnings per share for the three and six-month periods ended June 30, 2016, respectively. Due to the Company's reported net loss for the three and six-month periods ended June 30, 2017, 1,957 potential common share equivalents outstanding, consisting of restricted stock and deferred shares granted to directors, were antidilutive and excluded from the calculation of diluted loss per share.

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11. EARNINGS PER SHARE (Continued)

The calculation of basic and diluted earnings per share for the three and six-month periods ended June 30, 2017 and 2016 are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net (loss) income attributable to Alaska Communications	$ (2,798)	$ 317	$ (3,474)	$ 403
Weighted average common shares outstanding:				
Basic shares	52,341	51,231	52,177	50,986
Effect of stock-based compensation	—	907	—	1,020
Diluted shares	52,341	52,138	52,177	52,006
Net (loss) income per share attributable to Alaska Communications:				
Basic	$ (0.05)	$ 0.01	$ (0.07)	$ 0.01
Diluted	$ (0.05)	$ 0.01	$ (0.07)	$ 0.01

12. RETIREMENT PLANS

Multi-employer Defined Benefit Plan

Pension benefits for substantially all of the Company’s Alaska-based employees are provided through the Alaska Electrical Pension Fund (“AEPF”). The Company pays a contractual hourly amount based on employee classification or base compensation to the AEPF. As a multi-employer defined benefit plan, the accumulated benefits and plan assets are not determined for, or allocated separately to, the individual employer. This plan was not in endangered or critical status during the plan year.

Defined Benefit Plan

The Company has a separate defined benefit plan that covers certain employees previously employed by Century Telephone Enterprise, Inc. (“CenturyTel Plan”). This plan was transferred to the Company in connection with the acquisition of CenturyTel, Inc.’s Alaska properties, whereby assets and liabilities of the CenturyTel Plan were transferred to the ACS Retirement Plan on September 1, 1999. As of June 30, 2017, this plan is not fully funded under the Employee Retirement Income Security Act of 1974, as amended.

The following table presents the net periodic pension expense for the ACS Retirement Plan for the three and six-month periods ended June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Interest cost	$ 156	$ 168	$ 312	$ 335
Expected return on plan assets	(185)	(181)	(370)	(362)
Amortization of loss	183	230	366	461
Net periodic pension expense	$ 154	$ 217	$ 308	$ 434

13. SUPPLEMENTAL CASH FLOW INFORMATION

The Company adopted ASU 2016-15, which addresses the classification of certain cash inflows and outflows, effective in the first quarter of 2017. ASU 2016-15 was adopted retrospectively and did not have a material effect on the Company’s statement of cash flows. See Note 1 “ *Summary of Significant Accounting Policies* .”

The Company adopted ASU 2016-18 effective in the first quarter of 2017. ASU 2016-18 requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. As required, the Company adopted ASU 2016-18 on a retrospective basis. The net change in restricted cash of $13 originally reported as a cash inflow from financing activities on the statement of cash flows for the six-month period ended June 30, 2016 was associated with stand-by letters of credit and was eliminated from the statement as a result of the adoption of ASU 2016-18. See Note 1 “ *Summary of Significant Accounting Policies* ” for additional information.

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13. SUPPLEMENTAL CASH FLOW INFORMATION (Continued)

Restricted cash of $11,924 at June 30, 2017 consisted of $10,044 to fund the purchase or settlement at maturity of the Company's 6.25% Notes, and certificates of deposit of $1,880 required under the terms of certain contracts to which the Company is a party. Restricted cash of $1,917 at December 31, 2016 consisted of certificates of deposit as described above.

The following table provides a reconciliation of cash and cash equivalents and restricted cash reported within the statement of financial position at June 30, 2017 and 2016 that sum to the total of these items reported in the statement of cash flows:

	June 30, 2017	June 30, 2016
Cash and cash equivalents	$12,982	$22,248
Restricted cash	11,924	1,811
Total cash, cash equivalents and restricted cash	$24,906	$24,059

The following table presents supplemental non-cash transaction information for the six-month periods ended June 30, 2017 and 2016:

	2017	2016
Supplemental Non-cash Transactions:		
Capital expenditures incurred but not paid at June 30	$1,506	$2,536
Property acquired under capital leases	$1,078	$ —
Additions to ARO asset	$ 186	$ 141

14. BUSINESS SEGMENTS

The Company operates its business under a single reportable segment. The Company's chief operating decision maker assesses the financial performance of the business as follows: (i) revenues are managed on the basis of specific customers and customer groups; (ii) costs are managed and assessed by function and generally support the organization across all customer groups or revenue streams; (iii) profitability is assessed at the consolidated level; and (iv) investment decisions and the assessment of existing assets are based on the support they provide to all revenue streams.

15. COMMITMENTS AND CONTINGENCIES

The Company enters into purchase commitments with vendors in the ordinary course of business. The Company also has long-term purchase contracts with vendors to support the on-going needs of its business. These purchase commitments and contracts have varying terms and in certain cases may require the Company to buy goods and services in the future at predetermined volumes and at fixed prices.

The Company is involved in various claims, legal actions and regulatory proceedings arising in the ordinary course of business. The Company establishes an accrual when a particular contingency is probable and estimable, and has recorded litigation accruals of $668 at June 30, 2017 against certain current claims and legal actions. The Company also faces contingencies that are reasonably possible to occur that cannot currently be estimated. The Company believes that the disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, comprehensive income or cash flows. It is the Company's policy to expense costs associated with loss contingencies, including any related legal fees, as they are incurred.

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

FORWARD-LOOKING STATEMENTS AND ANALYSTS' REPORTS

This Form 10-Q and our future filings on Forms 10-K, 10-Q and 8-K and the documents incorporated therein by reference include forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934 ("Exchange Act"), as amended. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements. All statements other than statements of historical fact are "forward-looking statements" for purposes of federal and state securities laws, including statements about anticipated future operating and financial performance, financial position and liquidity, growth opportunities and growth rates, pricing plans, acquisition and divestiture opportunities, business prospects, strategic alternatives, business strategies, regulatory and competitive outlook, investment and expenditure plans, financing needs and availability and other similar forecasts and statements of expectation and statements of assumptions underlying any of the foregoing. Words such as "anticipates", "believes", "could", "estimates", "expects", "intends", "may", "plans", "projects", "seeks", "should" and variations of these words and similar expressions are intended to identify these forward-looking statements. These forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from our historical experience and our present expectations or projections. Forward-looking statements by us are based on estimates, projections, beliefs and assumptions of management and are not guarantees of future performance. Such forward-looking statements may be contained in this Form 10-Q under Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations and elsewhere. Actual future performance, outcomes, and results may differ materially from those expressed in forward-looking statements made by us as a result of a number of important factors. Examples of these factors include (without limitation):

- governmental and public policy changes, including on-going changes in our revenues, or obligations we will assume to receive these revenues, resulting from regulatory actions affecting inter-carrier compensation, and on-going support for federal and state programs such as lifeline services to our customers, Carrier of Last Resort obligations and the rural health care universal service support mechanism
- our size, because we are a smaller sized competitor in the markets we serve and we compete against large competitors with substantially greater resources
- the Alaskan economy, which has been impacted by continued low crude oil prices. If sustained, they could have a significant impact on both the level of spending by the State of Alaska and the level of investment in resource development projects by major natural resource exploration and development companies in Alaska. Both outcomes may impact the economy in the markets we serve and impact our future financial performance
- the success of our joint venture with Quintillion Holdings, LLC to provide broadband solutions to the North Slope of Alaska
- our ability to maintain our new cost structure as a more focused broadband and managed information technology ("IT") services company following the sale and subsequent wind-down of our Wireless operations. Maintaining our cost reductions is key to generating cash flow from operating activities. If we fail to maintain these reductions, our financial condition will be impacted
- the cost and availability of future financing, at the terms, and subject to the conditions necessary, to support our business and pursue growth opportunities; our debt could also have negative consequences for our business; for example, it could increase our vulnerability to general adverse economic and industry conditions, or limit our flexibility in planning for, or reacting to, changes in our business and the telecommunications industry; in addition, our ability to borrow funds in the future will depend in part on the satisfaction of the covenants in our credit facilities; if we are unable to satisfy the financial covenants contained in those agreements, or are unable to generate cash sufficient to make required debt payments, the lenders and other parties to those arrangements could accelerate the maturity of some or all of our outstanding indebtedness
- disruptions or failures in the physical infrastructure or operating systems that support our businesses and customers, or cyber-attacks or security breaches of the physical infrastructure, operating systems or devices that our customers use to access our products and services

- our ability to successfully renegotiate the Company's Master Collective Bargaining Agreement with the International Brotherhood of Electrical Workers, Local 1547 ("IBEW") that expired on December 31, 2016 without incurring significant incremental cost. As of the date of this report, negotiations for a new agreement are continuing and the parties will operate under the terms of the prior agreement until a new contract is in place. In the event of a work stoppage, we may be required to utilize cash on hand to support the funding of operations during the affected period
- our ability to keep pace with rapid technological developments and changing standards in the telecommunications industry, including on-going capital expenditures needed to upgrade our network to industry competitive speeds, particularly in light of expected 5G deployments by mobile wireless carriers
- our ability to continue to develop attractive, integrated products and services to evolving industry standards, and meet the pressure from competition to offer these services at lower prices
- unanticipated damage to one or more of our undersea fiber optic cables resulting from construction or digging mishaps, fishing boats or other reasons
- structural declines for voice and other legacy services within the telecommunications industry
- a maintenance or other failure of our network or data centers
- a failure of information technology systems
- a third-party claim that the Company is infringing upon their intellectual property, resulting in litigation or licensing expenses, or the loss of our ability to sell or support certain products
- unanticipated costs required to fund our post-retirement benefit plans, or contingent liabilities associated with our participation in a multi-employer pension plan
- the success or failure of any future acquisitions or other major transactions
- geologic or other natural disturbances relevant to the location of our operations
- the ability to attract, recruit, retain and develop the workforce necessary for implementing our business plan
- the success of the Company's expansion into managed IT services, including the execution of such services for customers
- our internal control over financial reporting may not be effective, which could cause our financial reporting to be unreliable
- our ability to meet or satisfy the terms and conditions of the 2017 Senior Credit Facility or to draw down funds under such facility or to meet its requirements
- our ability to complete the repurchase of our 6.25% Convertible Notes due 2018 or otherwise settle such notes, or repurchase shares of our Common Stock under our repurchase program
- the matters described under Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2016.

In light of these risks, uncertainties and assumptions, you should not place undue reliance on any forward-looking statements. Additional risks that we may currently deem immaterial or that are not currently known to us could also cause the forward-looking events discussed in this Form 10-Q or our other reports not to occur as described. Except as otherwise required by applicable securities laws, we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, changed circumstances or any other reason after the date of this Form 10-Q.

Investors should also be aware that while we do, at various times, communicate with securities analysts, it is against our policy to disclose to them any material non-public information or other confidential information. Accordingly, investors should not assume that we agree with any statement or report issued by an analyst irrespective of the content of the statement or report. To the extent that reports issued by securities analysts contain any projections, forecasts or opinions, such reports are not our responsibility.

OVERVIEW

Over the past five years, through a series of transactions and investments, we have evolved from a wireline and wireless telecom provider to a fiber broadband and managed IT services provider, focused primarily on business and wholesale customers in and out of Alaska. We also provide telecommunication services to consumers throughout the state. Our facilities based communications network extends throughout Alaska and connects to the contiguous states via our two diverse undersea fiber optic cable systems and our usage rights on a third undersea system. Our network is among the most expansive in Alaska and forms the foundation of service to our customers.

Our Market . Management estimates the Alaska wireline telecom and IT services market to be approximately $1.6 billion. This market is comprised of the IT services market of approximately $830 million, the broadband market of approximately $630 million and the voice market of approximately $140 million. Management estimates that over 85% of this market opportunity is from the business and wholesale customer segment.

Competition . We operate in a largely two-player terrestrial wireline market and we estimate our market share to be less than 25% statewide. However, our revenue performance relative to our largest competitor suggests that we are gaining market share in the markets we are serving.

The sections that follow provide information about important aspects of our operations and investments and include discussions of our results of operations, financial condition and sources and uses of cash. In addition, we have highlighted key trends and uncertainties to the extent practicable. The content and organization of the financial and non-financial data presented in these sections are consistent with information we use in evaluating our own performance and allocating our resources.

The Alaska Economy

We operate in a geographically diverse state with unique characteristics. We monitor the state of the economy and, in doing so, we compare Alaska economic activity with broader economic conditions. In general, we believe that the Alaska telecommunications market, as well as general economic activity in Alaska, is affected by certain economic factors, which include:

- investment activity in the oil and gas markets and the price of crude oil
- tourism levels
- governmental spending and activity of military personnel
- the price and price trends of bandwidth
- the growth in demand for bandwidth
- decline in demand for voice and other legacy services
- local customer preferences
- unemployment levels
- housing activity and development patterns

The population of Alaska, which grew marginally in 2016, is approximately 740,000 with Anchorage, Fairbanks and Juneau serving as the primary population and economic centers in the state.

We have observed variances in the factors affecting the Alaska economy as compared to the United States overall. Some factors, particularly the price of oil and gas, have a greater direct impact on the Alaska economy compared to other macro-economic trends impacting the U.S. economy as a whole.

It is estimated that one-third of Alaska’s economy is dependent on federal spending, one-third on natural resources, in particular the production of crude oil, and the remaining one-third on drivers such as tourism, mining, timber, seafood, international air cargo and miscellaneous support services.

Alaska’s economy is dependent on investment by oil companies, and state tax revenues correlate with the price of oil as the State assesses a tax based on the retail price of oil that transits the pipeline from the North Slope. The price of crude oil dropped substantially during the past three years and began to stabilize in 2016. This is primarily impacting the state in two ways:

1. Resource based companies have indicated that, although Alaska is a strategic area of investment, they are reducing their level of spending in the state, and in particular the North Slope, by reducing their operating costs. “In flight” development projects are continuing, however, should the price of oil remain at its current levels, spending on future development is expected to be lower.
2. The State of Alaska budget, which represents approximately 15% of the state’s total economy, is incurring deficits, but has established budgetary reserves that are available through 2017. Proposals to address these deficits include spending reductions, utilization of earnings from the state’s permanent fund and additional revenues, including new fees and taxes. Reduced spending by the State is expected to have a dampening effect on overall economic activity in the state.

Economists believe the Alaskan economy entered a moderate recession beginning in the second half of 2015. They are currently projecting that this recession will continue through at least 2017. The negative effects of the recession have been mitigated by diversity in the Alaskan economy, including growth in the health care and tourism industries.

Our objective is to continue generating sector leading revenue growth in the broadband market through investments in sales, service, marketing and product development while expanding our broadband network capabilities. We also intend to grow our managed IT services market by providing these services to our broadband customers, and are positioning the Company to become the premier Cloud Enabler for business in the state of Alaska. We also seek to continuously improve our customer service, and we use the Net Promoter Score (“NPS”) framework to track the feedback of our customers for virtually all customer interactions. We believe that higher NPS scores will allow us to increasingly provide a differentiated service experience for our customers, which will support our growth. We are focused on expanding our margins, and we utilize the LEAN framework to eliminate waste and simplify how we do business.

Regulatory Update

The items reported under Part I, Item 1. Business – Regulation in our Annual Report on Form 10-K for the year ended December 31, 2016, are updated as follows. This section should be read in conjunction with the corresponding items previously disclosed in our Annual Report.

US Federal Regulatory Matters

On February 23, 2017, the FCC adopted an Order streamlining its regulatory accounting rules and harmonizing them with generally accepted accounting practices. While we are currently evaluating the effects of these rules, they have the potential to reduce our regulatory accounting costs.

On March 28, 2017, Congress passed legislation under the Congressional Review Act ("CRA") preventing the FCC's November 2016 data security and privacy rules from taking effect, and President Trump signed that legislation into law on April 3, 2017. Those rules were originally adopted to govern service providers' use and sharing of information relating to their customers' use of telecommunications services, including mass market broadband Internet access service. Our use and sharing of this information continues to be subject to legal restrictions imposed by the Communications Act of 1934, as amended, even in the absence of the FCC's November 2016 rules. The CRA now prohibits the FCC from re-enacting those rules in substantially the same form as those that Congress blocked, and the FCC has not announced further action in this area.

On April 10, 2017, the Universal Service Administrative Company ("USAC"), which administers the FCC's rural health care universal service support mechanism, confirmed that demand for rural health care support had exceeded the program's $400 million annual cap in Funding Year 2016, which began July 1, 2016. As a result, USAC announced that applicants that filed successful funding requests between September 1 and November 30, 2016 would receive 92.5 percent of the funding for which they were otherwise eligible. On June 30, 2017, the FCC issued a waiver order that permitted us to forego collection of the funding shortfall from our health care provider customers in remote areas of Alaska.

June 30, 2017 was also the deadline for rural health care providers to apply for federal universal service funding for the current year, which started July 1, 2017. USAC has not yet released any estimate of the shortfall that may result from the $400 million annual cap for this current year, but we expect that rigorous review of funding applications, coupled with high demand for funds, will again adversely affect our service revenues associated with health care provider customers. We are continuing to evaluate the impact of the funding cap constraints on our rural health care customers and revenues in light of these developments.

On April 20, 2017, the FCC adopted an Order updating its regulations governing business data services, which are those circuit-switched or packet-switched services that offer our dedicated point-to-point transmission of data at certain guaranteed speeds and service levels using high-capacity connections. The FCC left in place the Phase I and Phase II pricing flexibility it granted to us in 2010, and granted further price deregulation of all business data services with transmission speeds above 45 Megabits per second. For legacy circuit-switched business data services with speeds at or below that level (DS-3 or below), the FCC adopted a new competitive market test, finding that price regulation is no longer required in counties (or county-equivalents, such as Alaskan boroughs) where (a) 50 percent of the buildings in a county are within a half-mile of a location served by a competitive provider; or (b) 75 percent of the census blocks in a county have a cable provider present. We are permitted to remove business data services in competitive areas from our tariffs over the next three years, following which time we will be required to do so. In areas that do not meet this competitive market test, the FCC adjusted its "price cap" rules governing rates for legacy services that will continue to be regulated, but also permitted us to offer those services with volume and term discounts, as well as under contract tariffs, which is the equivalent of the former Phase I pricing flexibility. In general, we expect this FCC Order to support the Company's ability to be market competitive for its business data services.

On May 18, 2017, the FCC opened a proceeding in which it proposed to reverse its 2015 decision to regulate broadband Internet access service as a "telecommunications service" subject to common carrier regulation under Title II of the Communications Act of 1934, as amended. Until 2015, Title II had historically applied only to traditional telephone service. If the FCC adopts its proposal, it is likely to reinstate its historical treatment of broadband Internet access service as an "information service," which is subject to far less intrusive governmental oversight. Regardless of the ultimate classification, the FCC has also sought comment on the extent of the continuing need for the bright line conduct and transparency rules that it adopted in 2015 to ensure both that consumers maintain access to the content, applications, and devices of their choosing as well as meaningful information about their service, and that service providers continue to pursue robust infrastructure investments and innovation. Until the FCC takes final action in this area, it is impossible for us to evaluate the effect that any eventual rule changes may have on our business.

State of Alaska Regulatory Matters

Alaska Universal Service Fund

The Alaska Universal Service Fund (“AUSF”) serves as a complement to the federal Universal Service Fund, but must meet federal statutory criteria concerning consistency with federal rules and regulations. The Regulatory Commission of Alaska (“RCA”) has opened a docket to evaluate and investigate the AUSF and its continued need. The RCA anticipates opening a rulemaking to review the regulations specific to shortfalls.

Other State Regulatory Matters

The RCA opened three dockets on July 27, 2016 to investigate the continued need for Carrier of Last Resort funding (“COLR”) in competitive areas. Two of the dockets investigating the continued need for COLR funding affect the Fairbanks and Juneau markets. This could impact the Company’s future COLR support. COLR funding will continue until the RCA has completed its investigation. On December 23 and 27, 2016, the RCA issued orders for ACSAK and ACSF which issued an initial impression that a carrier of last resort was no longer necessary and allowing the companies to respond. In May, 2017, the RCA issued an order approving the 2016 COLR filing for ACSF but denying the 2016 COLR filing for ACSAK and terminating its COLR status. ACSAK petitioned for reconsideration which was denied and on July 14, 2017 filed a notice of appeal in the Anchorage Superior Court. The RCA denied ACSAK’s request for 2017 COLR filing and reinstatement of COLR status. The Company filed for 2017 COLR funding for ACSN and ACSF. The RCA suspended these filings on July 31, 2017. ACSF also filed for reconsideration of the RCA COLR order impacting it. That petition was similarly denied and the Company is currently considering its options.

Business Plan Core Principles

Our results of operations, financial position and sources and uses of cash in the current and future periods reflect our focus on being the most successful broadband solutions company in Alaska by delivering the best customer experience in the markets we choose to serve. To do this we will continue to:

- ***Create a Workplace That Develops Our People and Celebrates Success*** We believe an engaged workforce is critical to our success. We are deeply committed to the development of our people and creating opportunities for them.
- ***Create a Consistent Customer Experience Every Time*** We strive to deliver service as promised to our customers, and make it right if our customers are not satisfied with what we delivered. We track virtually every customer interaction and we utilize the Net Promoter Score framework for assessing the satisfaction of our customers.
- ***Relentlessly Simplify How We Do Business*** We believe we must reduce waste, which is defined as any activity that does not add value to its intended customer. Doing so improves the experience we deliver to our customers. We make investments in technology and process improvement, utilize the LEAN framework, and expect these efforts to meaningfully impact our financial performance in the long-term.
- ***Offer Broadband Solutions to Our Customers at Work and Home*** We are building on strength in designing, building and operating quality broadband networks and providing new products and solutions to our customers.

We believe we can create value for our shareholders by:

- Driving revenue growth through increasing business broadband and managed IT service revenues,
- Generating Adjusted EBITDA and Adjusted Free Cash Flow growth through cost management, and
- Careful allocation of capital, including selectively investing success based capital into opportunities that generate appropriate return on investment.

2017 Operating Initiatives

- Business and Wholesale revenue growth driven by new customers, including those utilizing the North Slope fiber network.
- Continued expansion of managed IT services, including increased product offerings to existing customers.
- Consumer revenue growth driven by sustained broadband additions at 10MB and above and new product offerings.
- Manage cost structure growth by effective allocation of resources, and managing labor and healthcare costs.
- Effectively manage capital spending, focusing on customer opportunities, strategic initiatives, maintenance and utilization of funding received through CAF II support.
- Continue improving the service experience to all of our customers in a differentiated manner from our competition.
- Drive continued improvements in our service delivery organization to shorten service intervals and meet customers’ desired due dates.
- Consider strategic opportunities in and out of Alaska that address scale and geographic diversification and reduce the risk of investments made in our company.
- Continue our deployment of broadband solutions such as hosted VoIP and VPLS, and take advantage of our Metro Ethernet Forum designation.
- Continue building strategic customer relationships, including with anchor tenant type customers.

Revenue Sources by Customer Group

We manage our revenues based on the sale of services and products to the three customer categories listed below.

- **Business and Wholesale (broadband, voice and managed IT services)**
- **Consumer (broadband and voice services)**
- **Regulatory (access services, high cost support and carrier termination)**

Business and Wholesale

Providing services to Business and wholesale customers provides the majority of our revenues and is expected to continue being the primary driver of our growth over the next few years. Our business customers include large enterprises, government customers and small and medium business. We were the first Alaska-based carrier to be Carrier Ethernet 2.0 Certified and are currently the only Alaska-based carrier certified for multipoint-to-multipoint service. This certification means that we meet international standards for the quality of our broadband services. We also offer IP based voice including the largest SIP implementations in the state of Alaska, and are the first Microsoft Express Route provider in the state. We believe our network differentiates us in the markets we serve, because we prefer not to compete on price; but on the quality, reliability and the overall value of our solutions. Accordingly, we have significant capacity to "sell into" the network we operate and do so at what we believe are attractive incremental gross margins.

Business services have experienced significant growth and we believe the incremental economics of business services are attractive. Given the demand from our customers for more bandwidth and services, we expect revenue growth from these customers to continue for the foreseeable future. We provide services such as voice and broadband, managed IT services including remote network monitoring and support, managed IT security and IT professional services, and long distance services primarily over our own terrestrial network. We are also positioning the Company to become the premier Cloud Enabler for business in the state of Alaska.

Our wholesale customers are primarily national and international telecommunications carriers who rely on us to provide connectivity for broadband and other needs to access their customers over our Alaskan network. The wholesale market is characterized by larger transactions that can create variability in our operating performance. We have a dedicated sales team that sells into this customer segment, and we expect wholesale revenue to grow for the foreseeable future.

Consumer

We also provide voice and broadband services to residential customers. Given that our primary competitor has extensive quad play capabilities (video, voice, wireless and broadband) we target how and where we offer products and services to this customer group in order to maintain our returns. Our focus is to leverage the capabilities of our existing network and sell customers our highest available bandwidth. Our primary competitive advantage is that we offer reliable internet service without data caps, while our competitor charges customers or throttles customers' speeds for exceeding given levels of data usage. Overall revenues from these customers began to stabilize in the second half of 2016 and we have realized consistent growth in consumer broadband revenues in 2016 and 2017.

Regulatory

Regulatory revenue is generated from three primary sources: (i) Access charges, which include interstate and intrastate switched access and special access charges, and cellular access; (ii) Surcharges billed to the end user (pass-through and non-pass-through); and (iii) federal and state support. We provide voice and broadband origination and termination services to interstate and intrastate carriers. While we are compensated for these services, these revenue streams have been in decline and we expect them to continue to decline. In addition, as regulators have reformed traditional access charges, they have simultaneously implemented new end user surcharges that contribute to our revenue.

Access Charges

Interstate and intrastate switched access are services based primarily on originating and terminating access minutes from other carriers. Special access is primarily access to dedicated circuits sold to wholesale customers, substantially all of which is generated from interstate services. Cellular access is the transport of tariffed local network services between switches for cellular companies based on individually negotiated contracts.

Surcharges

We assess our customers for surcharges, typically on a monthly basis, as required by various state and federal regulatory agencies, and remit these surcharges to these agencies. These pass-through surcharges include Federal Universal Access and State Universal Access. These surcharges vary from year to year, and are primarily recognized as revenue, and the subsequent remittance to the state or federal agency as a cost of sale and service. The rates imposed by the regulators continue to increase. However, because the charges are only assessed on a portion of our services, and that portion continues to decline, we expect these revenue streams to decline over time as the revenue base declines. Other non-pass-through surcharges are collected from our customers as authorized by the regulatory body. The amount charged is based on the type of line: single line business, multi-line business, consumer or lifeline. The rates are established based on federal or state orders. These charges are recorded as revenue and do not have a direct associated cost. Rather, they represent a revenue recovery mechanism established by the FCC or the Regulatory Commission of Alaska.

Federal and State Support

We receive interstate and intrastate universal support funds and similar revenue streams structured by federal and state regulatory agencies that allow us to recover our cost of providing universal service in Alaska. For the year ending December 31, 2016, the Company recognized $19.7 million in federal high cost universal service revenues to support our wireline operations in high cost areas. The FCC has released the CAF Phase II order specific to Alaska Communications which transitioned from CAF Phase I frozen support to CAF Phase II. Funding under the new program will generally require the Company to provide broadband service to unserved locations throughout the designated coverage area by the end of a specified build-out period, and meet interim milestone build-out obligations. In addition to federal high cost support, the Company is designated by the State of Alaska as a Carrier of Last Resort (“COLR”) in five of the six study areas. In addition to COLR, the Company receives Carrier Common Line (“CCL”) support. We do not receive COLR or CCL funding for the ACS of Anchorage study area. As a COLR we are required to provide services essential for retail and carrier-to-carrier telecommunication throughout the applicable coverage area.

Executive Summary

The following summary should be read in conjunction with “Non-GAAP Financial Measures” included in this Management’s Discussion and Analysis of Financial Condition and Results of Operations.

Operating Revenues

Total revenue of $58.5 million increased $2.3 million, or 4.0%, in the second quarter of 2017 compared with the second quarter of 2016. Business and wholesale revenue increased $2.7 million, or 8.1%, driven by broadband growth totaling $3.7 million, or 16.7%. Consumer and regulatory revenue each declined $0.2 million. Total broadband revenue increased $3.9 million, or 13.9%.

Operating Income

Operating income of $5.6 million in the second quarter of 2017 increased $1.2 million, or 28.3%, compared with the second quarter of 2016 due to higher revenue, partially offset by marginally higher operating expenses. These items are discussed in more detail below.

Adjusted EBITDA

Adjusted EBITDA of $14.6 million in the second quarter of 2017 increased $0.6 million, or 4.4%, from $14.0 million in the second quarter of 2016 due primarily to the growth in broadband revenue. See “Non-GAAP Financial Measures” for the definition of Adjusted EBITDA and a reconciliation of Adjusted EBITDA to Net Income. As discussed in “Non-GAAP Financial Measures,” the Company does not provide a reconciliation of guidance for Adjusted EBITDA to Net (Loss) Income.

Operating Metrics

Business broadband average monthly revenue per user (“ARPU”) of $367.93 in the second quarter of 2017 increased from $313.92 in the second quarter of 2016. Business broadband connections of 15,475 at June 30, 2017, increased marginally from connections of 15,347 at June 30, 2016. We count connections on a unitary basis regardless of the size of the bandwidth. For example, a customer that has a 10MB connection is counted as one connection as is a customer with a 1MB connection. While we present metrics related to Business connections, we note that we manage Business and wholesale in terms of new Monthly Recurring Charges (“MRC”) sold. Achievement of sales performance in terms of MRC is the primary operating metric used by management to measure market performance. For competitive reasons, we do not disclose our sales or performance in MRC.

Consumer broadband connections of 34,675 were up 2.2% year over year due to growth in home internet subscribers. Consumer broadband ARPU of $61.57 in the second quarter of 2017 increased from $60.91 in the second quarter of 2016.

The table below provides certain key operating metrics as of or for the periods indicated.

	June 30, 2017	June 30, 2016
Voice:		
At quarter end:		
Business access lines	72,972	75,646
Consumer access lines	31,542	35,600
Quarter:		
ARPU - business	$ 23.20	$ 23.79
ARPU - consumer	$ 27.81	$ 28.61
Year-to-date:		
ARPU - business	$ 23.28	$ 23.65
ARPU - consumer	$ 28.14	$ 28.91
Broadband:		
At quarter end:		
Business connections	15,475	15,347
Consumer connections	34,675	33,913
Quarter:		
ARPU - business	$367.93	$313.92
ARPU - consumer	$ 61.57	$ 60.91
Year-to-date:		
ARPU - business	$360.62	$311.60
ARPU - consumer	$ 61.36	$ 60.47

Liquidity

We generated cash from operating activities of $17.1 million in the first six months of 2017 compared with $18.9 million in the first six months of 2016. This decline was due primarily to an increase in accounts receivable, including those associated with certain rural health care customers, mostly offset by improved operating results.

In the first six months of 2017, we invested a total of $13.0 million of cash in capital, including the settlement of items accrued in previous periods.

In the first quarter of 2017 we entered into the 2017 Senior Credit Facility and the settled our 2015 Senior Credit Facilities. This transaction extends our senior debt maturities to 2022 and 2023 and provided funding for the tender, repurchase or settlement at maturity of our 6.25% Notes due in 2018. In the second quarter of 2017 we completed the tender offer and settled the 6.25% Notes in an aggregate principal amount of $84.0 million.

Net debt (defined as total debt excluding debt issuance costs, less cash, cash equivalents and restricted cash held for settlement of the 6.25% Notes) at June 30, 2017 was $171.0 million compared with $162.8 million at December 31, 2016. The increase reflects the utilization of $15.0 million of cash in the settlement of our 2015 Senior Credit Facilities and tender of our 6.25% Notes and other changes in working capital.

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RESULTS OF OPERATIONS

The following table summarizes our results of operations for the three-month periods ended June 30, 2017 and 2016.

Three Months Ended June 30, 2017 Compared to Three Months Ended June 30, 2016

(in thousands)	2017	2016	Change	% Change
Operating revenues:				
Business and wholesale revenue				
Business broadband	$16,954	$14,392	$ 2,562	17.8%
Business voice and other	6,601	7,022	(421)	-6.0%
Managed IT services	1,151	818	333	40.7%
Equipment sales and installations	1,343	2,097	(754)	-36.0%
Wholesale broadband	8,941	7,791	1,150	14.8%
Wholesale voice and other	1,612	1,743	(131)	-7.5%
Total business and wholesale revenue	36,602	33,863	2,739	8.1%
Consumer revenue				
Broadband	6,460	6,234	226	3.6%
Voice and other	2,802	3,259	(457)	-14.0%
Total consumer revenue	9,262	9,493	(231)	-2.4%
Total business, wholesale and consumer revenue	45,864	43,356	2,508	5.8%
Growth in broadband revenue	*13.9%*			
Regulatory revenue				
Access	7,748	7,986	(238)	-3.0%
High cost support	4,924	4,920	4	0.1%
Total regulatory revenue	12,672	12,906	(234)	-1.8%
Total operating revenues	$58,536	$56,262	$ 2,274	4.0%
Operating expenses:				
Cost of services and sales (excluding depreciation and amortization)	26,454	25,543	911	3.6%
Selling, general and administrative	17,438	17,586	(148)	-0.8%
Depreciation and amortization	9,028	8,640	388	4.5%
Loss on disposal of assets, net	14	128	(114)	-89.1%
Total operating expenses	52,934	51,897	1,037	2.0%
Operating income	5,602	4,365	1,237	28.3%
Other income and (expense):				
Interest expense	(3,913)	(3,852)	(61)	1.6%
Loss on extinguishment of debt	(5,158)	—	(5,158)	NM
Interest income	7	6	1	16.7%
Total other income and (expense)	(9,064)	(3,846)	(5,218)	NM
(Loss) income before income tax benefit (expense)	(3,462)	519	(3,981)	NM
Income tax benefit (expense)	632	(236)	868	NM
Net (loss) income	(2,830)	283	(3,113)	NM
Less net loss attributable to noncontrolling interest	(32)	(34)	2	-5.9%
Net (loss) income attributable to Alaska Communications	$ (2,798)	$ 317	$(3,115)	NM

Operating Revenue

Business and Wholesale

Business and wholesale revenue of $36.6 million increased $2.7 million, or 8.1%, in the second quarter of 2017 from $33.9 million in the second quarter of 2016. This improvement was primarily driven by a $2.6 million increase from new and existing customers buying or increasing their consumption of bandwidth using our advanced network services such as multi-protocol label switching (“MPLS”), dedicated Internet and Enhanced Metro Ethernet. Business broadband ARPU drove overall revenue growth and reflects customer demand for increasing amounts of bandwidth. Business broadband ARPU increased to $367.93 in the second quarter of 2017 from $313.92 in the second quarter of 2016, or 17.2%, and Business broadband connections increased marginally year over year. Wholesale broadband revenue increased $1.2 million and Managed IT services increased $0.3 million. These increases were partially offset by a $0.8 million decline in equipment sales and installations and a $0.6 million decline in voice and other revenue. Business voice connections decreased 2,674, or 3.5%, year over year and ARPU of $23.20 was down marginally compared with $23.79 in 2016. While connections and ARPU serve as data points to support the analysis of period-over-period changes in revenue, they are not critical indicators utilized by the Company to manage the Business and Wholesale customer group.

Consumer

Consumer revenue of $9.3 million decreased $0.2 million, or 2.4%, in the second quarter of 2017. Broadband revenue increased 3.6% year over year due to a 762, or 2.2%, increase in connections and a 1.1% increase in ARPU to $61.57 from $60.91 in the prior year. Voice and other revenue decreased $0.5 million primarily due to 4,058 fewer connections and a decrease in ARPU to $27.81 from $28.61 in the prior year.

Regulatory

Regulatory revenue of $12.7 million decreased $0.2 million, or 1.8%, in the second quarter of 2017 from $12.9 million in the second quarter of 2016. Access revenue declined $0.2 million due to lower eligible access lines combined with lower rates. High cost support was unchanged year over year.

Operating Expenses

Cost of Services and Sales (excluding depreciation and amortization)

Cost of services and sales of $26.5 million increased $0.9 million, or 3.6%, in the second quarter of 2017 from $25.6 million in the second quarter of 2016. This increase primarily reflects increased circuit, installation and data costs, partially offset by lower labor costs.

Selling, General and Administrative

Selling, general and administrative expenses of $17.4 million decreased $0.2 million, or 0.8%, in the second quarter of 2017 from $17.6 million in the second quarter of 2016. This decrease reflects lower labor costs mostly offset by an increase in the allowance for doubtful accounts, including $1.1 million associated with rural health care customers.

Depreciation and Amortization

Depreciation and amortization expense of $9.0 million increased $0.4 million, or 4.5%, in the second quarter of 2017 from $8.6 million in the second quarter of 2016. This increase reflects, in part, broadband equipment (which typically has shorter depreciable lives) comprising an increased proportion of the Company’s assets.

Other Income and Expense

Interest expense of $3.9 million in the second quarter of 2017 compares with $3.9 million in the second quarter of 2016. As discussed below, the Company completed its refinancing transaction in March and April 2017. The cost of borrowing under the 2017 Senior Credit Facility is similar to that of the 2015 Senior Credit Facilities. The $5.2 million loss on extinguishment of debt in the second quarter of 2017 was associated with settlement of the Tender Offer on the Company’s 6.25% Notes and included the write-off of unamortized debt issuance costs and discounts, and third-party fees.

Income Taxes

The income tax benefit and effective tax rate in the second quarter of 2017 of $0.6 million and 18.3%, respectively, reflect the impact of permanent book to tax differences. Income tax expense and the effective tax rate in the second quarter of 2016 were $0.2 million and 45.5%, respectively.

Net Loss Attributable to Noncontrolling Interest

The net loss attributable to the noncontrolling interest of our joint venture with QHL was $32 thousand and $34 thousand in the second quarter of 2017 and 2016, respectively.

Net Income Attributable to Alaska Communications

The net loss attributable to Alaska Communications of $2.8 million in the second quarter of 2017 compares with net income of $0.3 million in the same period of 2016. The year over year results reflect the revenue and expense items discussed above.

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The following table summarizes our results of operations for the six-month periods ended June 30, 2017 and 2016.

Six Months Ended June 30, 2017 Compared to Six Months Ended June 30, 2016

(in thousands)	2017	2016	Change	% Change
Operating revenues:				
Business and wholesale revenue				
Business broadband	$ 33,235	$ 28,572	$ 4,663	16.3%
Business voice and other	13,232	14,112	(880)	-6.2%
Managed IT services	2,058	1,899	159	8.4%
Equipment sales and installations	2,117	3,684	(1,567)	-42.5%
Wholesale broadband	17,258	15,389	1,869	12.1%
Wholesale voice and other	3,241	3,758	(517)	-13.8%
Total business and wholesale revenue	71,141	67,414	3,727	5.5%
Consumer revenue				
Broadband	12,878	12,376	502	4.1%
Voice and other	5,712	6,641	(929)	-14.0%
Total consumer revenue	18,590	19,017	(427)	-2.2%
Total business, wholesale and consumer revenue	89,731	86,431	3,300	3.8%
Growth in broadband revenue	*12.5%*			
Regulatory revenue				
Access	15,689	16,158	(469)	-2.9%
High cost support	9,847	10,001	(154)	-1.5%
Total regulatory revenue	25,536	26,159	(623)	-2.4%
Total operating revenues	$115,267	$112,590	$ 2,677	2.4%
Operating expenses:				
Cost of services and sales (excluding depreciation and amortization)	51,596	51,671	(75)	-0.1%
Selling, general and administrative	35,531	34,926	605	1.7%
Depreciation and amortization	17,931	17,160	771	4.5%
Loss on disposal of assets, net	33	152	(119)	-78.3%
Total operating expenses	105,091	103,909	1,182	1.1%
Operating income	10,176	8,681	1,495	17.2%
Other income and (expense):				
Interest expense	(7,758)	(7,721)	(37)	0.5%
Loss on extinguishment of debt	(7,434)	(336)	(7,098)	NM
Interest income	14	11	3	27.3%
Total other income and (expense)	(15,178)	(8,046)	(7,132)	88.6%
(Loss) income before income tax benefit (expense)	(5,002)	635	(5,637)	NM
Income tax benefit (expense)	1,464	(299)	1,763	NM
Net (loss) income	(3,538)	336	(3,874)	NM
Less net loss attributable to noncontrolling interest	(64)	(67)	3	-4.5%
Net (loss) income attributable to Alaska Communications	$ (3,474)	$ 403	$(3,877)	NM

Operating Revenue

Business and Wholesale

Business and wholesale revenue of $71.1 million increased $3.7 million, or 5.5%, in the six-month period of 2017 from $67.4 million in the six-month period of 2016. This improvement was primarily driven by a $4.7 million increase from new and existing customers buying or increasing their consumption of bandwidth using our advanced network services. Business broadband ARPU drove overall revenue growth and reflects customer demand for increasing amounts of bandwidth. Business broadband ARPU increased to $360.62 in the six-month period of 2017 from $311.60 in the six-month period of 2016, or 15.7%, and Business broadband connections increased marginally year over year. Wholesale broadband revenue increased $1.9 million and Managed IT services increased $0.2 million. These increases were partially offset by a $1.6 million decline in equipment sales and installations and a $1.4 million decline in voice and other revenue. Business voice connections decreased 2,674, or 3.5%, year over year and ARPU of $23.28 was down marginally compared with $23.65 in 2016. While connections and ARPU serve as data points to support the analysis of period-over-period changes in revenue, they are not critical indicators utilized by the Company to manage the Business and Wholesale customer group.

Consumer

Consumer revenue of $18.6 million decreased $0.4 million, or 2.2%, in the six-month period of 2017. Broadband revenue increased 4.1% year over year due to a 762, or 2.2%, increase in connections and a 1.5% increase in ARPU to $61.36 from $60.47 in the prior year. Voice and other revenue decreased $0.9 million primarily due to 4,058 fewer connections and a decrease in ARPU to $28.14 from $28.91 in the prior year.

Regulatory

Regulatory revenue of $25.5 million decreased $0.6 million, or 2.4%, in the six-month period of 2017 from $26.1 million in the six-month period of 2016. Access revenue declined $0.5 million due to lower eligible access lines combined with lower rates. High cost support declined $0.2 million year over year due to a one-time $0.2 million increase recorded in 2016.

Operating Expenses

Cost of Services and Sales (excluding depreciation and amortization)

Cost of services and sales of $51.6 million decreased $0.1 million, or 0.1%, in the six-month period of 2017 from $51.7 million in the six-month period of 2016. This decrease primarily reflects lower labor and data costs, mostly offset by higher installation costs.

Selling, General and Administrative

Selling, general and administrative expenses of $35.5 million increased $0.6 million, or 1.7%, in the six-month period of 2017 from $34.9 million in the six-month period of 2016. This increase primarily reflects an increase in the allowance for doubtful accounts, including $1.1 million associated with rural health care customers recorded in the second quarter, and marketing costs, partially offset by lower labor costs.

Depreciation and Amortization

Depreciation and amortization expense of $17.9 million increased $0.8 million, or 4.5%, in the six-month period of 2017 from $17.1 million in the six-month period of 2016. This increase reflects, in part, broadband equipment (which typically has shorter depreciable lives) comprising an increased proportion of the Company’s assets.

Other Income and Expense

Interest expense of $7.8 million in the six-month period of 2017 compares with $7.7 million in the six-month period of 2016. As discussed below, the Company completed its refinancing transaction in March and April 2017. The cost of borrowing under the 2017 Senior Credit Facility is similar to that of the 2015 Senior Credit Facilities. The $7.4 million loss on extinguishment of debt in the six-month period of 2017 included $5.1 million associated with settlement of the Tender Offer on the Company’s 6.25% Notes in the second quarter and $2.3 million associated with the settlement of the 2015 Senior Credit Facilities in the first quarter. The $0.3 million loss on extinguishment of debt in the six-month period of 2016 was associated with the repurchase of the 6.25% Notes in the principal amount of $10.0 million.

Income Taxes

The income tax benefit and effective tax rate in the six-month period of 2017 of $1.5 million and 29.3%, respectively, reflect the impact of permanent book to tax differences. Income tax expense and the effective tax rate in the six-month period of 2016 were $0.3 million and 47.1%, respectively.

Net Loss Attributable to Noncontrolling Interest

The net loss attributable to the noncontrolling interest of our joint venture with QHL was $64 thousand and $67 thousand in the six-month periods of 2017 and 2016, respectively.

Net Income Attributable to Alaska Communications

The net loss attributable to Alaska Communications of $3.5 million in the six-month period of 2017 compares with net income of $0.4 million in the same period of 2016. The year over year results reflect the revenue and expense items discussed above.

FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

Cash Flows

We satisfied our cash requirements for operations, capital expenditures and scheduled debt service under our 2015 Senior Credit Facilities in the first six months of 2017 through internally generated funds and cash on hand. At June 30, 2017, we had $13.0 million of cash and cash equivalents, $11.9 million of restricted cash, $10.0 million of which was designated for repurchase of the 6.25% Notes, and a $15.0 million undrawn revolving credit facility.

Our major sources and uses of funds in the six months ended June 30, 2017 and 2016 were as follows:

(in thousands)	2017	2016
Net cash provided by operating activities	$ 17,065	$ 18,886
Capital expenditures	$ (10,522)	$(13,662)
Change in unsettled capital expenditures	$ (2,043)	$ (9,156)
Proceeds on sale of assets	$ 4	$ 2,663
Repayments of long-term debt	$(174,013)	$(11,486)
Proceeds from the issuance of long-term debt	$ 183,000	$ —
Debt issuance costs and discounts	$ (5,508)	$ (44)
Cash paid for debt extinguishment	$ (5,279)	$ (150)
Interest paid (1)	$ (7,595)	$ (6,359)
Payment of withholding taxes on stock-based compensation	$ (599)	$ (472)
Income taxes refunded (paid), net (1)	$ 572	$ (577)

(1) Included in net cash provided by operating activities.

Cash Flows from Operating Activities

Cash provided by operating activities of $17.1 million in the first six months of 2017 compares with $18.9 million in the first six months of 2016. The year over year decrease was primarily due to higher accounts receivable in 2017 as described below and higher interest payments, partially offset by payments in 2016 associated with the wind-down of wireless operations. Interest payments, net of cash interest income and including capitalized interest, were $7.6 million and $6.4 million in the first six months of 2017 and 2016, respectively.

Cash provided by operating activities of $17.1 million in the first six months of 2017 reflects net income excluding non-cash items (defined as cash provided by operating activities excluding changes in operating assets and liabilities) of $23.3 million offset by a $5.4 million decrease in accounts payable and other current liabilities and a $1.2 million increase in accounts receivable and other current assets. The decrease in accounts payable and other current liabilities includes incentive compensation payments and cash interest payments of $7.6 million. The increase in accounts receivable was largely due to the timing of receipts from certain rural health care customers.

Cash provided by operating activities of $18.9 million in the first six months of 2016 reflects net income excluding non-cash items of $20.0 million and a $3.1 million decrease in accounts receivable and other current assets, including the effect of payments from certain rural health care customers. These items were partially offset by a $3.2 decrease in accounts payable and other current liabilities reflecting incentive compensation, interest, and Wireless Sale transaction wind-down payments.

Cash Flows from Investing Activities

Cash used by investing activities of $13.0 million in the first six months of 2017 consisted primarily of expenditures on capital totaling $12.6 million. Of $10.5 million incurred in 2017, $5.9 million was success based versus maintenance.

Cash used by investing activities of $20.7 million in the first six months of 2016 consisted primarily of expenditures on capital totaling $22.8 million including the second $5.5 million payment for the purchase of the Fiber Optic System in 2015. Of $13.7 million incurred in 2016, $6.5 million was success based versus maintenance. Proceeds on the sale of assets included the second payment of $2.7 million for the fiber stands sold to QHL in 2015.

Our networks require the timely maintenance of plant and infrastructure. Future capital requirements may change due to impacts of regulatory decisions that affect our ability to recover our investments, changes in technology, the effects of competition, changes in our business strategy, and our decision to pursue specific acquisition and investment opportunities. Capital spending is typically higher during the second and third quarters. We intend to fund future capital expenditures with cash on hand and net cash generated from operations.

Cash Flows from Financing Activities

Cash used by financing activities were $2.3 million in the first six months of 2017. Repayments of long-term debt of $174.0 million included repayment of the outstanding principal of the 2015 Senior Credit Facilities of $86.8 million, settlement of the tender offer on the Company's 6.25% Notes in the principal amount of $84.0 million and repayment of a $3.0 million draw on the revolving credit facility. Proceeds from the issuance of long-term debt of $183.0 million consisted of gross proceeds of $180.0 million from the issuance of the 2017 Senior Credit Facility and a $3.0 million draw on the revolving credit facility. Payment of debt issuance costs and discounts of $5.5 million were associated with the issuance of the 2017 Senior Credit Facility. Cash paid for debt extinguishment of $5.3 million was associated with settlement of the 2015 Senior Credit Facilities and the tender offer on the 6.25% Notes.

Cash used by financing activities of $11.9 million in the first six months of 2016 consisted primarily of the repurchase of $10.0 million principal amount of our 6.25% Notes for $9.8 million and scheduled principal payment on the First Lien Term Loan of our 2015 Senior Credit Facilities totaling $1.5 million.

Liquidity and Capital Resources

Consistent with our history, our current and long-term liquidity could be impacted by a number of challenges, including, but not limited to: (i) potential future reductions in our revenues resulting from governmental and public policy changes, including regulatory actions affecting inter-carrier compensation and changes in revenue from Universal Service Funds; (ii) servicing our debt and funding principal payments; (iii) the funding of other obligations, including our pension plans and lease commitments; (iv) competitive pressures in the markets we serve; (v) the capital intensive nature of our industry; (vi) our ability to respond to and fund the rapid technological changes inherent to our industry, including new products; and (vii) our ability to obtain adequate financing to support our business and pursue growth opportunities.

We are responding to these challenges by (i) driving top line growth in broadband service revenues with a focus on business and wholesale customers; (ii) managing our cost structure to deliver consistent Adjusted EBITDA and Adjusted Free Cash flow performance; and (iii) holding capital spending to approximately $35 million annually.

On March 13, 2017, we entered into the 2017 Senior Credit Facility consisting of a Term A-1 Facility of $120 million, a Term A-2 Facility of $60 million and a revolving facility of $15 million. On March 28, 2017, the 2017 Senior Credit Facility was funded.

The obligations under the 2017 Senior Credit Facility are secured by substantially all personal property and certain material real property owned by the Company and its wholly-owned subsidiaries, with certain exceptions. The 2017 Senior Credit Facility contains customary representations, warranties and covenants, including covenants limiting the incurrence of debt, declaring dividends, making investments, dispositions, and entering into mergers and acquisitions. Repurchases of the Company's common stock are subject to a $10 million limitation, satisfying a minimum liquidity and cash-flow requirement and other conditions as described in the Agreement. Upon achieving certain Net Total Leverage Ratio targets, additional repurchases may be made. The

2017 Senior Credit Facility provides for events of default customary for credit facilities of this type, including non-payment under the agreement, breach of warranty, breach of covenants, defaults on other debt, incurrence of liens on collateral, change of control and insolvency, all as defined in the Agreement. Consequences of an event of default are defined in the Agreement.

The 2017 Senior Credit Facility requires the maintenance of certain financial ratios as defined in the Agreement and summarized below. The Company was in compliance with all relevant financial ratios at June 30, 2017.

Net Total Leverage Ratio: The ratio of our (a) total debt, less unrestricted cash and cash equivalents held in pledged accounts, less cash held for repurchase or repayment of the 6.25% Notes to (b) Consolidated EBITDA (as defined more specifically below) for the consecutive four fiscal quarters ending as of the calculation date. The maximum allowable net total leverage ratio is provided in the table below.

Period	Ratio
March 28, 2017 through June 30, 2017	3.75 to 1.00
July 1, 2017 through December 31, 2017	3.50 to 1.00
January 1, 2018 through June 30, 2018	3.25 to 1.00
July 1, 2018 through December 31, 2018	3.00 to 1.00
January 1, 2019 through September 30, 2019	2.75 to 1.00
October 1, 2019 and thereafter	2.50 to 1.00

The actual net total leverage ratio was 2.93 at June 30, 2017.

Fixed Charge Coverage Ratio: The ratio of our (a) Consolidated EBITDA for the consecutive four fiscal quarters ending as of the calculation date to (b) the sum of, for the same period, consolidated interest expense, capital expenditures (with certain exceptions), the current portion of long term debt including capital lease obligations, restricted payments, and cash payments for income taxes. This ratio is calculated at June 30, 2017 using the most recent fiscal quarter multiplied by four; at September 30, 2017 using the most recent two fiscal quarters multiplied by two; and at December 31, 2017 using the most recent three fiscal quarters multiplied by four-thirds. The minimum fixed charge coverage ratio is 1.05 to 1.00 commencing June 30, 2017. The actual fixed charge coverage ratio was 1.08 at June 30, 2017.

Consolidated EBITDA , as defined in the 2017 Senior Credit Facility, means consolidated net income attributable to Alaska Communications, plus (to the extent deducted in calculating net income) the sum of:

- cash and non-cash interest expense;
- depreciation and amortization expense;
- income taxes;
- other non-cash charges and expenses, including equity-based compensation expense;
- the write down or write off on any assets, other than accounts receivable;
- subject to limitation, fees and out-of-pocket transaction costs incurred in connection with the 2017 refinancing transactions;
- unusual, non-recurring losses, charges and expenses;
- one-time costs associated with permitted acquisitions; and
- cost savings from synergies in connection with permitted acquisitions or dispositions.

minus (to the extent included in calculating net income) the sum of:

- unusual, non-recurring gains on permitted sales or dispositions of assets and casualty events;
- cash and non-cash interest income;
- other unusual nonrecurring items;
- the write up of any asset;
- patronage refunds or similar distributions from any lender; and
- the Company's share of earnings in its joint venture with Quintillion if such earnings exceed $0.5 million and at least 50% of the Company's share in such earnings have not been received in cash by the Company.

Consolidated EBITDA as defined in the 2017 Senior Credit Facility is not a GAAP measure and is not consistent with Adjusted EBITDA presented elsewhere in Management's Discussion and Analysis of Financial Condition and Results of Operations.

The Term A-1 Facility bears interest at LIBOR plus 5.0% per annum, with a LIBOR minimum of 1.0%. The Term A-2 Facility bears interest at LIBOR plus 7.0% per annum, with a LIBOR minimum of 1.0%. The revolving facility bears interest at LIBOR plus 5.0% per annum, with a LIBOR minimum of 1.0%.

The weighted interest rate on the 2017 Senior Credit Facility was 6.89% at June 30, 2017.

As required under the terms of the 2017 Senior Credit Facility and as a component of its cash flow hedging strategy, the Company has entered into interest rate hedges sufficient to effectively fix or limit the interest rate on borrowings under the 2017 Senior Credit Facility of $90.0 million through June 28, 2019.

In the second quarter of 2017, the Company's Board of Directors authorized a program to repurchase up to $10 million of the Company's outstanding common stock. Repurchases can be conducted in the open market or through private transactions, including through purchases made in accordance with Rule 10b plans. The timing and amount of repurchases will be determined by the Company based on its evaluation of market conditions, its financial position, the trading price of its stock and other factors. The Company intends to use cash on hand to fund share repurchases subject to, among other things, federal and state securities, corporate and other laws and regulations, and the Company's financing arrangements. Shares repurchased under this program will be accounted for as treasury stock.

The Federal Communications Act requires the FCC to establish a universal service program to ensure that affordable, quality telecommunications services are available to all Americans. We have received universal support in several forms, including support from the Federal Rural Health Care universal service support mechanism, which supports telemedicine and rural health care communications through increased connectivity. This program has been in existence since 1999 and is an important contributor in supporting health care programs in high cost areas of the United States, including Alaska. While rural health care represents an important sector for us and we see continued opportunity in the long term, it represents less than 10% of our total revenue.

As discussed under *US Federal Regulatory Matters* , on April 10, 2017, USAC confirmed that demand for rural health care support had exceeded the program's $400 million annual cap in Funding Year 2016, which began July 1, 2016 and ended on June 30, 2017. As a result, USAC announced that applicants that filed successful funding requests between September 1 and November 30, 2016 would receive 92.5 percent of the funding for which they were otherwise eligible. On June 30, 2017, the FCC issued an order to Alaskan health care providers impacted by the Rural Health Care Program pro-ration, allowing customers unable to fund the shortfall to remain in regulatory compliance with the program. We subsequently notified this subset of our customers that, subject to certain terms and conditions, we would suspend collection of the funding shortfall for Funding Year 2016. In the second quarter, we recorded a charge of $1.1 million to fully reserve the effect of the funding shortfall for Funding Year 2016 on our rural health care customers. Our accounts receivable balance for all rural health care customers, net of amounts reserved, was $4.2 million at June 30, 2017, including $1.5 million from rural health care customers who have not yet received notification from USAC that their funding requests for Funding Year 2016 have been approved. We will continue to evaluate the impact of potential shortfalls in Funding Year 2016 on our accounts receivable.

Due to the geographic remoteness and the limited availability of staff, telemedicine will be a key facilitator of more timely and advanced medical attention across the state of Alaska and the demand for technology-enabled health care delivery will remain strong. We currently believe that the rural health care market will continue to grow in future years, and will continue to be an important part of our business. The funding shortfall for Funding Year 2016 was the first such shortfall in the program's history and has created uncertainty about funding levels in future years. Accordingly, we are monitoring the status of rural health care support for Funding Year 2017, which began on July 1, 2017. To date, USAC and the FCC have not announced funding levels or a cap for Funding Year 2017. As of the date of this report, we cannot predict what the funding levels will be, or the impact they will have on our rural health care customers. Concurrently, we have significant advocacy efforts underway to increase the funding levels for this program considering that the annual cap on funding has not been revised for nearly 20 years since the program's inception. As a business matter, we intend to factor this uncertainty into our future planning, while on a tactical basis we will continue to evaluate the potential impact of this funding on our revenues and accounts receivable beginning in the third quarter of 2017.

We believe that we will have sufficient cash on hand, cash provided by operations and availability under our 2017 Senior Credit Facility to service our debt and fund our operations, capital expenditures and other obligations over the next twelve months. However, our ability to make such an assessment is dependent upon our future financial performance, which is subject to future economic conditions and to financial, business, regulatory, competitive entry and many other factors, many of which are beyond our control and could impact us during the time period of this assessment. See Item 1A. Risk Factors in our Annual Report on Form 10-K for further information regarding these risks.

Contractual Obligations

Our contractual obligations as of December 31, 2016 are presented in the following table. The amounts presented reflect our refinancing transactions completed in March and April 2017. For purpose of this presentation, payment of the remaining principal balance of our 6.25% Notes of $10,044 at June 30, 2017 is assumed to occur at its maturity date in 2018 utilizing, in part, restricted cash designated for this purpose.

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(in thousands)	Total	2017	2018-2019	2020-2021	Thereafter
Long-term debt	$190,044	$ 1,650	$ 23,244	$ 25,050	$140,100
Interest on long-term debt	68,863	12,193	25,437	22,788	8,445
Capital leases	4,262	1,260	275	119	2,608
Operating leases	67,717	8,047	16,181	12,430	31,059
Unconditional purchase obligations	50,988	6,429	7,989	6,497	30,073
Total contractual cash obligations	$381,874	$29,579	$ 73,126	$ 66,884	$212,285

NON-GAAP FINANCIAL MEASURES

The Company provides certain non-GAAP financial information, including Adjusted EBITDA, Adjusted Free Cash Flow and Net Debt. Adjusted EBITDA eliminates the effects of period to period changes in costs that are not directly attributable to the underlying performance of the Company's business operations and is used by Management and the Company's Board of Directors to evaluate current operating financial performance, analyze and evaluate strategic and operational decisions and better evaluate comparability between periods. Adjusted Free Cash Flow is a non-GAAP liquidity measure used by Management and the Board of Directors to assess the Company's ability to generate cash and plan for future operating and capital actions. Adjusted EBITDA and Adjusted Free Cash Flow are common measures utilized by our peers (other telecommunications companies) and we believe they provide useful information to investors and analysts about the Company's operating results, financial condition and cash flows. Net Debt provides Management and the Board of Directors with a measure of the Company's current leverage position.

Adjusted EBITDA is defined as net income (loss) before interest, loss on extinguishment of debt, depreciation and amortization, gain or loss on asset purchases or disposals, income taxes, stock-based compensation, pension adjustments, net loss attributable to noncontrolling interest and expenses under the Company's long term cash incentive plan ("LTCI"). LTCI expenses are considered part of an interim compensation structure, which ended in 2016, to mitigate the dilutive impact of additional share issuances for executive compensation.

Management considers Adjusted Free Cash Flow a non-GAAP liquidity measure and is defined as Adjusted EBITDA, less recurring operating cash requirements which include capital expenditures, net of cash received for a fiber build for a carrier customer, less cash income taxes refunded or paid, cash interest paid, amortization of GCI capacity revenue, and cash payments associated with the purchase of the North Slope fiber network. Amortization of deferred revenue associated with our interconnection agreement with GCI is excluded from Adjusted Free Cash Flow because no cash was received by the Company in connection with this agreement. Amortization of all other deferred revenue, including that associated with other IRU capacity arrangements, is included in Adjusted Free Cash Flow because cash was received by the Company, typically at contract inception, and is being amortized to revenue over the term of the relevant agreement.

Amortization of deferred revenue included in our operating revenues for the three and six-month periods ended June 30, 2017 and 2016, were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
GCI capacity revenue	$ 516	$ 516	$1,027	$ 1,025
Other deferred capacity revenue	354	339	690	677
Total deferred capacity revenue	870	855	1,717	1,702
Other deferred revenue	705	789	1,541	1,514
Total	$ 1,575	$ 1,644	$3,258	$ 3,216

The Company does not provide reconciliations of guidance for Adjusted EBITDA to Net Income, and Adjusted Free Cash Flow to Net Cash Provided by Operating Activities, in reliance on the unreasonable efforts exception provided under Item 10(e)(1)(i)(B) of Regulation S-K. The Company does not forecast certain items required to develop the comparable GAAP financial measures. These items are charges and benefits for uncollectible accounts, certain other non-cash expenses, unusual items typically excluded from Adjusted EBITDA and Adjusted Free Cash Flow, and changes in operating assets and liabilities (generally the most significant of these items, representing cash outflows of $6.2 million in the six-month period ended June 30, 2017).

Adjusted EBITDA and Adjusted Free Cash Flow are not GAAP measures and should not be considered a substitute for Net Income, Net Cash Provided by Operating Activities, or Net Cash Provided or Used. Adjusted EBITDA as computed below is not consistent with the definition of Consolidated EBITDA referenced in our 2017 Senior Credit Facility, and other companies may not calculate Non-GAAP measures in the same manner we do.

The following tables provide the computation of Adjusted EBITDA and reconciliation to Net (Loss) Income, and the computation of Adjusted Free Cash Flow and reconciliation to Net Cash Provided by Operating Activities for the three and six-month periods ended June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net (loss) income	$ (2,830)	$ 283	$ (3,538)	$ 336
Add (subtract):				
Interest expense	3,913	3,852	7,758	7,721
Loss on extinguishment of debt	5,158	—	7,434	336
Interest income	(7)	(6)	(14)	(11)
Depreciation and amortization	9,028	8,640	17,931	17,160
Loss on disposal of assets, net	14	128	33	152
Income tax (benefit) expense	(632)	236	(1,464)	299
Stock-based compensation	(29)	642	581	1,447
Long-term cash incentives	—	194	—	405
Pension adjustment	—	20	—	41
Net loss attributable to noncontrolling interest	32	34	64	67
Adjusted EBITDA	$14,647	$14,023	$28,785	$27,953

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Reconciliation of Net Cash Provided by Operating Activities to Adjusted Free Cash Flow and Computation of Adjusted Free Cash Flow

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net cash provided by operating activities	$11,767	$ 8,705	$ 17,065	$ 18,886
Adjustments to reconcile net cash provided by operating activities to adjusted free cash flow:				
Capital expenditures	(5,374)	(8,487)	(10,522)	(13,662)
Payment for North Slope fiber network	—	(5,500)	—	(5,500)
Proceeds on sale of fiber to joint venture partner	—	—	—	2,650
Amortization of deferred capacity revenue	870	855	1,717	1,702
Amortization of GCI capacity revenue	(516)	(516)	(1,027)	(1,025)
Amortization of debt issuance costs and debt discount	(512)	(1,005)	(1,537)	(2,021)
Interest expense	3,913	3,852	7,758	7,721
Interest paid	(6,059)	(4,562)	(7,595)	(6,359)
Interest income	(7)	(6)	(14)	(11)
Income tax (benefit) expense	(632)	236	(1,464)	299
Income taxes (payable) receivable	—	(8)	(574)	722
Income taxes (paid) refunded, net	(2)	—	572	(577)
Deferred income tax benefit (expense)	634	(228)	1,466	(495)
Tax deficiencies from share-based payments	—	—	—	51
Charge for uncollectible accounts	(1,544)	(209)	(1,633)	(77)
Long-term cash incentives	—	194	—	405
Pension adjustment	—	20	—	41
Net loss attributable to noncontrolling interest	32	34	64	67
Other non-cash expense, net	(143)	(197)	(288)	(414)
Changes in operating assets and liabilities	269	1,780	6,225	1,077
Adjusted free cash flow	$ 2,696	$ (5,042)	$ 10,213	$ 3,480
Adjusted EBITDA	$14,647	$14,023	$ 28,785	$ 27,953
Less:				
Capital expenditures	(5,374)	(8,487)	(10,522)	(13,662)
Payment for North Slope fiber network	—	(5,500)	—	(5,500)
Proceeds on sale of fiber to joint venture partner	—	—	—	2,650
Amortization of deferred GCI capacity revenue	(516)	(516)	(1,027)	(1,025)
Income taxes (paid) refunded, net	(2)	—	572	(577)
Interest paid	(6,059)	(4,562)	(7,595)	(6,359)
Adjusted free cash flow	$ 2,696	$ (5,042)	$ 10,213	$ 3,480

OUTLOOK

We expect to see continued strength in business and wholesale revenues, led by broadband revenue and managed IT services. These revenue increases are driven by continued demand for broadband as businesses migrate their IT infrastructure to the cloud, expansion into managed IT services and continued gain in market share. We expect margins will strengthen through the course of the year. Strategically, we continue to evaluate opportunities to advance our position as the premier cloud enabler for businesses.

We expect variable growth in equipment sales, as this revenue stream is impacted by non-recurring transactions. We expect access revenues to continue to decline as voice traffic experiences decline with long distance carriers. As the only price cap carrier in Alaska, we will receive approximately $19.7 million annually in high cost support for the next nine years under the CAF II order issued in the fourth quarter of 2016. This is the same amount we received under the CAF I high cost frozen support.

Our financial guidance for the full year 2017 is as follows:

- Total revenue of $229 million to $235 million.
- Adjusted EBITDA of $59 million to $61 million.
- Capital spending of $35 million to $38 million.
- Adjusted free cash flow of $4 million to $7 million.

As discussed in “Non-GAAP Financial Measures,” the Company does not provide reconciliations of guidance for Adjusted EBITDA to Net Income, and Adjusted Free Cash Flow to Net Cash Provided by Operating Activities.

LEGAL

We are involved in various claims, legal actions, personnel matters and regulatory proceedings arising in the ordinary course of business and as of June 30, 2017, we have recorded litigation accruals of $0.7 million against certain of those claims and legal actions. Estimates involved in developing these litigation accruals could change as these claims, legal actions and regulatory proceedings progress. See also Part II, Item 1. Legal Proceedings.

EMPLOYEES

As of June 30, 2017, we employed 619 regular full-time employees, 8 regular part-time employees and 4 temporary employees, compared with 629, 9 and 4, respectively at December 31, 2016. Approximately 56% of our employees are represented by the IBEW. Our Master Collective Bargaining Agreement (“CBA”) with the IBEW governs the terms and conditions of employment for all IBEW represented employees working for us in the state of Alaska and expired on December 31, 2016. As of the date of this report we continue to operate under the prior agreement. Negotiations for a new agreement are continuing, and Management considers employee relations to be generally good.

CRITICAL ACCOUNTING POLICIES AND ACCOUNTING ESTIMATES

We have identified certain policies and estimates as critical to our business operations and the understanding of our past or present results of operations. For additional discussion on the application of these significant accounting policies, see “Critical Accounting Policies and Estimates” in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2016. These policies and estimates are considered critical because they had a material impact, or have the potential to have a material impact, on our financial statements and because they require significant judgments, assumptions or estimates.

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Among the significant estimates affecting the financial statements are those related to the realizable value of accounts receivable and long-lived assets, the value of derivative instruments, deferred capacity revenue, legal contingencies, stock-based compensation and income taxes. As future events and their effects cannot be determined with precision, actual results may differ significantly from those estimates. Changes in those estimates will be reflected in the financial statements of future periods.

Recently Adopted Accounting Pronouncements

In the first quarter of 2017, the Company adopted ASU No. 2016-09, “ *Compensation – Stock Compensation (Topic 718), Improvements to Employee Share-Based Payment Accounting* ” (“ASU 2016-09”). The amendments in ASU 2016-09 simplify several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The relevant provisions of ASU 2016-09 and the effect of adoption on the Company’s financial statements and related disclosures are summarized as follows: (i) The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. Excess tax benefits should be recognized regardless of whether the benefit reduces taxes payable in the current period. Excess tax benefits and tax deficiencies should be recognized as income tax expense or benefit in the income statement. The Company adopted these provisions on a modified retrospective basis. Excess tax benefits and tax deficiencies are included in the income tax provision beginning in the first quarter of 2017. A cumulative-effect adjustment was recorded in the first quarter of 2017 to reclassify $1,441 from additional paid in capital to retained earnings for excess tax benefits and deficiencies recorded to additional paid in capital prior to 2017. (ii) Excess tax benefits and tax deficiencies should be classified as an operating activity in the statement of cash flows. The Company adopted this provision on a retrospective basis. Tax deficiencies from share-based payments of $51 classified as a financing activity on the statement of cash flows in the six-month period of 2016 were reclassified to operating activities. See the condensed consolidated statement of cash flows. (iii) An entity may make an accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. Prior to 2017, the Company’s stock-based compensation expense reflected an estimate of the number of awards that were expected to vest, including an estimate of forfeitures. Effective in the first quarter 2017, the Company elected to account for forfeitures when they occur.

This provision was adopted on a modified retrospective basis, and a cumulative-effect adjustment was recorded in the first quarter of 2017 to reclassify $163 from additional paid in capital to retained earnings for the effect of this accounting change on periods prior to 2017. Retained earnings was charged $96 net of the income tax effect of $67. (iv) The threshold to qualify for equity classification permits withholding up to the maximum statutory tax rates. The Company has historically withheld taxes at the minimum statutory rate. Adoption of this provision is not expected to have a material effect on the Company's financial statements. (vii) Cash paid by an employer when directly withholding shares for tax withholding purposes should be classified as a financing activity. This classification is consistent with the Company's historical practice. See the consolidated statement of stockholders' equity, Note 9 " *Stock Incentive Plans* " and Note 10 " *Income Taxes* " for additional information.

In August 2016, the Financial Accounting Standards Board ("FASB") issued ASU No. 2016-15, " *Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments* " ("ASU 2016-15"). The amendments in this update address eight specific cash flow classification issues for which current GAAP either is unclear or does not include specific guidance, and for which there exists diversity in practice: Debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, and interim periods within those years, and early adoption is permitted. The Company adopted ASU 2016-15 effective in the first quarter of 2017 on a modified retrospective basis as required by the standard. The Company's cash flow classifications for the eight issues addressed in ASU 2016-15, where applicable, were generally consistent with the new guidance. Accordingly, adoption of ASU 2016-15 did not have a material effect on the Company's financial statements.

In November 2016, the FASB issued ASU No. 2016-18, " *Statement of Cash Flows (Topic 230), Restricted Cash* " ("ASU 2016-18"). ASU 2016-18 requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. ASU 2016-18 is effective for fiscal years beginning after December 15, 2017, and was adopted by the Company effective in the first quarter of 2017 as permitted. The Company adopted ASU 2016-18 on a retrospective basis as required by the standard. See Note 13 " *Supplemental Cash Flow Information* " for additional information.

Accounting Pronouncements Issued Not Yet Adopted

In May 2014, the FASB issued ASU No. 2014-09, " *Revenue from Contracts with Customers (Topic 606)* " ("ASU 2014-09"). The amendments in ASU 2014-09 and subsequent updates require that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Adoption of the new standard is to be applied on a full retrospective basis or modified retrospective basis. The Company's assessment of ASU 2014-09 and subsequent updates is nearing completion and is currently expected to be completed during the third quarter of 2017. This assessment includes determining the effect of the new standard on the Company's financial statements, accounting systems, business processes, and internal controls. Based on its assessment to date, the Company does not currently expect adoption to have a material effect on its consolidated revenues. It is currently expected that adoption of the new standard will result in the deferral of certain contract fulfillment and other costs, including certain sales commissions, connection costs and modems, which are currently expensed as incurred. Such deferred costs will be amortized over the period that the associated revenue is recognized. The Company is in the early stages of implementation, which will require changes to the Company's accounting systems, business processes and internal controls. The Company will adopt ASU 2014-09 effective January 1, 2018 and has not yet selected an adoption method.

In February 2016, the FASB issued ASU No. 2016-02, " *Leases (Topic 842)* " ("ASU 2016-02"). The primary change in GAAP addressed by ASU 2016-02 is the requirement for a lessee to recognize on the balance sheet a liability to make lease payments ("lease liability") and a right-of-use asset representing its right to use the underlying asset for the lease term. The accounting applied by a lessor is largely unchanged from that applied under previous GAAP. ASU 2016-02 also requires qualitative and quantitative disclosures to enable users of the financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those years. Lessees must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The Company is evaluating the effect that ASU 2016-02 will have on its consolidated financial statements and related disclosures.

In March 2017, the FASB issued ASU No. 2017-07, " *Compensation – Retirement Benefits (Topic 715)* " ("ASU 2017-07"). The amendments in ASU 2017-07 require that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees. The other components of net benefit costs are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. If a separate line item or items are used to present the other components of net benefit costs, that line item or items must be appropriately described. If a separate line item or items are not used, the line item or items used in the income statement to present the other components of net benefit cost must be disclosed. ASU 2017-07 also requires that only the service cost component is eligible for capitalization when applicable. ASU 2017-07 is effective for fiscal years beginning after December 15, 2017. The Company does not currently expect that adoption of ASU 2017-07 will have a material effect on its consolidated financial statements and related disclosures.

In May 2017, the FASB issued ASU No. 2017-09, " *Compensation – Stock Compensation (Topic 718)* " ("ASU 2017-09"). The amendments in ASU 2017-09 are intended to provide clarity, and reduce diversity in practice and the cost and complexity of applying the guidance in Topic 718. The primary provision of ASU 2017-09 is to provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting. An entity should account for the effects of a change as a modification unless all the following conditions are met: (i) The fair value of the modified award is the same as the fair value of the original award immediately before the original award is modified. If the modification does not affect any of the inputs to the valuation technique that the entity uses to value the award, the entity is not required to estimate the value immediately before and after the modification. (ii) The vesting conditions of the modified award are the same as the vesting conditions of the original award immediately before the original award is modified. (iii) The classification of the modified award as an equity instrument or a liability instrument is the same as the classification of the original award immediately before the original award is modified. ASU 2017-09 is effective for fiscal years beginning after December 15, 2017. Early adoption is permitted, including adoption in any interim period. The amendments in this update should be applied prospectively to awards modified on or after the adoption date. The effect of the adoption of ASU 2017-09 on the Company's financial statements and related disclosures will be dependent on the frequency and types of changes made to its share-based payment awards.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our primary exposure to market risk is associated with changes in interest rates. The interest rates and cash interest payments were substantially fixed on approximately $100.9 million, or 53%, of our total borrowings of $190.9 million as of June 30, 2017. Our 6.25% Notes have a fixed coupon rate. The $120.0 million Term A-1 Facility of our 2017 Senior Credit Facility bears interest of LIBOR plus 5.0% with a LIBOR floor of 1.0% and the $60.0 million Term A-2 Facility bears interest of LIBOR plus 7.0% with a LIBOR floor of 1.0% as of June 30, 2017.

We manage a portion of our exposure to fluctuations in LIBOR and the resulting impact on interest expense and cash interest payments on our 2017 Senior Credit Facility through the utilization of pay-fixed, receive-floating interest rate swaps designated as a cash flow hedge. As of June 30, 2017, interest expense on $90.0 million, or approximately 50%, of the amount outstanding under the 2017 Senior Senior Credit Facility was hedged. A hypothetical 100 basis point increase in LIBOR over the floor of 1.0% during the next twelve months would result in an approximately $0.9 million increase in interest expense and cash interest payments associated with the unhedged portion of the 2017 Senior Credit Facility. Under the terms of the 2017 Senior Credit Facility, the Company is required to hedge the variable rate interest payments on a minimum of $90.0 million principal borrowed under the Agreement for a weighted average life of at least two years.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this Quarterly Report on Form 10-Q, we carried out an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer and our Principal Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934. Based on the evaluation, our Chief Executive Officer and our Principal Financial Officer have concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective to ensure that the information required to be disclosed by us in the reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required financial disclosure.

Changes in Internal Control Over Financial Reporting

Under the supervision and with the participation of our management, including our Chief Executive Officer and our Principal Financial Officer, we have evaluated any changes in our internal control over financial reporting that occurred during the second quarter of 2017 and have concluded that there were no changes to our internal control over financial reporting during the second quarter of 2017 that materially affect, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are involved in various claims, legal actions, personnel matters and regulatory proceedings arising in the ordinary course of business. As of June 30, 2017, we have recorded litigation accruals of $0.7 million against certain current claims and legal actions. Other than as described above and as disclosed previously in Item 3. Legal Proceedings in our Annual Report on Form 10-K for the year ended December 31, 2016, we believe that the disposition of these matters will not have a material adverse effect on our consolidated financial position, results of operations or cash flows.

ITEM 1A. RISK FACTORS

There have been no material changes to the Company's risk factors as previously disclosed in Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2016.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Working Capital Restrictions and Other Limitations on the Payment of Dividends

Our 2017 Senior Credit Facility contains a number of restrictive covenants and events of default, including covenants limiting capital expenditures, incurrence of debt and the payment of dividends. The 2017 Senior Credit Facility also requires that we maintain certain financial ratios.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit Number	Exhibit	Where Located
10.1	Compensation Letter from Alaska Communications Systems Group, Inc. to Randy Ritter dated April 3, 2017.	Exhibit 10.1 to Form 8-K (filed April 17, 2017
10.2	Compensation Letter from Alaska Communications Systems Group, Inc. to William Bishop dated April 3, 2017.	Exhibit 10.2 to Form 8-K (filed April 17, 2017)
31.1	Certification of Anand Vadapalli, President and Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed herewith
31.2	Certification of Laurie Butcher, Senior Vice President of Finance, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed herewith
32.1	Certification of Anand Vadapalli, President and Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	Furnished herewith
32.2	Certification of Laurie Butcher, Senior Vice President of Finance, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	Furnished herewith
101.INS	XBRL Instance Document	Filed herewith
101.SCH	XBRL Taxonomy Extension Schema Document	Filed herewith
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document	Filed herewith
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document	Filed herewith
101.LAB	XBRL Taxonomy Extension Label Linkbase Document	Filed herewith
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document	Filed herewith

SIGNATURES

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.

	ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Date: August 4, 2017	/s/ Anand Vadapalli
	Anand Vadapalli President and Chief Executive Officer (Principal Executive Officer)
Date: August 4, 2017	/s/ Laurie Butcher
	Laurie Butcher Senior Vice President of Finance (Principal Financial and Accounting Officer)

Exhibit 31.1

Sarbanes-Oxley Section 302(a) Certification

I, Anand Vadapalli, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Alaska Communications Systems Group, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:
   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 4, 2017

/s/ Anand Vadapalli

Anand Vadapalli
President and Chief Executive Officer
Alaska Communications Systems Group, Inc.

Exhibit 31.2

Sarbanes-Oxley Section 302(a) Certification

I, Laurie Butcher, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Alaska Communications Systems Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: August 4, 2017

/s/ Laurie Butcher

Laurie Butcher
Senior Vice President of Finance
Alaska Communications Systems Group, Inc.

Exhibit 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Alaska Communications Systems Group, Inc. (the "Company") on Form 10-Q for the period ending June 30, 2017 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Anand Vadapalli, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 4, 2017

/s/ Anand Vadapalli

Anand Vadapalli
President and Chief Executive Officer
Alaska Communications Systems Group, Inc.

Exhibit 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Alaska Communications Systems Group, Inc. (the "Company") on Form 10-Q for the period ending June 30, 2017 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Laurie Butcher, Senior Vice President of Finance of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 4, 2017

/s/ Laurie Butcher
Laurie Butcher
Senior Vice President of Finance
Alaska Communications Systems Group, Inc.