ALLTEL CORP
Form 10-Q
May 09, 2006

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

FORM 10-Q

[x] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2006
OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 1-4996

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

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

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

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

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

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

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

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

Number of common shares outstanding as of April 28, 2006: 389,107,443

The Exhibit Index is located on page 51.

ALLTEL CORPORATION
FORM 10-Q
TABLE OF CONTENTS

Page No.

PART I - FINANCIAL INFORMATION

Item 1.	Financial Statements	2
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	21
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	48
Item 4.	Controls and Procedures	49

PART II - OTHER INFORMATION

Item 1.	Legal Proceedings	*
Item 1A.	Risk Factors	49
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	49
Item 3.	Defaults Upon Senior Securities	*
Item 4.	Submission of Matters to a Vote of Security Holders	*
Item 5.	Other Information	*
Item 6.	Exhibits	49

* No reportable information under this item.

Forward-Looking Statements

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

Actual future events and results may differ materially from those expressed in these forward-looking statements as a result of a number of important factors. Representative examples of these factors include (without limitation) adverse changes in economic conditions in the markets served by Alltel; the extent, timing, and overall effects of competition in the communications business; material changes in the communications industry generally that could adversely affect vendor relationships with equipment and network suppliers and customer relationships with wholesale customers; changes in communications technology; the risks associated with pending acquisitions and dispositions, including the pending acquisition of Midwest Wireless and the pending dispositions of the Bolivan operations and the wireline business; the risks associated with the integration of acquired businesses; the uncertainties related to any

discussions or negotiations regarding the sale of any remaining international assets; adverse changes in the terms and conditions of the wireless roaming agreements of Alltel; the potential for adverse changes in the ratings given to Alltel's debt securities by nationally accredited ratings organizations; the availability and cost of financing in the corporate credit and debt markets necessary to consummate the disposition of the wireline business; the uncertainties related to Alltel's strategic investments; the effects of litigation; and the effects of federal and state legislation, rules, and regulations governing the communications industry.

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

ALLTEL CORPORATION
FORM 10-Q
PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(Dollars in millions, except per share amounts)		March 31,		December 31,
Assets		2006		2005
Current Assets:				
Cash and short-term investments	$	886.5	$	989.2
Accounts receivable (less allowance for doubtful				
accounts of $70.0 and $84.7, respectively)		1,015.0		1,077.2
Inventories		193.9		232.6
Prepaid expenses and other		100.5		115.2
Assets held for sale		2,027.1		1,951.2
Total current assets		4,223.0		4,365.4
Investments		374.8		358.4
Goodwill		8,981.7		8,677.3
Other intangibles		2,207.6		2,179.1
Property, Plant and Equipment:				
Land		310.1		298.6
Building and improvements		1,237.7		1,211.4
Wireline		6,988.3		6,942.0
Wireless		6,971.0		6,852.6
Information processing		1,223.3		1,187.2
Other		540.0		530.3
Under construction		412.2		475.4
Total property, plant and equipment		17,682.6		17,497.5
Less accumulated depreciation		9,759.6		9,433.9
Net property, plant and equipment		7,923.0		8,063.6
Other assets		336.0		369.3
Total Assets	$	24,046.1	$	24,013.1
Liabilities and Shareholders' Equity				
Current Liabilities:				
Current maturities of long-term debt	$	205.1	$	205.1
Accounts payable		517.2		645.4
Advance payments and customer deposits		239.7		240.5
Accrued taxes		233.7		174.7
Accrued dividends		149.5		147.8
Accrued interest		79.2		102.5
Current deferred income taxes		340.1		339.0
Other current liabilities		262.7		255.4
Liabilities related to assets held for sale		301.7		294.4
Total current liabilities		2,328.9		2,404.8
Long-term debt		5,661.9		5,782.9
Deferred income taxes		1,868.5		1,860.9
Other liabilities		891.0		949.0
Shareholders' Equity:				

Preferred stock, Series C, $2.06, no par value, 10,702 and 11,122				
shares issued and outstanding, respectively		0.3		0.3
Common stock, par value $1 per share, 1.0 billion shares authorized,				
388,857,700 and 383,605,936 shares issued and outstanding, respectively		388.9		383.6
Additional paid-in capital		5,440.8		5,339.3
Unrealized holding gain on investments		30.3		22.3
Foreign currency translation adjustment		14.8		(2.8)
Retained earnings		7,420.7		7,272.8
Total shareholders' equity		13,295.8		13,015.5
Total Liabilities and Shareholders' Equity	$	24,046.1	$	24,013.1

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

CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

(Millions, except per share amounts)	Three Months Ended March 31, 2006		2005
Revenues and sales:			
Service revenues	$	2,247.7	$ 1,898.3
Product sales		292.0	227.7
Total revenues and sales		2,539.7	2,126.0
Costs and expenses:			
Cost of services (excluding depreciation of $251.3 and $241.9, respectively, included below)		731.7	626.3
Cost of products sold		355.8	281.8
Selling, general, administrative and other		499.0	407.4
Depreciation and amortization		404.5	341.2
Integration expenses and other charges		19.5	-
Total costs and expense		2,010.5	1,656.7
Operating income		529.2	469.3
Equity earnings in unconsolidated partnerships		12.9	10.7
Minority interest in consolidated partnerships		(13.9)	(18.3)
Other income, net		11.9	120.7
Interest expense		(89.0)	(86.7)
Income from continuing operations before income taxes		451.1	495.7
Income taxes		171.5	182.7
Income from continuing operations		279.6	313.0
Discontinued operations (net of income taxes of $28.8)		17.8	-
Net income		297.4	313.0
Preferred dividends		-	-
Net income applicable to common shares	$	297.4	$ 313.0
Earnings per share:			
Basic:			
Income from continuing operations		$.72	$1.04
Income from discontinued operations		.05	-
Net income		$.77	$1.04
Diluted:			
Income from continuing operations		$.72	$1.03
Income from discontinued operations		.05	-
Net income		$.77	$1.03

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

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(Millions)	Three Months Ended March 31, 2006	2005
Cash Provided from Operations:		
Net income	$ 297.4	$ 313.0
Adjustments to reconcile net income to net cash provided from operations:		
Income from discontinued operations	(17.8)	-
Depreciation and amortization	404.5	341.2
Provision for doubtful accounts	53.7	40.9
Change in deferred income taxes	21.5	(19.1)
Other, net	11.2	13.6
Changes in operating assets and liabilities, net of effects of acquisitions and dispositions:		
Accounts receivable	9.3	16.5
Inventories	38.7	8.7
Accounts payable	(120.5)	17.6
Other current liabilities	33.6	86.6
Other, net	1.5	(40.3)
Net cash provided from operations	733.1	778.7
Cash Flows from Investing Activities:		
Additions to property, plant and equipment	(213.7)	(254.9)
Additions to capitalized software development costs	(7.2)	(11.1)
Additions to investments	-	(0.7)
Purchases of property, net of cash acquired	(458.9)	(51.8)
Proceeds from the return on investments	8.9	7.8
Other, net	(0.9)	3.0
Net cash used in investing activities	(671.8)	(307.7)
Cash Flows from Financing Activities:		
Dividends on common and preferred stock	(147.8)	(105.7)
Repayments of long-term debt	(0.7)	(1.9)
Conversion of convertible notes	(59.8)	-
Distributions to minority investors	(11.8)	(12.7)
Excess tax benefits from stock option exercises	1.9	-
Long-term debt issued	-	50.0
Common stock issued	54.9	2.8
Net cash used in financing activities	(163.3)	(67.5)
Cash Flows from Discontinued Operations:		
Cash provided from operating activities	85.6	-
Cash provided from investing activities	4.9	-
Cash used in financing activities	(91.7)	-
Net cash used in discontinued operations	(1.2)	-
Effect of exchange rate changes on cash and short-term investments	0.5	-
	(102.7)	403.5

Increase (decrease) in cash and short-term investments				
Cash and Short-term Investments:				
Beginning of the period		989.2		484.9
End of the period	$	886.5	$	888.4

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

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY (UNAUDITED)

(Millions)	Preferred Stock	Common Stock	Additional Paid-In Capital	Unrealized Holding Gain On Investments	Foreign Currency Translation Adjustment	Retained Earnings	Total
Balance at December 31, 2005	$ 0.3	$ 383.6	$ 5,339.3	$ 22.3	$ (2.8)	$ 7,272.8	$ 13,015.5
Net income	-	-	-	-	-	297.4	297.4
Other comprehensive loss, net of tax: (See Note 11)							
Unrealized holding losses on investments,							
net of reclassification adjustments	-	-	-	8.0	-	-	8.0
Foreign currency translation adjustment	-	-	-	-	17.6	-	17.6
Comprehensive income	-	-	-	8.0	17.6	297.4	323.0
Employee plans, net	-	1.5	53.3	-	-	-	54.8
Restricted stock	-	0.3	-	-	-	-	0.3
Amortization of unearned compensation (See Note 2)	-	-	9.0	-	-	-	9.0
Tax benefit for non-qualified stock options	-	-	2.5	-	-	-	2.5
Conversion of convertible notes (See Note 3)	-	3.5	36.7	-	-	-	40.2
Dividends:							
Common - $.385 per share	-	-	-	-	-	(149.5)	(149.5)
Preferred	-	-	-	-	-	-	-
Balance at March 31, 2006	$ 0.3	$ 388.9	$ 5,440.8	$ 30.3	$ 14.8	$ 7,420.7	$ 13,295.8

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

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

1. General:

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

2. Accounting Changes:

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

Changes in Accounting Estimates - Effective January 1, 2006, the Company prospectively reduced depreciation rates for its incumbent local exchange carrier operations in Pennsylvania to reflect the results of a study of depreciable lives completed by Alltel in January 2006. The depreciable lives were lengthened to reflect the estimated remaining useful lives of the wireline plant based on the Company's expected future network utilization and capital expenditure levels required to provide service to its customers. The effect of this change resulted in a decrease in depreciation expense of $4.4 million and an increase in net income of $2.7 million or $.01 per share for the three months ended March 31, 2006.

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

previously calculated by Alltel in developing its pro forma disclosures in accordance with the provisions of SFAS No. 123. Operating results for prior periods have not been restated.

Upon adoption of SFAS No. 123(R), Alltel elected to continue to value its share-based payment transactions using a Black-Scholes valuation model, which was previously used by the Company for purposes of preparing the pro forma disclosures under SFAS No. 123. Under the provisions of SFAS No. 123(R), stock-based compensation expense recognized during the period is based on the portion of the share-based payment awards that is ultimately expected to vest. Accordingly, stock-based compensation expense recognized in the first quarter of 2006 has been reduced for estimated forfeitures. SFAS No. 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Pre-vesting forfeitures were estimated to be 5.1 percent based on Alltel's historical experience. In the Company's pro forma information required under SFAS No. 123, Alltel accounted for forfeitures as they occurred. Compensation expense for stock option awards granted after January 1, 2006 will be expensed using a straight-line single option method, which is the same attribution method that was used by Alltel for purposes of its pro forma disclosures under SFAS No. 123.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

2. Accounting Changes, Continued:

Stock-based compensation expense recognized for the three months ended March 31, 2006 was as follows:

(Millions, except per share amounts)		
Compensation expense related to stock options issued by Alltel	$	4.8
Compensation expense related to stock options converted to Alltel stock options in connection with the acquisition of Western Wireless Corporation		0.5
Compensation expense related to restricted stock awards		3.7
Compensation expense before income taxes		9.0
Income tax benefit		(2.8)
Compensation expense, net of tax	$	6.2
Earnings per share effects of compensation expense, net of tax		
Basic earnings per share		$.02
Diluted earnings per share		$.02

Comparatively, stock-based compensation expense recognized for the three months ended March 31, 2005 was $1.6 million consisting solely of expense related to restricted stock awards. Stock-based compensation expense is included in selling, general, administrative and other expenses within the Company's unaudited interim consolidated statements of income. For the three months ended March 31, 2006, stock-based compensation expense allocated to business segments totaled $7.3 million to the wireless segment, $0.9 million to the wireline segment and $0.8 million to corporate expenses. As presented in the table above, the effect of adopting SFAS No. 123(R) consisted of compensation expense for stock options issued by Alltel and resulted in a pretax charge of $4.8 million, which decreased net income $3.6 million or $.01 per share for the three months ended March 31, 2006.

Prior to adopting the provisions of SFAS No. 123(R), the Company recorded estimated compensation cost for employee stock options based upon the intrinsic value of the option on the date of grant consistent with the recognition and measurement principles of APB Opinion No. 25. Because Alltel had established the exercise price of its employee stock options based on the fair market value of the Company's stock at the date of grant, the stock options had no intrinsic value upon grant, and accordingly, Alltel did not record compensation expense for employee stock options prior to adopting SFAS No. 123(R). The following table illustrates the effects on net income and earnings per share had the Company applied the fair value recognition provisions of SFAS No. 123 to its stock-based employee compensation plans for the three months ended March 31, 2005:

(Millions, except per share amounts)			
Net income as reported		$	313.0
Add stock-based compensation expense included in net income, net of related tax effects			1.0
Deduct stock-based employee compensation expense determined under fair value method for all awards, net of related tax effects			(6.6)
Pro forma net income		$	307.4
Basic earnings per share:	As reported		$1.04
	Pro forma		$1.02
Diluted earnings per share:	As reported		$1.03
	Pro forma		$1.01

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

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

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

3. Acquisitions:

On March 16, 2006, Alltel purchased from Palmetto MobileNet, L.P. for $456.3 million in cash the remaining ownership interests in ten wireless partnerships that cover approximately 2.0 million potential customers ("POPs") in North and South Carolina. Prior to this transaction, Alltel owned a 50 percent interest in each of the ten wireless partnerships. During March 2006, Alltel completed a preliminary purchase price allocation for this transaction based upon a fair value analysis of the net tangible and identifiable intangible assets acquired and assigned the excess of the aggregate purchase price over the fair market value of the tangible net assets acquired of $399.1 million to customer list ($38.0 million), cellular licenses ($40.0 million) and goodwill ($321.1 million). The customer list recorded in connection with this transaction is being amortized over a five-year period using the sum-of-the-years digits method. The cellular licenses are classified as indefinite-lived intangible assets and are not subject to amortization. The Company expects the goodwill and other identified intangible assets recorded in connection with this transaction to be deductible for income tax purposes. Given the close proximity to quarter end that this transaction was completed, the values of certain assets and liabilities have been based on preliminary valuations and are subject to adjustment as additional information is obtained. Accordingly, the purchase price allocation is subject to adjustment based upon completion of third party valuations and the final determination of fair values.

During the first quarter of 2006, Alltel also acquired the remaining ownership interest in a wireless property in Wisconsin in which the Company owned a majority interest. In connection with this acquisition, the Company paid $2.6 million in cash and assigned the excess of the aggregate purchase price over the fair market value of the tangible net assets acquired of $1.0 million to goodwill.

For both of the 2006 acquisitions, Alltel paid a premium (i.e. goodwill) over the fair value of the net tangible and identifiable intangible assets acquired in order to gain full control over the day-to-day operations of the wireless markets in North Carolina, South Carolina and Wisconsin. In addition, Alltel will no longer incur certain general and administrative expenses, such as audit and legal fees, attributable to managing its relationship with the other partners.

On August 1, 2005, Alltel and Western Wireless Corporation ("Western Wireless") completed the merger of Western Wireless into a wholly-owned subsidiary of Alltel. As a result of the merger, Alltel added approximately 1.3 million domestic wireless customers, adding wireless operations in nine new states, including California, Idaho, Minnesota, Montana, Nevada, North Dakota, South Dakota, Utah and Wyoming, and expanding its wireless operations in Arizona, Colorado, New Mexico and Texas. In the merger, each share of Western Wireless common stock was exchanged for 0.535 shares of Alltel common stock and $9.25 in cash unless the shareholder made an all-cash election, in which case the shareholder received $40 in cash. Western Wireless shareholders making an all-stock election were subject to proration and received approximately 0.539 shares of Alltel common stock and $9.18 in cash. In the aggregate, Alltel issued approximately 54.3 million shares of stock valued at $3,430.4 million and paid approximately $933.4 million in cash. Through its wholly-owned subsidiary that merged with Western Wireless, Alltel also assumed debt of approximately $2.1 billion and acquired cash of $12.6 million. On the date of closing, Alltel repaid approximately $1.3 billion of term loans representing all borrowings outstanding under Western Wireless' credit facility that, as a result of a change in control, became due and payable immediately upon the closing of the merger. On August 1, 2005, Alltel also announced a tender offer to purchase all of the issued and outstanding 9.25 percent senior notes due July 15, 2013 of Western Wireless, representing an aggregate principal amount of $600.0 million, as well as a related consent solicitation to amend the indenture governing the senior notes. During the third quarter of 2005, Alltel repurchased all $600.0 million of the senior notes.

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

During the first quarter of 2006, Alltel adjusted the purchase price allocation related to the Western Wireless acquisition to reflect the resolution of a pre-acquisition contingency concerning universal service fund support that Western Wireless had received as an Eligible Telecommunications Carrier (“ETC”) in the State of Kansas and to adjust certain income tax valuation allowances related to the international operations. The effects of these adjustments resulted in a reduction in goodwill of $21.5 million.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

3. Acquisitions, Continued:

During the first quarter of 2006, Alltel substantially completed the integration of the domestic operations acquired from Western Wireless. In connection with this integration, the Company incurred integration expenses, principally consisting of costs for branding, signage, retail store redesigns and computer system conversions. (See Note 8 for a discussion of integration expenses recorded by Alltel during the first quarter of 2006). Employee termination benefits of $23.8 million, including involuntary severance and related benefits to be provided to 337 former Western Wireless employees, and employee retention bonuses of $7.4 million payable to approximately 1,150 former Western Wireless employees were recorded during 2005. These employee benefit costs were recognized in accordance with Emerging Issues Task Force Issue No. 95-3, "Recognition of Liabilities in Connection with a Purchase Business Combination", as liabilities assumed in the business combination. As of March 31, 2006, Alltel had paid $20.9 million in employee termination and retention benefits, and 292 of the scheduled employee terminations had been completed.

As a condition of receiving approval for the merger from the U.S. Department of Justice ("DOJ") and Federal Communications Commission ("FCC"), Alltel agreed to divest certain wireless operations of Western Wireless in 16 markets in Arkansas, Kansas and Nebraska, as well as the "Cellular One" brand. On December 19, 2005, Alltel completed an exchange of wireless properties with United States Cellular Corporation ("U.S. Cellular") that included a substantial portion of the divestiture requirements related to the Company's merger with Western Wireless. During December 2005, Alltel completed the sale of the Cellular One brand to Dobson Cellular Systems, Inc. and on March 24, 2006, Alltel completed the sale of the remaining market in Arkansas to Cingular Wireless LLC ("Cingular"). During 2005, Alltel completed the sale of Western Wireless' international operations in Georgia, Ghana and Ireland. As discussed in Note 15, on April 28, 2006, Alltel completed sales of the Western Wireless international operations in Austria and Haiti, and Alltel has a pending definitive agreement to sell the international operations in Bolivia. Alltel is also actively pursuing the disposition of the remaining international operations acquired from Western Wireless and expects to complete the disposition of the remaining operations during the second quarter of 2006. Accordingly, the acquired international operations and interests of Western Wireless and the domestic markets required to be divested by Alltel have been classified as assets held for sale and discontinued operations in the accompanying unaudited interim consolidated financial statements. (See Note 10).

Under terms of the agreement with U.S. Cellular, Alltel acquired two rural markets in Idaho that are adjacent to the Company's existing operations and received $48.2 million in cash in exchange for 15 rural markets in Kansas and Nebraska formerly owned by Western Wireless. During the first quarter of 2006, Alltel completed the purchase price allocation for this exchange based upon a fair value analysis of the tangible and identifiable intangible assets acquired and the wireless property interests relinquished. The excess of the aggregate purchase price over the fair market value of the tangible net assets acquired of $100.1 million was assigned to customer list, cellular licenses and goodwill. The customer list recorded in connection with this transaction is being amortized over a five-year period using the sum-of-the-years digits method. The cellular licenses are classified as indefinite-lived intangible assets and are not subject to amortization. The finalization of the purchase price allocation resulted in a reduction to the preliminary values assigned to cellular licenses ($1.5 million), customer list ($0.5 million), and acquired net tangible assets ($1.8 million) with an increase to goodwill
($3.8 million) compared to the corresponding values that had been previously recorded in the Company's consolidated balance sheet as of December 31, 2005.

The following unaudited pro forma consolidated results of operations of the Company for the three months ended March 31, 2005 assume that the acquisition of wireless properties from Western Wireless occurred as of January 1, 2005:

(Millions, except per share amounts)	
Revenues and sales	$2,366.5
Income from continuing operations	$318.0
Combined earnings per share from continuing operations:	
Basic earnings per share	$.83
Diluted earning per share	$.82
Net income	$344.3
Combined earnings per share:	
Basic earnings per share	$.90
Diluted earning per share	$.89

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

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

4. Goodwill and Other Intangible Assets:
Goodwill represents the excess of cost over the fair value of net identifiable tangible and intangible assets acquired through various business combinations. The Company has acquired identifiable intangible assets through its acquisitions of interests in various wireless and wireline properties. The cost of acquired entities at the date of the acquisition is allocated to identifiable assets, and the excess of the total purchase price over the amounts assigned to identifiable assets is recorded as goodwill. As of January 1, 2006, Alltel completed the annual impairment reviews of its goodwill and other indefinite-lived intangible assets and determined that no write-down in the carrying value of these assets was required. The changes in the carrying amount of goodwill by business segment for the three months ended March 31, 2006 were as follows:

(Millions)	Wireless	Wireline	Communications Support Services	Total
Balance at December 31, 2005	$ 7,427.4	$ 1,247.6	$ 2.3	$ 8,677.3
Acquired during the period	322.1	-	-	322.1
Other adjustments	(17.7)	-	-	(17.7)
Balance at March 31, 2006	$ 7,731.8	$ 1,247.6	$ 2.3	$ 8,981.7

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

(Millions)	March 31, 2006	December 31, 2005
Cellular licenses	$ 1,430.8	$ 1,392.3
Personal Communications Services licenses	79.1	79.1
Franchise rights - wireline	265.0	265.0
	$ 1,774.9	$ 1,736.4

Intangible assets subject to amortization were as follows:

March 31, 2006

(Millions)	Gross Cost	Accumulated Amortization	Net Carrying Value
Customer lists	$ 797.9	$ (375.9)	$ 422.0
Franchise rights	22.5	(16.7)	5.8
Roaming agreement	6.1	(1.2)	4.9
	$ 826.5	$ (393.8)	$ 432.7

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

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

4. Goodwill and Other Intangible Assets, Continued:
Amortization expense for intangible assets subject to amortization was $47.5 million and $15.8 million for the three month periods ended March 31, 2006 and 2005, respectively. Amortization expense for intangible assets subject to amortization is estimated to be $168.6 million in 2006, $128.6 million in 2007, $93.7million in 2008, $51.6 million in 2009 and $24.0 million in 2010. See Note 3 for a discussion of the acquisitions completed during the first quarter of 2006 that resulted in the recognition of goodwill and other intangible assets.

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

6. Stock-Based Compensation:
Under the Company's stock-based compensation plans, Alltel may grant fixed and performance-based incentive and non-qualified stock options, restricted stock, and other equity securities to officers and other management employees. The maximum number of shares of the Company's common stock that may be issued to officers and other management employees under all stock compensation plans in effect at March 31, 2006 was 31.6 million shares.

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

The weighted average fair value of stock options granted during the three months ended March 31, 2006 was $19.13 per share using the Black-Scholes option-pricing model and the following weighted average assumptions:

Expected life	6.5 years
Expected volatility	23.6%
Dividend yield	0.8%
Risk-free interest rate	4.3%

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

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

6. Stock-Based Compensation, Continued:

Alltel believes that estimating expected volatility based on a combination of implied and historical volatility is more representative of future stock price trends than using historical volatility alone. The expected dividend yield was based on the Company's approved annual dividend rate in effect at the date of grant adjusted to reflect the expected reduction in Alltel's dividend rate from $1.54 to $.50 per share following the completion of the spin off of the Company's wireline operations to Alltel's shareholders (see Note 14). Future increases to the dividend rate were not included in the development of the dividend yield assumption because Alltel's board of directors has not approved any increase to the dividend rate following completion of the spin-off. The risk-free interest rate was determined using the implied yield currently available for zero-coupon U.S. government issues with a remaining term equal to the expected life of the stock options.

Activity under all of the Company's stock options plans for the three months ended March 31, 2006 was as follows:

	(Thousands) Number of Shares	Weighted Average Price Per Share
Outstanding at December 31, 2005	17,316.5	$53.94
Granted	792.0	62.05
Exercised	(1,529.5)	36.22
Forfeited	(41.7)	53.52
Expired	(7.6)	31.60
Outstanding at March 31, 2006	16,529.7	$55.98
Exercisable at end of period	12,115.7	$56.95

The total intrinsic value of stock options exercised during the three months ended March 31, 2006 was $42.2 million. Alltel received $55.4 million in cash from the exercise of stock options.

The following is a summary of stock options outstanding and exercisable as of March 31, 2006:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	(Thousands) Number of Shares	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price Per Share	(Thousands) Number of Shares	Weighted Average Exercise Price Per Share
$ 7.57 - $14.71	240.6	4.2 years	$10.14	200.8	$10.65
$26.61 - $32.50	519.5	2.3 years	31.63	467.8	31.55
$33.88 - $40.30	1,155.3	1.5 years	34.51	1,153.9	34.50
$43.12 - $50.28	2,480.6	7.0 years	48.35	1,145.2	48.27
$50.81 - $58.46	4,401.3	6.9 years	54.80	2,207.6	55.09
$62.05 - $68.25	7,590.9	4.7 years	65.24	6,798.9	65.61
$70.75 - $73.13	141.5	3.4 years	72.43	141.5	72.43

16,529.7	5.3 years	$55.98	12,115.7	$56.95

Non-vested stock options as of March 31, 2006 and changes during the three months ended March 31, 2006 were as follows:

	(Thousands) Number of Shares	Weighted Average Price Per Share
Non-vested at December 31, 2005	5,051.4	$51.94
Granted	792.0	62.05
Vested	(1,390.9)	53.22
Forfeited	(38.5)	52.80
Non-vested at March 31, 2006	4,414.0	$53.34

At March 31, 2006, the total unamortized compensation cost for non-vested stock option awards amounted to $45.7 million and is expected to be recognized over a weighted average period of 3.4 years. Unrecognized compensation expense for stock options was included in additional paid-in capital in the accompanying consolidated balance sheet and statement of shareholders' equity.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

6. Stock-Based Compensation, Continued:

Restricted Stock - In January 2006, 2005 and 2004, Alltel granted to certain senior management employees restricted stock awards which had an aggregate fair value on the date of grant of $16.6 million, $11.1 million and $8.5 million, respectively. The cost of the restricted stock awards is determined based on the fair market value of the shares at the date of grant reduced by the $1.00 par value per share charged to the employee and is expensed ratably over the vesting period. The restricted shares granted in 2006 will vest in equal increments over a three-year period following the date of grant, except for awards representing 72,000 shares, which will vest in increments of 40%, 30% and 30% over a five-year period beginning three years after the date of grant. The restricted shares granted in 2005 vest three years from the date of grant, except that one-third of the restricted shares may vest after each of the first two-year anniversaries from the grant date if Alltel achieves a certain targeted total stockholder return for its peer group during the three-year period preceding each of those two years. The restricted shares granted in 2004 will vest in equal increments over a three-year period following the date of grant.

Non-vested restricted stock activity for the three months ended March 31, 2006 was as follows:

	Number of Shares	Weighted Average Fair Value Per Share
Non-vested at December 31, 2005	302,530	$52.52
Granted	272,000	61.07
Vested	(52,511)	49.28
Forfeited	-	-
Non-vested at March 31, 2006	522,019	$57.30

At March 31, 2006, unrecognized compensation expense for the restricted shares amounted to $22.7 million and was included in additional paid-in capital in the accompanying consolidated balance sheet and statement of shareholders' equity. The unrecognized compensation expense for the non-vested restricted shares at March 31, 2006 is expected to be recognized over a weighted average period of 2.5 years.

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

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

(Millions)	2006	2005
Benefits earned during the year	$ 6.7	$ 8.4
Interest cost on benefit obligation	14.9	14.6

Special termination benefits		4.5		-
Settlement loss		1.0		-
Amortization of prior service cost		0.1		0.1
Recognized net actuarial loss		8.4		7.6
Expected return on plan assets		(20.9)		(20.7)
Net periodic benefit expense	$	14.7	$	10.0

As further discussed in Note 14, on December 9, 2005, Alltel announced that it would spin off its wireline telecommunications business to its stockholders and merge it with Valor Communications Group, Inc. (“Valor”). Two former executive officers of Alltel still employed by the Company, who are eligible to receive supplemental retirement benefits payable under the Company’s supplemental executive retirement plan, will join the new wireline company being formed in the merger of Alltel’s wireline business with Valor. As a result, the supplemental executive retirement plan was amended to provide for the immediate pay out of the accrued supplemental retirement benefits earned by the two executives at the time the spin-off is consummated. The special termination benefits payable to the two executives and the corresponding settlement loss are being recognized ratably during the first six months of 2006 and have been included in

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

7. Employee Benefit Plans and Postretirement Benefits Other Than Pensions, Continued:
integration expenses and other charges within the Company's consolidated statement of income for the three months ended March 31, 2006. (See Note 8).

Alltel disclosed in its financial statements for the year ended December 31, 2005 that it expected to contribute $20.5 million for retirement benefits in 2006 consisting solely of amounts necessary to fund the expected benefit payments related to the unfunded supplemental retirement plans, a substantial portion of which are for payments to the two executives discussed above. Through March 31, 2006, Alltel had contributed $0.8 million to fund the supplemental retirement plans. Alltel does not expect that any contribution to the qualified defined pension plan calculated in accordance with the minimum funding requirements of the Employee Retirement Income Security Act of 1974 will be required in 2006. Future discretionary contributions to the plan will depend on various factors, including future investment performance, changes in future discount rates and changes in the demographics of the population participating in Alltel's qualified pension plan.

The Company provides postretirement healthcare and life insurance benefits for eligible employees. Employees share in the cost of these benefits. The Company funds the accrued costs of these plans as benefits are paid. The components of postretirement expense were as follows for the three month periods ended March 31:

(Millions)		2006		2005
Benefits earned during the year	$	0.1	$	0.1
Interest cost on benefit obligation		3.3		3.5
Amortization of transition obligation		0.2		0.2
Amortization of prior service cost		0.5		0.5
Recognized net actuarial loss		1.6		1.7
Expected return on plan assets		-		-
Net periodic benefit expense	$	5.7	$	6.0

8. Integration Expenses and Other Charges:
A summary of the integration expenses and other charges recorded during the three months ended March 31, 2006 was as follows:

(Millions)		Wireless		Wireline		Total
Rebranding and signage costs	$	8.3	$	-	$	8.3
Computer system conversion and other integration expenses		2.5		-		2.5
Costs associated with pending spin-off of wireline operations		-		8.7		8.7
Total integration expenses and other charges	$	10.8	$	8.7	$	19.5

The Company incurred $10.8 million of integration expenses related to its acquisition of Western Wireless. These expenses consisted of $8.3 million of rebranding and signage costs and $2.5 million of system conversion and other integration costs. The system conversion and other integration expenses included internal payroll and employee benefit costs, contracted services, relocation expenses and other programming costs incurred in converting Western

Wireless' customer billing and operational support systems to Alltel's internal systems, a process which was completed during the first quarter of 2006. In connection with the spin-off and merger of Alltel's wireline business with Valor, Alltel incurred $8.7 million of incremental costs, primarily consisting of the $5.5 million of special termination benefits payable to the two executives and the corresponding settlement loss previously discussed (see Note 7) and additional consulting and legal fees of $2.7 million.

The following is a summary of the activity related to the liabilities associated with the Company's integration and other restructuring activities for the three months ended March 31, 2006:

(Millions)		
Balance, beginning of period	$	29.7
Integration expenses and other charges recorded during the period		19.5
Non-cash portion of integration expenses and other charges		(0.7)
Cash outlays during the period		(12.6)
Balance, end of period	$	35.9

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

8. Integration Expenses and Other Charges, Continued:
At March 31, 2006, the remaining unpaid liability related to Alltel's integration and restructuring activities consisted of investment banker, audit, consulting and legal fees of $33.1 million, integration costs of $2.6 million and lease and contract termination costs of $0.2 million. Of the total remaining liability, $33.1 million was included in accounts payable and $2.8 million was included in other current liabilities in the accompanying consolidated balance sheet as of March 31, 2006. The integration expenses and other charges decreased net income $12.7 million for the three months ended March 31, 2006.

9. Investments - Special Cash Dividend:
On March 28, 2005, Alltel received a special $10 per share cash dividend from Fidelity National totaling $111.0 million, related to the shares of Fidelity National common stock received as partial consideration for the sale of Alltel's financial services business to Fidelity National on April 1, 2003. On April 6, 2005, Alltel completed the sale of all of its shares of Fidelity National common stock. The special cash dividend was included in other income, net in the accompanying consolidated statement of income for the three months ended March 31, 2005.

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

On September 15, 2005, Alltel completed the sale of Western Wireless' international operations in Georgia and Ghana for $51.7 million in cash. On November 23, 2005, Alltel also completed the sale of Western Wireless' international operations in Ireland to a subsidiary of eircom Group plc, the Irish fixed-line telecommunications operator, for 420 million euros or approximately $518.6 million. On August 10, 2005, Alltel announced a definitive agreement to sell the Western Wireless international operations in Austria to T-Mobile Austria GmbH, a subsidiary of Deutsche Telekom for 1.3 billion euros. As discussed in Note 15, on April 28, 2006, Alltel completed the sale of the Austrian business and received cash proceeds of $1.6 billion. On that same day, Alltel also completed the sale of the Western Wireless international operations in Haiti for $70.6 million in cash. Alltel has a pending definitive agreement to sell the international operations in Bolivia and is actively pursuing the disposition of the remaining international operations acquired from Western Wireless. Alltel expects to complete the disposition of the remaining international operations during the second quarter of 2006.

The acquired international operations and interests of Western Wireless and the domestic market in Arkansas to be divested by Alltel have been classified as assets held for sale and discontinued operations in the Company's interim consolidated financial statements as of and for the period ended March 31, 2006. Depreciation of long-lived assets related to the international operations and the domestic markets to be divested was not recorded subsequent to the completion of the merger. The fair value of the net assets held for sale was based upon the expected proceeds to be received by Alltel from the disposition of these operations.

The following table includes certain summary income statement information related to the international operations and the domestic market in Arkansas to be divested reflected as discontinued operations for the three months ended March 31, 2006:

(Millions)		
Revenues and sales	$	206.4
Operating expenses		154.6
Operating income		51.8
Minority interest expense in unconsolidated entities		(4.5)
Other expense, net (a)		(0.7)
Pretax income from discontinued operations		46.6
Income tax expense		28.8
Income from discontinued operations	$	17.8

Notes:

(a) Except for the Bolivian credit facility discussed below, Alltel had no outstanding indebtedness directly related to the international operations that were acquired from Western Wireless, and accordingly, no additional interest expense was allocated to discontinued operations for the period presented.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

10. Discontinued Operations, Continued:

The following table includes the net assets of the remaining international operations in Austria, Bolivia, Haiti and Slovenia that have been classified as held for sale in the accompanying unaudited consolidated balance sheet as of March 31, 2006:

(Millions)		
Current assets	$	216.1
Property, plant and equipment		334.0
Goodwill and other intangible assets (a)		1,439.9
Other assets		37.1
Assets held for sale	$	2,027.1
Current liabilities	$	182.6
Long-term debt (b)		47.6
Other liabilities		71.5
Liabilities related to assets held for sale	$	301.7

Notes:

(a) Includes the fair value of licenses and customer lists. Because substantially all of the assets classified as held for sale will be disposed of by June 30, 2006, the Company will not complete third party valuations to assign specific fair values to the identifiable intangible assets of the international operations and the domestic markets to be divested.

(b) Represents amounts outstanding under a credit facility agreement between Alltel's Bolivian subsidiary and the Overseas Private Investment Corporation. Under the terms of the credit facility, all outstanding principal is required to be repaid in predetermined quarterly installments beginning on July 15, 2006 and ending on April 15, 2014. Interest accrues at a rate of 8.74 percent and is payable on a quarterly basis. The credit facility contains certain restrictive covenants, including a debt service coverage ratio which does not become effective until the third quarter of 2006, limitations on the Bolivian subsidiary's ability to incur additional indebtedness, make certain asset dispositions or restricted payments. Substantially all of the Bolivian subsidiary's assets have been pledged as collateral for the credit facility.

11. Other Comprehensive Income (Loss):

Other comprehensive income (loss) consists of unrealized holding gains (losses) on investments in equity securities and foreign currency translation adjustments. Other comprehensive income (loss) was as follows for the three month periods ended March 31:

(Millions)		2006		2005
Other comprehensive income (loss):				
Unrealized holding gains (losses) on investments:				
Unrealized holding gains (losses) arising in the period	$	12.4	$	(142.6)

Income tax expense (benefit)		4.4		(49.9)
		8.0		(92.7)
Foreign currency translation adjustment for the period		17.6		-
Other comprehensive income (loss) before tax		30.0		(142.6)
Income tax expense (benefit)		4.4		(49.9)
Other comprehensive income (loss)	$	25.6	$	(92.7)

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

12. Earnings per Share:

Basic earnings per share of common stock was computed by dividing net income applicable to common shares by the weighted average number of common shares outstanding during each period. Diluted earnings per share reflects the potential dilution that could occur assuming conversion or exercise of all dilutive unexercised stock options and outstanding restricted and preferred stock. The dilutive effects of stock options and preferred stock were determined using the treasury stock method. Under the treasury stock method, the proceeds received from the exercise of stock options, the amount of compensation cost for future service not yet recognized by the Company and the amount of tax benefits that would be recorded in additional paid in capital when the stock options become deductible for income tax purposes are assumed to be used to repurchase shares of the Company's common stock. The number of stock options that were not included in the computation of diluted earnings per share were approximately 4.6 million and 9.0 million shares of common stock for the three months ended March 31, 2006 and 2005, respectively. A reconciliation of the net income and number of shares used in computing basic and diluted earnings per share was as follows for the three month periods ended
March 31:

(Millions, except per share amounts)		2006		2005
Basic earnings per share:				
Income from continuing operations	$	279.6	$	313.0
Income from discontinued operations		17.8		-
Less preferred dividends		-		-
Net income applicable to common shares	$	297.4	$	313.0
Weighted average common shares outstanding for the period		386.8		302.2
Basic earnings per share:				
From continuing operations		$.72		$1.04
From discontinued operations		.05		-
Net income		$.77		$1.04
Diluted earnings per share:				
Net income applicable to common shares	$	297.4	$	313.0
Adjustment for interest expense on convertible notes, net of tax		0.1		-
Adjustment for convertible preferred stock dividends		-		-
Net income applicable to common shares assuming conversion of preferred stock and convertible notes	$	297.5	$	313.0
Weighted average common shares outstanding for the period		386.8		302.2
Increase in shares resulting from:				
Assumed exercise of stock options		1.5		1.0
Assumed conversion of convertible notes		1.0		-
Assumed conversion of preferred stock		0.2		0.2
Non-vested restricted stock awards		0.2		0.1
Weighted average common shares assuming conversion		389.7		303.5
Diluted earnings per share				
From continuing operations		$.72		$1.03
From discontinued operations		.05		-
Net income		$.77		$1.03

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

13. Business Segment Information:

Alltel manages its business operations based on differences in products and services. The Company evaluates performance of the segments based on segment income, which is computed as revenues and sales less operating expenses, excluding the effects of the items discussed in Notes 8 and 9, respectively. Items not allocated to the segments are included in corporate operations. In addition, as previously discussed in Note 2, effective January 1, 2006, the Company retrospectively changed its business segment reporting to exclude from wireless segment income the effects of amortization expense related to intangible assets recorded in connection with the acquisition of wireless properties. As a result, wireless segment income excludes pretax amortization expense of $45.5 million and $13.8 million for the three months ended March 31, 2006 and 2005, respectively. This amortization expense is now included in corporate expenses. Segment operating results were as follows for the three month periods ended March 31:

(Millions)		2006		2005
Revenues and Sales from External Customers:				
Wireless	$	1,755.9	$	1,350.4
Wireline		537.0		556.0
Communications support services		191.0		170.1
Total business segments	$	2,483.9	$	2,076.5
Intersegment Revenues and Sales:				
Wireless	$	1.5	$	1.6
Wireline		38.4		37.6
Communications support services		59.9		54.6
Total business segments	$	99.8	$	93.8
Total Revenues and Sales:				
Wireless	$	1,757.4	$	1,352.0
Wireline		575.4		593.6
Communications support services		250.9		224.7
Total business segments		2,583.7		2,170.3
Less intercompany eliminations		(44.0)		(44.3)
Total revenues and sales	$	2,539.7	$	2,126.0
Segment Income:				
Wireless	$	355.5	$	285.3
Wireline		226.6		214.5
Communications support services		21.5		11.9
Total segment income		603.6		511.7
Corporate expenses		(54.9)		(42.4)
Integration expenses and other charges		(19.5)		-
Equity earnings in unconsolidated partnerships		12.9		10.7
Minority interest in consolidated partnerships		(13.9)		(18.3)
Other income, net		11.9		120.7
Interest expense		(89.0)		(86.7)
Income from continuing operations before income taxes	$	451.1	$	495.7

Segment assets were as follows:

(Millions)	March 31, 2006	December 31, 2005
Wireless	$ 15,536.2	$ 15,416.3
Wireline	4,828.0	4,878.6
Communications support services	495.6	533.5
Total business segments	20,859.8	20,828.4
Corporate headquarters assets not allocated to segments	1,182.8	1,270.1
Assets held for sale	2,027.1	1,951.2
Less elimination of intersegment receivables	(23.6)	(36.6)
Total consolidated assets	$ 24,046.1	$ 24,013.1

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

13. Business Segment Information, Continued:

Supplemental information pertaining to the communications support services segment was as follows for the three month periods ended March 31:

(Millions)		2006		2005
Revenues and Sales from External Customers:				
Product distribution	$	108.9	$	93.8
Long-distance and network management services		53.6		47.0
Directory publishing		24.5		24.1
Telecommunications information services		4.0		5.2
Total	$	191.0	$	170.1
Intersegment Revenues and Sales:				
Product distribution	$	30.6	$	26.8
Long-distance and network management services		27.4		25.6
Directory publishing		1.9		2.2
Telecommunications information services		-		-
Total	$	59.9	$	54.6
Total Revenues and Sales:				
Product distribution	$	139.5	$	120.6
Long-distance and network management services		81.0		72.6
Directory publishing		26.4		26.3
Telecommunications information services		4.0		5.2
Total revenues and sales	$	250.9	$	224.7

14. Pending Transactions:

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

Spin Off of Wireline Business and Merger with Valor Communications Group, Inc. - On December 9, 2005, Alltel announced that its board of directors had approved the spin-off of the Company’s wireline telecommunications business to its stockholders and the merger of that wireline business with Valor. The spin off will include the majority of Alltel’s communications support services, including directory publishing, information technology outsourcing services, retail long distance and the wireline sales portion of communications products. Pursuant to the plan of distribution and immediately prior to the effective time of the merger with Valor described below, Alltel will contribute all of the assets of its wireline telecommunications business to ALLTEL Holding Corp. (“Alltel Holding” or “Spinco”), a wholly owned subsidiary of the Company, in exchange for: (i) the issuance to Alltel of Spinco common stock to be distributed pro rata to Alltel’s stockholders as a tax free stock dividend, (ii) the payment of a special

dividend to Alltel in an amount not to exceed the Company's tax basis in Spinco, and (iii) the distribution by Spinco to Alltel of certain Spinco debt securities, which Alltel intends to exchange for outstanding Company debt securities or otherwise transfer to Alltel's creditors. Alltel will also transfer to Spinco approximately $261.0 million of long-term debt that had been issued by the Company's wireline subsidiaries. Prior to the distribution and merger with Valor, Spinco will borrow approximately $4.0 billion (the "Spinco financing amount") through a new senior credit agreement, the issuance of high yield debt securities in the private placement market or through a public offering to pay the special dividend and to distribute debt securities to Alltel in an amount equal to the difference between the Spinco financing amount and the special dividend. Alltel has received a commitment letter from various financial institutions to provide Spinco with up to $4.2 billion in senior secured credit facilities comprised of term loan facilities in an aggregate amount of up to $3.7 billion and a revolving credit facility of up to $500 million.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS-(Continued)

14. Pending Transactions, Continued:

Immediately after the consummation of the spin off, Alltel Holding will merge with and into Valor, with Valor continuing as the surviving corporation. As a result of the merger, all of the issued and outstanding shares of Spinco common stock will be converted into the right to receive an aggregate number of shares of common stock of Valor. Valor is expected to issue in the aggregate approximately 403 million shares of common stock to Alltel stockholders pursuant to the merger, or approximately 1.04 shares of Valor common stock (subject to variation based on the number of Spinco common shares to be distributed to Alltel stockholders and as a result of compensatory equity grants and other issuances) for each share of Spinco common stock outstanding as of the effective time of the merger. Upon completion of the merger, Alltel stockholders will own approximately 85 percent of the outstanding equity interests of the surviving corporation, which will be named Windstream Corporation, and the stockholders of Valor will own the remaining 15 percent of such equity interests. As a result of the merger, Valor will also assume approximately $4.2 billion of long-term debt.

Upon the spin-off of the wireline business, the number of shares underlying stock options held by wireless employees and the related per share exercise price will be adjusted to maintain both the aggregate fair market value of stock underlying the stock options and the relationship between the per share exercise price and the related per share market value. Unvested options held by wireline employees will be replaced with restricted shares of Valor common stock. As of March 31, 2006, wireline employees held vested options to purchase approximately 1.7 million shares of Alltel common stock.

Consummation of the merger is subject to certain outstanding conditions, including the approval of the merger by the stockholders of Valor, consummation of the Spinco financing, and the receipt of regulatory approvals from multiple state public service commissions. The transaction is expected to close by mid-year 2006. The merger agreement contains certain termination rights for each of Alltel and Valor and further provides that, upon termination of the merger agreement under specified circumstances involving an alternative transaction, Valor may be required to pay Alltel a termination fee of $35.0 million. Conversely, Alltel may be required to pay Valor a termination fee of (i) $35.0 million if Valor terminates the merger agreement because of a material breach by Alltel or Spinco that results in the failure of the parties to obtain the Spinco financing or any party terminates the merger agreement after December 8, 2006 and at the time of termination all conditions have been satisfied other than the Spinco financing condition and (ii) $20.0 million if Valor terminates the merger agreement because of a material breach by Alltel or Spinco that results in the failure of the parties to obtain the required tax opinions or any party terminates the merger agreement after December 8, 2006 and at the time of termination all conditions have been satisfied other than the tax opinion conditions.

15. Subsequent Events

Sale of Certain International Operations - On April 28, 2006, Alltel completed the sale of Western Wireless' international operations in Austria to T-Mobile Austria GmbH, a subsidiary of Deutsche Telekom for 1.3 billion euros, or $1.6 billion. Also on April 28, 2006, the Company completed the sale of Western Wireless' international operations in Haiti and received approximately $70.6 million in cash proceeds. Because the carrying value of the sold operations at March 31, 2006 approximated the net proceeds received, Alltel expects that any pretax gain or loss realized from these sales will be immaterial to the Company's consolidated results of operations for the interim periods ended
June 30, 2006.

Receipt of Liquidating Distribution - On November 10, 2005, federal legislation was enacted which included provisions to dissolve and liquidate the assets of the Rural Telephone Bank (“RTB”). In connection with the dissolution and liquidation, the RTB will redeem all outstanding shares of its Class C stock. During April 2006, Alltel received liquidating cash distributions of $198.7 million in exchange for its $22.1 million investment in RTB Class C stock. The pretax gain of $176.6 million resulting from the liquidating distributions will be included in Alltel’s consolidated results of operations for the interim periods ended June 30, 2006.

ALLTEL CORPORATION
FORM 10-Q
PART I - FINANCIAL INFORMATION

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

GENERAL

The following is a discussion and analysis of the historical results of operations and financial condition of ALLTEL Corporation ("Alltel" or the "Company"). This discussion should be read in conjunction with the unaudited consolidated financial statements, including the notes thereto, for the interim periods ended March 31, 2006 and 2005, and Alltel's Annual Report on Form 10-K for the year ended December 31, 2005.

EXECUTIVE SUMMARY

Alltel is a customer-focused communications company providing wireless, local telephone, long-distance, Internet and high-speed data services to more than 15 million residential and business customers in 36 states. Among the highlights in the first quarter of 2006:

- Wireless revenues and sales increased 30 percent over 2005 reflecting the effects of Alltel's August 1, 2005 acquisition of Western Wireless Corporation ("Western Wireless") and the exchange of wireless properties with Cingular Wireless LLC ("Cingular") completed during the second quarter of 2005. Excluding the effects of acquisitions, wireless revenues and sales increased 9 percent from a year ago driven by Alltel's continued focus on quality customer growth, improvements in data revenues and additional Eligible Telecommunications Carrier ("ETC") subsidies. Average revenue per customer increased 4 percent from a year ago to $50.90, while retail revenue per customer increased to $46.21, a 2 percent increase from a year ago. Retail minutes of use per wireless customer per month increased to 610 minutes, a 12 percent increase from the same period of 2005.

- Wireless gross customer additions were 805,000 in the quarter, and net customer additions were 165,000. Within its non-acquired or heritage markets, gross customer additions increased 20 percent compared to the first quarter of 2005. In its heritage markets, Alltel added 48,000 net postpay wireless customers and added 105,000 net prepaid customers during the first quarter of 2006. The net gain in prepaid customers reflected continued growth in Simple Freedom, Alltel's phone-in-the-box prepay service that is sold primarily through Wal-Mart stores and the roll-out of Alltel's new "U" prepaid wireless service, which offers customers expanded phone selection, choice of enhanced features and free nationwide long distance calling originating within the Alltel network. In the acquired markets, Alltel added 12,000 customers. Wireless postpay churn decreased 6 basis points from the same period a year ago to 1.66 percent, while total churn declined 11 basis points year-over-year to 2.00 percent. In Alltel's heritage markets, postpay churn declined 4 basis points year-over-year to 1.68 percent.

- Wireless segment income increased 25 percent from a year ago, primarily reflecting the acquisition-related growth in revenues and sales noted above. Growth in wireless segment income was affected by additional customer acquisition costs due to the significant increase in gross customer additions noted above.

- In its wireline business, Alltel added 44,000 broadband customers, increasing Alltel's broadband customer base to 441,000. During the quarter, the Company lost approximately 23,000 wireline access lines, a year-over-year decline of 4 percent. Average revenue per wireline customer increased 1 percent from a year ago to $66.77 due primarily to growth in broadband revenues. Although wireline revenues and sales decreased 3 percent from a year ago, wireline segment income increased 6 percent year-over-year, primarily due to a reduction in depreciation rates for Alltel's Florida, Georgia, Pennsylvania and South Carolina operations, reflecting the results of studies of depreciable lives

completed by Alltel during the second half of 2005 and in January 2006.

As further discussed under “Acquisitions to be Completed in 2006”, Alltel positioned its wireless business for future growth opportunities as a result of the Company’s planned acquisition of Midwest Wireless Holdings of Mankato, Minnesota (“Midwest Wireless”). Through this acquisition, which is expected to close in the third quarter of 2006, Alltel will add approximately 400,000 wireless customers and expand its wireless operations in Minnesota, Iowa and Wisconsin. On May 1, 2006, Alltel also purchased a wireless property in Illinois with a potential service area covering 485,000 potential customers for $141.1million in cash.

On December 9, 2005, Alltel announced that it would spin off its wireline telecommunications business to its stockholders and merge it with Valor Communications Group, Inc. (“Valor”). The spin off will include the majority of Alltel’s communications support services, including directory publishing, information technology outsourcing services, retail long distance and the wireline sales portion of communications products. The transaction, which is further discussed under “Pending Transactions to be Completed in 2006”, is expected to close by mid-year 2006.

During the first quarter of 2006, Alltel expanded its opportunities for selling additional wireless data service through the launch of an EV-DO blackberry device and several new data applications including Axcess Radio, which includes 40 channels of commercial-free streaming music. Alltel expects to continue to launch data applications and products throughout the year to take advantage of its expanded EV-DO coverage, resulting from the Company’s network build plans with market launches scheduled for the second half of the year. To maintain its post-pay customer growth and extend the reach of the Alltel brand, the Company also recently launched a new service offering called “My Circle”, which enables Alltel customers, on select rate plans priced $59.95 or higher, to make and receive unlimited free calls to up to ten phone numbers connected to any wireless or wireline network, and add these phone numbers to their mobile-to-mobile service.

Throughout the remainder of 2006, Alltel will continue to face significant challenges resulting from competition in the telecommunications industry and changes in the regulatory environment, including the effects of potential changes to the rules governing universal service and inter-carrier compensation. In addressing these challenges, Alltel will continue to focus its efforts on improving customer service, enhancing the quality of its networks, expanding its product and service offerings, and conducting vigorous advocacy efforts in favor of governmental policies that will benefit Alltel’s business and its customers.

PENDING TRANSACTIONS TO BE COMPLETED DURING 2006

Spin Off of Wireline Business and Merger with Valor

Pursuant to the plan of distribution and immediately prior to the effective time of the merger with Valor described below, Alltel will contribute all of the assets of its wireline telecommunications business to ALLTEL Holding Corp. (“Alltel Holding” or “Spinco”), a wholly owned subsidiary of Alltel, in exchange for: (i) the issuance to Alltel of Spinco common stock to be distributed pro rata to Alltel’s stockholders as a tax free stock dividend, (ii) the payment of a special dividend to Alltel in an amount not to exceed the Company’s tax basis in Spinco, and (iii) the distribution by Spinco to Alltel of certain Spinco debt securities, which Alltel intends to exchange for outstanding Company debt securities or otherwise transfer to Alltel’s creditors. Alltel will also transfer to Spinco approximately $261.0 million of long-term debt that had been issued by the Company’s wireline subsidiaries. Prior to the distribution and merger with Valor, Spinco will borrow approximately $4.0 billion (the “Spinco financing amount”) through a new senior credit agreement, the issuance of high yield debt securities in the private placement market or through a public offering to pay the special dividend and to distribute debt securities to Alltel in an amount equal to the difference between the Spinco financing amount and the special dividend. Alltel has received a commitment letter from various financial institutions to provide Spinco with up to $4.2 billion in senior secured credit facilities comprised of term loan facilities in an aggregate amount of up to $3.7 billion and a revolving credit facility of up to $500 million.

Immediately after the consummation of the spin off, Alltel Holding will merge with and into Valor, with Valor continuing as the surviving corporation. As a result of the merger, all of the issued and outstanding shares of Spinco common stock will be converted into the right to receive an aggregate number of shares of common stock of Valor. Valor is expected to issue in the aggregate approximately 403 million shares of common stock to Alltel stockholders pursuant to the merger, or approximately 1.04 shares of Valor common stock (subject to variation based on the number of Spinco common shares to be distributed to Alltel stockholders and as a result of compensatory equity grants and other issuances) for each share of Spinco common stock outstanding as of the effective time of the merger. Upon completion of the merger, Alltel stockholders will own approximately 85 percent of the outstanding equity interests of the surviving corporation, which will be named Windstream Corporation, and the stockholders of Valor will own the remaining 15 percent of such equity interests. Valor will also assume approximately $4.2 billion of

long-term debt. Consummation of the merger is subject to certain outstanding conditions, including the approval of the merger by the stockholders of Valor, consummation of the Spinco financing, and the receipt of regulatory approvals from multiple state public service commissions. The transaction is expected to close by mid-year 2006. (See "Integration Expenses and Other Charges" below for a discussion of nonrecurring expenses recorded by Alltel in the first quarter of 2006 related to the spin off and merger transaction).

Acquisitions to be Completed During 2006
On November 18, 2005, Alltel announced that it had entered into a definitive agreement to purchase Midwest Wireless for $1.075 billion in cash. Under terms of the agreement, Alltel will acquire wireless properties, including 850 MHz licenses and Personal Communications Services spectrum covering approximately 2.0 million potential customers ("POPs"), network assets and approximately 400,000 customers in select markets in southern Minnesota, northern and eastern Iowa, and western Wisconsin. Closing of the transaction is contingent upon regulatory approval, including approval of the Federal Communications Commission ("FCC") and the termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended. (See Note 14 to the unaudited interim consolidated financial statements for additional information regarding these pending transactions.)

ACQUISITIONS
On March 16, 2006, Alltel purchased from Palmetto MobileNet, L.P. for $456.3 million in cash the remaining ownership interests in ten wireless partnerships that cover approximately 2.0 million POPs in North and South Carolina. Prior to this transaction, Alltel owned a 50 percent interest in each of the ten wireless partnerships. During the first quarter of 2006, Alltel also acquired for $2.6 million in cash the remaining ownership interest in a wireless property in Wisconsin in which the Company owned a majority interest.

On August 1, 2005, Alltel and Western Wireless completed the merger of Western Wireless with and into a wholly-owned subsidiary of Alltel. In the merger, each share of Western Wireless common stock was exchanged for 0.535 shares of Alltel common stock and $9.25 in cash unless the shareholder made an all-cash election, in which case the shareholder received $40 in cash. Western Wireless shareholders making an all-stock election were subject to proration and received approximately 0.539 shares of Alltel common stock and $9.18 in cash. In the aggregate, Alltel issued approximately 54.3 million shares of stock valued at $3,430.4 million and paid approximately $933.4 million in cash. Through its wholly-owned subsidiary that merged with Western Wireless, Alltel also assumed debt of approximately $2.1 billion. As a result of the merger, Alltel added approximately 1.3 million domestic wireless customers in 19 midwestern and western states that are contiguous to the Company's existing wireless properties, increasing the number of wireless customers served by Alltel to more than 10 million customers in 34 states.

As a condition of receiving approval for the merger from the U.S. Department of Justice ("DOJ") and FCC, Alltel agreed to divest certain wireless operations of Western Wireless in 16 markets in Arkansas, Kansas and Nebraska, as well as the "Cellular One" brand. On December 19, 2005, Alltel completed an exchange of wireless properties with United States Cellular Corporation ("U.S. Cellular") that included a substantial portion of the divestiture requirements related to the merger. Under terms of the agreement, Alltel acquired approximately 90,000 customers in two Rural Service Area ("RSA") markets in Idaho that are adjacent to the Company's existing operations and received $48.2 million in cash in exchange for 15 rural markets in Kansas and Nebraska owned by Western Wireless. In December 2005, Alltel sold the Cellular One brand to Dobson Cellular Systems, Inc., and on March 24, 2006, Alltel completed the sale of the remaining market in Arkansas to Cingular. During 2005, Alltel completed the sale of Western Wireless' international operations in Georgia, Ghana and Ireland for $570.3 million in cash, and on April 28, 2006, Alltel completed the sales of the Western Wireless international operations in Austria and Haiti for approximately $1.7 billion in cash. Alltel has a pending definitive agreement to sell the international operations in Bolivia and is actively pursuing the disposition of the remaining international operations acquired from Western Wireless. Alltel expects to complete the disposition of the remaining operations during the second quarter of 2006. Accordingly, the acquired international operations and interests of Western Wireless and the domestic markets required to be divested by Alltel have been classified as assets held for sale and discontinued operations in the accompanying consolidated financial statements. During the first quarter of 2006, Alltel substantially completed the integration of the remaining acquired domestic operations of Western Wireless and in connection with its integration efforts incurred $10.8 million of incremental expenses during the first three months of 2006, principally consisting of costs for branding, signage, retail store redesigns and computer system conversions. (See "Integration Expenses and Other Charges" below for a discussion of integration expenses recorded by Alltel in the first quarter of 2006).

On April 15, 2005, Alltel and Cingular exchanged certain wireless assets. Under the terms of the agreement, Alltel acquired former AT&T Wireless properties, including licenses, network assets, and subscribers, in selected markets in Kentucky, Oklahoma, Texas, Connecticut and Mississippi representing approximately 2.7 million POPs. Alltel also acquired 20MHz of spectrum and network assets formerly owned by AT&T Wireless in Kansas and wireless spectrum in several counties in Georgia and Texas. In addition, Alltel and Cingular exchanged partnership interests, with Cingular receiving interests in markets in Kansas, Missouri and Texas, and Alltel receiving more ownership in majority-owned markets it manages in Michigan, Louisiana, and Ohio. Alltel also paid Cingular approximately $153.0 million in cash. In this transaction, Alltel added approximately 212,000 customers. (See Note 3 to the consolidated financial statements for additional information regarding these acquisitions.)

CONSOLIDATED RESULTS OF OPERATIONS

(Millions, except per share amounts)	Three Months Ended March 31, 2006	2005
Revenues and sales:		
Service revenues	$ 2,247.7	$ 1,898.3
Product sales	292.0	227.7
Total revenues and sales	2,539.7	2,126.0
Costs and expenses:		
Cost of services	731.7	626.3
Cost of products sold	355.8	281.8
Selling, general, administrative and other	499.0	407.4
Depreciation and amortization	404.5	341.2
Integration expenses and other charges	19.5	-
Total costs and expenses	2,010.5	1,656.7
Operating income	529.2	469.3
Non-operating income, net	10.9	113.1
Interest expense	(89.0)	(86.7)
Income from continuing operations before income taxes	451.1	495.7
Income taxes	171.5	182.7
Income from continuing operations	279.6	313.0
Income from discontinued operations, net of tax	17.8	-
Net income	$ 297.4	$ 313.0
Basic earnings per share:		
Income from continuing operations	$.72	$1.04
Income from discontinued operations	.05	-
Net income	$.77	$1.04
Diluted earnings per share:		
Income from continuing operations	$.72	$1.03
Income from discontinued operations	.05	-
Net income	$.77	$1.03

Total revenues and sales increased 19 percent, or $413.7 million, for the three months ended March 31, 2006, compared to the same period of 2005. Service revenues increased by 18 percent, or $349.4 million, in the first quarter of 2006 compared to the prior year. The acquisitions of wireless properties from Cingular, Western Wireless and U.S. Cellular previously discussed accounted for approximately $270.4 million of the overall increase in service revenues in 2006. In addition to the effects of the acquisitions, service revenues increased $55.5 million in the first quarter of 2006 due to nonacquisition-related growth in Alltel’s wireless postpay customer base and increased revenues derived from the Company’s Simple Freedom and ”U” prepaid service offerings. Service revenues for 2006 also reflected growth in revenues derived from wireless and wireline data services, which increased $43.0 million from the same period a year ago, primarily reflecting strong demand for these services. Wireless services revenues also included increases in regulatory and other fees of $14.7 million in the three month period of 2006 due to additional Universal Service Fund (“USF”) support received by Alltel reflecting an increase in the contribution factor, and additional revenues attributable to Alltel’s certification in 23 states as an ETC, which accounted for $9.9 million of the overall increase in regulatory fees in the first quarter of 2006. Revenues from the sale of wireless equipment protection plans increased $11.9 million in the three month period of 2006 compared to the same prior year period, reflecting customer growth and continued demand for these plans. As compared to the same period of 2005, wholesale wireless revenues increased

$3.4 million in the first quarter of 2006, primarily due to growth in CDMA minutes of use.

The above increases in service revenues were partially offset by lower wireless airtime and retail roaming revenues and reductions in wireline access and toll service revenues. Compared to the first quarter of 2005, wireless airtime and retail roaming revenues decreased $22.5 million in the three month period of 2006, primarily due to the effects of customers migrating to rate plans with a larger number of packaged minutes. Such rate plans, for a flat monthly service fee, provide customers with a specified number of airtime minutes and include unlimited weekend, nighttime and mobile-to-mobile minutes at no extra charge. Wireline local access service and intrastate network access and toll revenues decreased $25.0 million in the first quarter of 2006, primarily as a result of the loss of wireline access lines due, in part, to broadband and wireless substitution.

Product sales increased $64.3 million, or 28 percent, in the three month period ended March 31, 2006, compared to the same period of 2005. The increase in product sales in 2006 was primarily driven by higher retail prices realized on the sale of wireless handsets that include advanced features, such as picture messaging, and that are capable of downloading music, games, entertainment content, weather and office applications. The acquisitions of wireless properties previously discussed accounted for $14.5 million of the overall increase in product sales in the first quarter of 2006. The increase in product sales in 2006 also reflected the continued retention efforts by the Company focused on migrating existing wireless customers to new wireless technologies.

Cost of services increased $105.4 million, or 17 percent, in the three month period ended March 31, 2006, compared to the same period of 2005. The wireless property acquisitions accounted for approximately $71.6 million of the overall increase in cost of services in 2006. Cost of services for 2006 also reflected higher wireless network-related costs of $32.8 million, resulting from increased network traffic due to nonacquisition-related customer growth, increased minutes of use and expansion of network facilities. Cost of services in 2006 also included increased wireless customer service expenses of $8.2 million, reflecting additional costs associated with Alltel’s retention efforts focused on improving customer satisfaction and reducing postpay churn. Compared to the same period in 2005, payments to data content providers increased $8.0 million in the first quarter of 2006 consistent with the growth in revenues derived from data services discussed above. Cost of services for 2006 also included additional wireless bad debt expense of $7.7 million, primarily due to non-acquisition growth in customers and increased write-offs associated with early disconnect penalties. Conversely, cost of services in Alltel’s wireline operations decreased $5.1 million in the first quarter of 2006 due to the loss of wireline access lines and the Company’s continued efforts to control operating expenses in its wireline business. Comparatively, cost of services for the three month period of 2005 included $19.8 million of incremental costs primarily related to a change in accounting for operating leases. Certain of Alltel’s operating lease agreements for cell sites and for office and retail locations include scheduled rent escalations during the initial lease term and/or during succeeding optional renewal periods. Prior to January 1, 2005, Alltel had not recognized the scheduled increases in rent expense on a straight-line basis in accordance with the provisions of Statement of Financial Accounting Standards (“SFAS”) No. 13, “Accounting for Leases”, and Financial Accounting Standards Board (“FASB”) Technical Bulletin No. 85-3, “Accounting for Operating Leases with Scheduled Rent Increases”. The effects of this change, which were included in corporate expenses, were not material to Alltel’s previously reported consolidated results of operations, financial position or cash flows.

Cost of products sold increased $74.0 million, or 26 percent, in the first quarter of 2006 compared to the same period a year ago. The increase in 2006 was consistent with the overall growth in product sales noted above and reflected the sales of higher-priced wireless handsets and increased sales to resellers and other distributors. The wireless acquisitions discussed above accounted for $27.8 million of the overall increase in cost of products sold in 2006. In addition to the effects of the acquisitions, cost of products sold increased primarily due to increased sales of higher-priced wireless handsets and the Company’s continuing customer retention efforts, which include subsidizing the cost of new handsets provided to existing customers before the expiration of their service contracts.

Selling, general, administrative and other expenses increased $91.6 million, or 22 percent, in first quarter of 2006, compared to the same period a year ago. The wireless property acquisitions accounted for $64.4 million of the overall increase in these expenses in the first quarter of 2006. In addition to the effects of the acquisitions, selling, general, administrative and other operating expenses for 2006 also reflected increased commission costs of $15.7 million consistent with the significant increase in gross customer additions for the quarter. Selling, general, administrative and other expenses also included increased advertising costs of $9.6 million attributable to the Company’s continued efforts to promote the Alltel brand, and incremental stock-based compensation of $7.4 million, primarily due to Alltel’s adoption of SFAS No. 123(R), “Share-Based Payment”, effective January 1, 2006, as more fully discussed in Note 2 to the unaudited interim consolidated financial statements.

Depreciation and amortization expense increased $63.3 million, or 19 percent, in the three month period ended March 31, 2006, compared to the same period of 2005. Depreciation expense increased $32.6 million in the first quarter of 2006 primarily due to the wireless property acquisitions, which accounted for $41.5 million of the overall increase in depreciation expense. Additionally, growth in wireless plant in service, consistent with Alltel's plans to expand and upgrade its network facilities, also contributed to the overall increase in depreciation expense in the first quarter of 2006. The increases in depreciation expense attributable to the wireless property acquisitions and growth in wireless plant in service were partially offset by lower wireline depreciation expense of $23.7 million, reflecting a reduction in depreciation rates for the Company's Florida, Georgia, Pennsylvania and South Carolina operations. Depreciation rates for these operations were reduced as a result of studies of depreciable lives completed by Alltel during the second half of 2005 and in January 2006. Compared to the same period a year ago, amortization expense increased $31.7 million in the first quarter of 2006 due to the wireless property acquisitions and the adverse effects of using an accelerated amortization method for customer lists recorded in connection with those acquisitions.

Operating income increased $59.9 million, or 13 percent, in the three month period ended March 31, 2006, compared to the same period a year ago. The increase in 2006 primarily reflected growth in wireless segment income resulting from the effects of the wireless property acquisitions, which accounted for $79.5 million of the overall increase in operating income for the first quarter of 2006. Wireline segment income increased $12.1 million year-over-year, primarily due to a reduction in depreciation rates for the Company's Florida, Georgia, Pennsylvania and South Carolina operations discussed above. Operating income comparisons for the three month period of 2006 were adversely affected by the increase in amortization expense related to acquired intangible assets previously discussed and the effects of integration expenses and other charges, as further discussed below. The changes in wireless and wireline segment income in the first quarter of 2006 are further discussed below under "Results of Operations by Business Segment". Comparatively, operating income for the first quarter of 2005 included the incremental costs associated with Alltel's change in accounting for certain operating leases previously discussed.

Integration Expenses and Other Charges

A summary of the integration expenses and other charges recorded during the three months ended March 31, 2006 was as follows:

(Millions)		Wireless		Wireline		Total
Rebranding and signage costs	$	8.3	$	-	$	8.3
Computer system conversion and other integration expenses		2.5		-		2.5
Costs associated with pending spin-off of wireline operations		-		8.7		8.7
Total integration expenses and other charges	$	10.8	$	8.7	$	19.5

The Company incurred $10.8 million of integration expenses related to its acquisition of Western Wireless. These expenses consisted of $8.3 million of rebranding and signage costs and $2.5 million of system conversion and other integration costs. The system conversion and other integration expenses included internal payroll and employee benefit costs, contracted services, relocation expenses and other programming costs incurred in converting Western Wireless' customer billing and operational support systems to Alltel's internal systems, a process which was completed during the first quarter of 2006. In connection with the spin-off and merger of Alltel's wireline business with Valor, Alltel incurred $8.7 million of incremental costs, primarily consisting of special termination benefits payable to two executives, who will be joining the new wireline company formed by the merger of Alltel's wireline business with Valor. As a result of the spin-off, Alltel's supplemental executive retirement plan was amended to provide for the immediate pay out of the accrued supplemental retirement benefits earned by the two executives at the time the spin-off is consummated. The special termination benefits, including a corresponding settlement loss, are being recognized ratably over the first six months of 2006 and totaled $5.5 million in the first quarter of 2006. Costs incurred associated with the spin-off also included $2.7 million in additional consulting and legal fees.

At March 31, 2006, the remaining unpaid liability related to Alltel's integration and restructuring activities consisted of investment banker, audit, consulting and legal fees of $33.1 million, integration costs of $2.6 million and lease and contract termination costs of $0.2 million. Cash outlays for the remaining unpaid liability will be disbursed over the next 12 months and will be funded from operating cash flows. (See Note 8 to the unaudited interim consolidated financial statements for additional information regarding the integration expenses and other charges.)

Non-Operating Income, Net

	Three Months Ended March 31,			
(Millions)		2006		2005
Equity earnings in unconsolidated partnerships	$	12.9	$	10.7
Minority interest in consolidated partnerships		(13.9)		(18.3)

Other income, net		11.9		120.7
Non-operating income, net	$	10.9	$	113.1

As indicated in the table above, non-operating income, net decreased $102.2 million in the three months ended March 31, 2006, as compared to the same period in 2005. The increase in equity earnings in unconsolidated partnerships of $2.2 million primarily resulted from improved operating results in those markets in which the Company owns a minority interest. The decrease in minority interest expense of $4.4 million primarily reflected the effects of Alltel's acquisitions during the first quarter of 2006 of the remaining ownership interests in wireless properties in North Carolina, South Carolina and Wisconsin. Other income, net in the three month period of 2005 included a special cash dividend received on the Company's investment in Fidelity National Financial, Inc. ("Fidelity National") common stock. On March 9, 2005, Fidelity National declared a special $10 per share cash dividend to Fidelity National stockholders. The special cash dividend of $111.0 million was paid to Alltel on March 28, 2005.

On April 6, 2005, Alltel completed the sale of all of its shares of Fidelity National common stock to Goldman Sachs for $350.8 million in cash. Alltel had originally acquired the Fidelity National shares as partial consideration in connection with the April 1, 2003 sale of Alltel's financial services business to Fidelity National.

Compared to the same period of 2005, other income, net in 2006 included additional interest income earned on the Company's cash and short-term investments of $4.6 million due to significant growth in Alltel's available cash on hand following the May 17, 2005 issuance of common stock to settle the purchase contract portion of the Company's mandatorily convertible units. As more fully discussed in Note 5 to the unaudited interim consolidated financial statements, during 2002, Alltel issued 27.7 million equity units which included a purchase contract that obligated the holder to purchase, and obligated Alltel to sell, on May 17, 2005, a variable number of newly-issued Alltel common shares at a price of $50 per share. Upon settlement of the purchase contract obligation, Alltel issued 24.5 million common shares and received proceeds of $1,385.0 million.

Interest Expense

Interest expense increased $2.3 million, or 3 percent, in the three month period ended March 31, 2006 compared to the same period of 2005. The increase primarily reflected additional interest costs resulting from $950.0 million of incremental commercial paper borrowings outstanding as of March 31, 2006, as compared to March 31, 2005. The incremental commercial paper borrowings were incurred by Alltel to finance a portion of the repayment of Western Wireless' long-term debt subsequent to the merger and the cash portion of the merger consideration, as further discussed below under "Cash Flows-Financing Activities". The increase in interest expense in 2006 attributable to higher commercial paper borrowings was partially offset by favorable effects on interest costs attributable to the April 8, 2005 redemption of $450.0 million, 7.50 percent senior notes and the repayment of $200.0 million 6.75 percent senior notes on September 15, 2005. Interest expense for the three month period of 2006 also reflected the effects of the February 17, 2005 remarketing of the senior note portion of Alltel's equity units that reset the annual interest rate on the notes to 4.656 percent from 6.25 percent for periods subsequent to February 17, 2005.

Income Taxes

Income tax expense decreased $11.2 million, or 6 percent, for the three month period ended March 31, 2006, compared to the same period of 2005. The decrease in income tax expense was consistent with the overall decline in the Company's income before income taxes, when compared to the same prior year period, and primarily reflected the effects of the special cash dividend received from Fidelity National in the first quarter of 2005, as previously discussed. The decrease in income before income taxes in 2006 attributable to the absence of the special cash dividend was partially offset by growth in wireless segment income, reflecting the wireless property acquisitions, and growth in Alltel's wireline operations due to the reduction in depreciation rates. Income tax expense for the first quarter of 2006 also reflected an increase in the Company's effective income tax rate, which increased to 38.0 percent in the three months ended March 31, 2006, compared to 36.9 percent for the corresponding period of 2005. The lower effective income tax rate in the first quarter of 2005 included the favorable income tax treatment of the special cash dividend received from Fidelity National.

In determining its quarterly provision for income taxes, Alltel uses an estimated annual effective tax rate, which is based on the Company's expected annual income, statutory rates and tax planning opportunities and reflects Alltel's best estimate of the ultimate outcome of tax examinations and assessments. Significant or unusual items, such as the taxes related to the sale of a business, are separately recognized in the quarter in which they occur.

Net Income and Earnings per Share from Continuing Operations

Net income from continuing operations decreased $33.4 million, or 11 percent, for the three month period ended March 31, 2006, compared to the same period of 2005. Basic and diluted earnings per share from continuing operations decreased 31 percent and 30 percent, respectively, in the three month period of 2006 compared to the same

period of 2005. The decreases in net income and earnings per share in 2006 reflected the absence of the special cash dividend received from Fidelity National in the first quarter of 2005 and the effects of the integration expenses and other charges incurred during the first quarter of 2006 previously discussed. The decreases in basic and diluted earnings per share in the three month period of 2006 also reflected the increases in weighted average share counts due to the equity unit conversion in May 2005 and the Western Wireless merger as further discussed below. The decreases in net income and earnings per share attributable to these factors were partially offset by growth in wireless and wireline segment income. For a further discussion of the wireless and wireline segment operating results, see “Results of Operations by Business Segment” below.

Discontinued Operations

As discussed earlier, as a condition of receiving approval from the DOJ and FCC for its merger with Western Wireless, Alltel agreed to divest certain wireless operations of Western Wireless in 16 markets in Arkansas, Kansas and Nebraska, as well as the "Cellular One" brand. On December 19, 2005, Alltel completed an exchange of wireless properties with U.S. Cellular that included a substantial portion of the divestiture requirements related to the merger. In December 2005, Alltel sold the Cellular One brand to Dobson Cellular Systems, Inc., and on March 24, 2006, Alltel sold the remaining market in Arkansas to Cingular. During the third and fourth quarters of 2005, Alltel completed the sale of Western Wireless' international operations in Georgia, Ghana and Ireland, and on April 28, 2006, Alltel completed the sales of the Western Wireless international operations in Austria and Haiti. Alltel has a pending definitive agreement to sell the international operations in Bolivia, and is also actively pursuing the disposition of the remaining international operations acquired from Western Wireless. Alltel expects to complete the disposition of the remaining international operations during the second quarter of 2006. The acquired international operations and interests of Western Wireless and the domestic market in Arkansas required to be divested by Alltel have been classified as assets held for sale and discontinued operations in the accompanying consolidated financial statements.

The table presented below includes certain summary income statement information related to the international operations and the domestic market in Arkansas to be divested reflected as discontinued operations for the three months ended March 31, 2006.

(Millions)		
Revenues and sales	$	206.4
Operating expenses		154.6
Operating income		51.8
Minority interest expense in unconsolidated entities		(4.5)
Other expense, net		(0.7)
Pretax income from discontinued operations		46.6
Income tax expense		28.8
Income from discontinued operations	$	17.8

The depreciation of long-lived assets related to the international operations and the domestic markets to be divested ceased as of August 1, 2005, the date of the Western Wireless merger with Alltel. The cessation of depreciation had the effect of reducing operating expenses by approximately $17.4 million in the first quarter of 2006. (See Note 10 to the unaudited interim consolidated financial statements for additional information regarding the discontinued operations.)

Weighted Average Common Shares Outstanding

The weighted average number of common shares outstanding increased 28 percent in the three month period ended March 31, 2006, compared to the same period of 2005. The increase primarily reflected the issuance of approximately 54.3 million Alltel common shares to effect the August 1, 2005 merger with Western Wireless and the issuance of 24.5 million Alltel common shares to settle the purchase contract portion of the Company's equity units on May 17, 2005.

RESULTS OF OPERATIONS BY BUSINESS SEGMENT

Communications-Wireless Operations

	Three Months Ended March 31,	
(Millions, customers in thousands)	2006	2005
Revenues and sales:		
Service revenues	$ 1,638.8	$ 1,274.4
Product sales	118.6	77.6
Total revenues and sales	1,757.4	1,352.0
Costs and expenses:		
Cost of services	537.9	405.7
Cost of products sold	204.4	148.8
Selling, general, administrative and other	413.1	322.4
Depreciation	246.5	189.8
Total costs and expenses	1,401.9	1,066.7
Segment income	$ 355.5	$ 285.3
Customers	10,827.1	8,801.3
Average customers	10,731.4	8,704.6
Gross customer additions (a)	805.5	723.7
Net customer additions (a)	164.7	174.8
Market penetration	14.0%	13.8%
Postpay customer churn	1.66%	1.72%
Total churn	2.00%	2.11%
Retail minutes of use per customer per month (b)	610	547
Retail revenue per customer per month (c)	$46.21	$45.31
Average revenue per customer per month (d)	$50.90	$48.80
Cost to acquire a new customer (e)	$352	$306

Notes:

(a) Includes the effects of acquisitions. Excludes reseller customers for all periods presented.

(b) Represents the average monthly minutes that Alltel’s customers use on both the Company’s network and while roaming on other carriers’ networks.

(c) Retail revenue per customer is calculated by dividing wireless retail revenues by average customers for the period. A reconciliation of the revenues used in computing retail revenue per customer per month was as follows for the three month periods ended March 31:

	Three Months Ended	
(Millions)	2006	2005
Service revenues	$ 1,638.8	$ 1,274.4
Less wholesale revenues	(151.0)	(91.1)
Total retail revenues	$ 1,487.8	$ 1,183.3

(d)

Average revenue per customer per month is calculated by dividing wireless service revenues by average customers for the period.

(e) Cost to acquire a new customer is calculated by dividing the sum of product sales, cost of products sold and sales and marketing expenses (included within "Selling, general, administrative and other"), as reported above, by the number of internal gross customer additions in the period. Customer acquisition costs exclude amounts related to the Company's customer retention efforts. A reconciliation of the revenues, expenses and customer additions used in computing cost to acquire a new customer was as follows for the three month periods ended March 31:

	Three Months Ended	
(Millions, customers in thousands)	2006	2005
Product sales	$ (65.2)	$ (49.9)
Cost of products sold	95.1	69.7
Sales and marketing expense	253.7	185.0
Total costs incurred to acquire new customers	$ 283.6	$ 204.8
Gross customer additions, excluding acquisitions	805.5	669.7
Cost to acquire a new customer	$352	$306

The total number of wireless customers served by Alltel increased by 2,026,000 customers, or 23 percent, during the twelve month period ended March 31, 2006. As previously discussed, on August 1, 2005, Alltel completed the acquisition of Western Wireless . During the last nine months of 2005, Alltel also exchanged certain wireless properties with Cingular and U.S. Cellular. The acquired properties accounted for approximately 1,640,000 of the overall increase in wireless customers during the twelve month period ended March 31, 2006. Excluding the effects of acquisitions, Alltel added 48,000 net postpay wireless customers and added 105,000 net prepaid customers during the first quarter of 2006. The net gain in prepaid customers reflected continued growth in Simple Freedom, Alltel’s phone-in-the-box prepay service that is sold primarily through Wal-Mart stores and the roll-out of Alltel’s new “U” prepaid wireless service. In the acquired markets, net customer additions for the quarter were 12,000. Sales of Alltel’s higher-yield Total and National Freedom rate plans accounted for approximately 33 percent of the gross additions during the first quarter of 2006. At March 31, 2006, customers on the Company’s Total and National Freedom rate plans represented approximately 47 percent of Alltel’s wireless customer base. Overall, the Company’s wireless market penetration rate (number of customers as a percent of the total population in Alltel’s service areas) increased to 14.0 percent as of March 31, 2006.

The level of customer growth for the remainder of 2006 will be dependent upon the Company’s ability to attract new customers and retain existing customers in a highly competitive marketplace. The Company will continue to focus its efforts on sustaining value-added customer growth by improving service quality and customer satisfaction, managing its distribution channels and customer segments, offering attractively priced rate plans and new or enhanced services and other features, selling additional services to existing customers, integrating acquired operations, and pursuing strategic acquisitions, such as the pending acquisition of Midwest Wireless previously discussed.

The Company continues to focus its efforts on lowering postpay customer churn (average monthly rate of customer disconnects). To improve customer retention, Alltel continues to upgrade its telecommunications network in order to offer expanded network coverage and quality and to provide enhanced service offerings to its customers. In addition, the Company has increased the number of its customers under contract through the offering of competitively priced rate plans, proactively analyzing customer usage patterns and migrating customers to newer digital handsets. The Company believes that its improvements in customer service levels, digital network expansion and proactive retention efforts contributed to the decrease in postpay customer churn in the three month period of 2006 compared to the same period of 2005. Primarily due to the success of the Simple Freedom and “U” prepaid product offerings and the resulting improvement in prepay churn rates, total churn decreased 11 basis points in the first quarter of 2006 from the same period a year ago.

Wireless revenues and sales increased $405.4 million, or 30 percent, and service revenues increased $364.4 million, or 29 percent, for the three month period ended March 31, 2006, compared to the same period of 2005. The acquisitions of wireless properties previously discussed accounted for approximately $270.4 million of the overall increase in service revenues in 2006. In addition to the effects of the acquisitions, service revenues also reflected an increase in wireless access revenues, which increased $55.5 million in the three months ended March 31, 2006, as compared to same period a year ago, primarily driven by nonacquisition-related customer growth and increased revenues derived from the Company’s Simple Freedom and ”U” prepaid service offerings. Service revenues for 2006 also reflected growth in revenues derived from wireless data services, including text and picture messaging and downloadable applications, such as music, games, ringtones, wallpaper and office applications. Revenues from data services increased 80 percent, or $37.5 million, in the first three months of 2006, as compared to the same period of 2005, reflecting strong demand for these services.

Wireless service revenues in the first quarter of 2006 also included increases in regulatory and other fee revenues of $14.7 million, which included USF support received by Alltel pursuant to its certification in 23 states as an ETC, and accounted for $5.5 million of the overall increase in regulatory fees in the first quarter of 2006. After deducting the

portion of USF subsidies distributed to its partners in wireless markets operated in partnership with other companies, Alltel expects to receive in 2006, on a quarterly basis, net USF subsidies of approximately $55.0 million in its wireless business. The increase in regulatory fees in the first quarter of 2006 also reflected additional amounts billed to customers to offset costs related to certain regulatory mandates, which increased consistent with the overall growth in customers and also reflected an increase in the contribution factor applicable to universal service funding. Revenues from the sale of wireless equipment protection plans increased $11.9 million in the three month period of 2006 compared to the same prior year period, reflecting customer growth and continued demand for these plans. As compared to the same period of 2005, wholesale wireless revenues also increased $3.4 million in the first quarter of 2006, primarily due to growth in CDMA minutes of use, partially offset by the effects of other carriers migrating traffic to their own networks.

The increase in service revenues in 2006 attributable to increased access revenues from customer growth including the effects of acquisitions, additional revenues earned from data services and equipment protection plans, increased regulatory and other fees, and growth in wholesale revenues were partially offset by a decline of $22.5 million in airtime and retail roaming revenues. In addition, revenues derived from sales of enhanced features, including caller identification, call waiting and voice mail, decreased by $6.5 million in the first quarter of 2006, as compared to the same period in 2005. The decrease in airtime, retail roaming and feature revenues primarily reflected the effects of customers migrating to rate plans with a larger number of packaged minutes that, for a flat monthly service fee, provide customers with a specified number of airtime minutes and include at no extra charge unlimited weekend, nighttime and mobile-to-mobile minutes and certain enhanced features.

Primarily due to Alltel's continued focus on quality customer growth and improvements in data revenues, retail revenue per customer per month and average revenue per customer per month both increased in the first quarter of 2006, compared to the same period of 2005. Retail revenue per customer per month increased 2 percent to $46.21 and average revenue per customer per month increased 4 percent to $50.90. Growth in both retail and average revenue per customer per month in the first quarter of 2006 was affected by an increase in sales of family and prepay rate plans combined with limited ETC revenue growth, trends which Alltel expects to continue throughout the remainder of 2006. Accordingly, growth in service revenues and average revenue per customer per month for the remainder of 2006 will depend upon Alltel's ability to effectively integrate acquired operations and maintain market share in a competitive marketplace by adding new customers, retaining existing customers, increasing customer usage, and continuing to sell data services.

Product sales increased $41.0 million, or 53 percent, in the three month period ended March 31, 2006, as compared to the same period a year ago. The increase in product sales was primarily driven by higher retail prices for wireless handsets that include advanced features, such as picture messaging, and that are capable of downloading music, games, entertainment content, weather and office applications. The acquisitions of wireless properties previously discussed accounted for $14.5 million of the overall increase in product sales in the first quarter of 2006. The increase in product sales in 2006 also reflected the continued retention efforts by the Company focused on migrating existing wireless customers to new wireless technologies.

Cost of services increased $132.2 million, or 33 percent, in the first quarter of 2006, as compared to the same period of 2005. The wireless property acquisitions accounted for approximately $71.6 million of the overall increase in cost of services in 2006. In addition to the effects of the acquisitions, cost of services for 2006 also reflected higher network-related costs of $32.8 million, resulting from increased network traffic due to non-acquisition related customer growth, increased minutes of use and expansion of network facilities. Cost of services in 2006 also included increased regulatory fees of $2.9 million related to various regulatory mandates, including USF, consistent with the growth in revenues derived from regulatory fees discussed above. In addition, cost of services in 2006 also reflected increased wireless customer service expenses of $8.2 million, primarily reflecting additional costs associated with Alltel's retention efforts focused on improving customer satisfaction and reducing postpay churn. Compared to the same period in 2005, payments to data content providers increased $8.0 million in the first quarter of 2006 consistent with the growth in revenues derived from data services discussed above. When compared to the first quarter of 2005, cost of services for 2006 also included additional bad debt expense of $7.7 million, primarily due to non-acquisition growth in customers and increased write-offs associated with early disconnect penalties.

Cost of products sold increased $55.6 million, or 37 percent, for the three month period ended March 31, 2006, as compared to the same period in 2005. The wireless acquisitions discussed above accounted for $27.8 million of the overall increase in cost of products sold in 2006. In addition to the effects of the acquisitions, cost of products sold increased primarily due to increased sales of higher-priced wireless handsets and the Company's continuing customer retention efforts, which include subsidizing the cost of new handsets provided to existing customers before the

expiration of their service contracts.

Selling, general, administrative and other expenses increased $90.7 million, or 28 percent, in the first quarter of 2006, as compared to the same period of 2005. The wireless property acquisitions accounted for $64.4 million of the overall increase in these expenses in the first quarter of 2006. In addition to the effects of the acquisitions, selling, general, administrative and other operating expenses for 2006 also reflected increased commission costs of $15.7 million consistent with the significant increase in gross customer additions for the quarter. Selling, general, administrative and other expenses also included increased advertising costs of $9.6 million attributable to the Company’s continued efforts to promote the Alltel brand. The increase in selling, general, administrative and other expenses in 2006 also included $6.5 million of incremental stock-based compensation expense, primarily related to the Company’s adoption of SFAS No. 123(R).

Depreciation expense increased $56.7 million, or 30 percent, for the three month period ended March 31, 2006 compared to the same period of 2005. The increase in depreciation expense in 2006 was primarily due to the wireless property acquisitions which accounted for $41.5 million of the overall increase in depreciation expense in the first quarter of 2006. Additionally, growth in wireless plant in service, consistent with Alltel's plans to expand and upgrade its network facilities, also contributed to the overall increase in 2006.

Primarily as a result of growth in revenues and sales discussed above, wireless segment income increased $70.2 million, or 25 percent, for the three month period ended March 31,2006, as compared to the same period in 2005. The wireless property acquisitions accounted for $79.5 million of the overall increase in wireless segment income in 2006. The growth in segment income in 2006 attributable to the acquisitions was partially offset by increased network costs attributable to the significant growth in customer usage, higher customer acquisition costs consistent with the growth in gross postpay customer additions and additional costs associated with the Company's retention efforts and initiatives designed to improve customer satisfaction and reduce postpay churn.

The cost to acquire a new wireless customer represents sales, marketing and advertising costs and the net equipment cost, if any, for each new customer added. The increase in cost to acquire a new customer in 2006 primarily reflected additional advertising and commissions costs, as previously discussed. In addition, net equipment cost increased $10.1 million from the first quarter of 2005 consistent with selling higher-cost, wireless handsets that offer advanced features and capabilities. For the three month period ended March 31, 2006, approximately 57 percent of the gross customer additions came from Alltel's internal distribution channels, compared to approximately 62 percent in 2005. Alltel's internal distribution channels include Company retail stores and kiosks located in shopping malls, other retail outlets and mass merchandisers. Incremental sales costs at a Company retail store or kiosk are significantly lower than commissions paid to dealers. Although Alltel intends to manage the costs of acquiring new customers during 2006 by continuing to enhance its internal distribution channels, the Company will also continue to utilize its large dealer network.

As more fully discussed in Note 2 to the interim unaudited consolidated financial statements, wireless segment income does not include the effects of amortization expense related to intangible assets recorded in connection with the acquisition of wireless properties. Amortization expense related to the wireless operations amounted to $45.5 million and $13.8 million for the three months ended March 31, 2006 and 2005, respectively. For business segment reporting purposes, this amortization expense has been included in corporate expenses.

Set forth below is a summary of the integration expenses and other charges related to the wireless operations that were not included in the determination of segment income for the three months ended March 31, 2006:

(Millions)		
Rebranding and signage costs	$	8.3
Computer system conversion and other integration expenses		2.5
Total integration expenses and other charges	$	10.8

Regulatory Matters-Wireless Operations

Regulatory Oversight

Alltel is subject to regulation by the FCC as a provider of Commercial Mobile Radio Services ("CMRS"). The FCC's regulatory oversight consists of ensuring that wireless service providers are complying with the Communications Act of 1934, as amended (the "Communications Act"), and the FCC's regulations governing technical standards, spectrum usage, license requirements, market structure, consumer protection, including public safety issues like enhanced 911 emergency service ("E-911") and the Communications Assistance for Law Enforcement Act ("CALEA"), and

environmental matters governing tower siting. State public service commissions are pre-empted under the Communications Act from regulatory oversight of wireless carriers' market entry and retail rates, but they are entitled to address certain terms and conditions of service offered by wireless service providers. Recently, various state public service commissions have sought to regulate wireless carriers' terms and conditions of service. At this time, the Company cannot estimate the impact that increased state regulatory oversight would have on its operations in the event state pub