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

# FORM 10-Q

**(Mark One)**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF1934**

**For the quarterly period ended September 30, 2019**

**or**

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

**For the transition period from____________ to ______________________**

**Commission File Number: 001-38341**

## ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.

(Exact name of registrant as specified in its charter)

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

**600 Telephone Avenue, Anchorage, Alaska 99503-6091**
(Address of principal executive offices) (Zip Code)
**(907) 297-3000**
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class | Trading Symbol | Name of each exchange on which registered |
|---|---|---|
| Common Stock, par value $.01 per share | ALSK | The Nasdaq Stock Market LLC |

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

**Yes** **No** ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

**Yes** **No** ☐

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

Large accelerated filer [ ] Accelerated filer [X] Non-accelerated filer [ ] Smaller reporting company [X]
Emerging growth company [ ]

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

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

**Yes** ☐ **No**

As of October 31, 2019, there were outstanding 53,011,579 shares of Common Stock, $.01 par value, of the registrant.

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**PART I. FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS**

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

| | September 30, 2019 | December 31, 2018 |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 25,046 | $ 13,351 |
| Restricted cash | 1,631 | 1,634 |
| Short-term investments | 134 | 134 |
| Accounts receivable, net of allowance of $4,807 and $3,936 | 25,438 | 31,472 |
| Materials and supplies | 9,185 | 6,737 |
| Prepayments and other current assets | 13,191 | 12,169 |
| Total current assets | 74,625 | 65,497 |
| Property, plant and equipment | 1,414,940 | 1,390,622 |
| Less: accumulated depreciation and amortization | (1,036,422) | (1,017,442) |
| Property, plant and equipment, net | 378,518 | 373,180 |
| Deferred income taxes | - | 498 |
| Operating lease right of use assets | 80,748 | - |
| Other assets | 12,354 | 16,010 |
| Total assets | $ 546,245 | $ 455,185 |
| **Liabilities and Stockholders' Equity** | | |
| Current liabilities: | | |
| Current portion of long-term obligations | $ 5,674 | $ 2,289 |
| Accounts payable, accrued and other current liabilities | 40,317 | 40,957 |
| Advance billings and customer deposits | 3,791 | 4,024 |
| Operating lease liabilities - current | 2,626 | - |
| Total current liabilities | 52,408 | 47,270 |
| Long-term obligations, net of current portion | 171,541 | 168,023 |
| Deferred income taxes | 2,823 | 2,315 |
| Operating lease liabilities - noncurrent | 78,362 | - |
| Other long-term liabilities, net of current portion | 71,250 | 67,827 |
| Total liabilities | 376,384 | 285,435 |
| Commitments and contingencies | | |
| Common stock, $.01 par value; 145,000 authorized; 54,012 issued and 53,012 outstanding at September 30, 2019; 53,268 issued and outstanding at December 31, 2018 | 540 | 533 |
| Treasury stock, 1,000 shares at cost | (1,812) | - |
| Additional paid in capital | 160,931 | 160,514 |
| Retained earnings | 12,723 | 10,439 |
| Accumulated other comprehensive loss | (3,384) | (2,675) |
| Total Alaska Communications stockholders' equity | 168,998 | 168,811 |
| Noncontrolling interest | 863 | 939 |
| Total stockholders' equity | 169,861 | 169,750 |
| Total liabilities and stockholders' equity | $ 546,245 | $ 455,185 |

*See Notes to Condensed Consolidated Financial Statements*

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

| | Three Months Ended September 30, 2019 | Three Months Ended September 30, 2018 | Nine Months Ended September 30, 2019 | Nine Months Ended September 30, 2018 |
|---|---|---|---|---|
| Operating revenues | $ 59,128 | $ 58,229 | $ 173,432 | $ 173,779 |
| Operating expenses: | | | | |
| Cost of services and sales (excluding depreciation and amortization) | 26,785 | 27,220 | 78,768 | 79,595 |
| Selling, general and administrative | 16,832 | 16,879 | 52,206 | 49,398 |
| Depreciation and amortization | 9,546 | 8,352 | 27,425 | 25,336 |
| Loss on disposal of assets, net | 198 | 15 | 101 | 56 |
| Total operating expenses | 53,361 | 52,466 | 158,500 | 154,385 |
| Operating income | 5,767 | 5,763 | 14,932 | 19,394 |
| Other income and (expense): | | | | |
| Interest expense | (2,997) | (3,286) | (9,149) | (10,191) |
| Loss on extinguishment of debt | - | - | (2,830) | - |
| Interest income | 121 | 36 | 291 | 74 |
| Other income, net | 192 | 66 | 192 | 79 |
| Total other income and (expense) | (2,684) | (3,184) | (11,496) | (10,038) |
| Income before income tax expense | 3,083 | 2,579 | 3,436 | 9,356 |
| Income tax expense | (1,084) | (774) | (1,228) | (2,080) |
| Net income | 1,999 | 1,805 | 2,208 | 7,276 |
| Less net loss attributable to noncontrolling interest | (23) | (12) | (76) | (84) |
| Net income attributable to Alaska Communications | 2,022 | 1,817 | 2,284 | 7,360 |
| Other comprehensive (loss) income: | | | | |
| Minimum pension liability adjustment | (69) | 55 | (30) | 169 |
| Income tax effect | 19 | (16) | 8 | (48) |
| Amortization of defined benefit plan loss | (192) | (13) | 51 | 169 |
| Income tax effect | 55 | 4 | (14) | (48) |
| Interest rate swap marked to fair value | (396) | 17 | (362) | 429 |
| Income tax effect | 112 | (5) | 102 | (123) |
| Reclassification to interest expense | (197) | (136) | (648) | (258) |
| Income tax effect | 56 | 39 | 184 | 74 |
| Total other comprehensive (loss) income | (612) | (55) | (709) | 364 |
| Total comprehensive income attributable to Alaska Communications | 1,410 | 1,762 | 1,575 | 7,724 |
| Net loss attributable to noncontrolling interest | (23) | (12) | (76) | (84) |
| Total other comprehensive income attributable to noncontrolling interest | - | - | - | - |
| Total comprehensive loss attributable to noncontrolling interest | (23) | (12) | (76) | (84) |
| Total comprehensive income | $ 1,387 | $ 1,750 | $ 1,499 | $ 7,640 |
| Net income per share attributable to Alaska Communications: | | | | |
| Basic | $ 0.04 | $ 0.03 | $ 0.04 | $ 0.14 |
| Diluted | $ 0.04 | $ 0.03 | $ 0.04 | $ 0.14 |
| Weighted average shares outstanding: | | | | |
| Basic | 53,328 | 53,184 | 53,503 | 52,994 |
| Diluted | 53,991 | 54,116 | 54,405 | 53,887 |

*See Notes to Condensed Consolidated Financial Statements*

**ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.**
**Condensed Consolidated Statements of Stockholders' Equity**
**(Unaudited, In Thousands Except Per Share Amounts)**

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | **2019** | **2018** | **2019** | **2018** |
| **Number of Common Shares Issued and Outstanding** | | | | |
| Balance at beginning of period | 53,774 | 53,184 | 53,268 | 52,526 |
| Issuance of common stock pursuant to stock plans, $.01 par | 119 | - | 744 | 658 |
| Purchases of common stock, $.01 par | (881) | - | (1,000) | - |
| Balance at end of period | 53,012 | 53,184 | 53,012 | 53,184 |
| **Total Stockholders' Equity - Beginning Balance** | $ 169,804 | $ 165,646 | $ 169,750 | $ 154,510 |
| **Common Stock** | | | | |
| Balance at beginning of period | 540 | 532 | 533 | 525 |
| Issuance of common stock pursuant to stock plans, $.01 par | - | - | 7 | 7 |
| Balance at end of period | 540 | 532 | 540 | 532 |
| **Treasury Stock** | | | | |
| Balance at beginning of period | (205) | - | - | - |
| Purchases of 1,000 shares of common stock, $.01 par | (1,607) | - | (1,812) | - |
| Balance at end of period | (1,812) | - | (1,812) | - |
| **Additional Paid In Capital** | | | | |
| Balance at beginning of period | 160,654 | 159,230 | 160,514 | 158,969 |
| Stock-based compensation | 277 | 642 | 766 | 1,209 |
| Surrender of shares to cover minimum withholding taxes on stock-based compensation | - | - | (448) | (410) |
| Issuance of common stock pursuant to stock plans, $.01 par | - | - | 99 | 104 |
| Balance at end of period | 160,931 | 159,872 | 160,931 | 159,872 |
| **Retained Earnings (Accumulated Deficit)** | | | | |
| Balance at beginning of period | 10,701 | 6,902 | 10,439 | (3,579) |
| Net income attributable to Alaska Communications | 2,022 | 1,817 | 2,284 | 7,360 |
| Cumulative effect of new accounting principles adopted | - | - | - | 4,938 |
| Balance at end of period | 12,723 | 8,719 | 12,723 | 8,719 |
| **Accumulated Other Comprehensive Loss** | | | | |
| Balance at beginning of period | (2,772) | (1,977) | (2,675) | (2,396) |
| Other comprehensive (loss) income | (612) | (55) | (709) | 364 |
| Balance at end of period | (3,384) | (2,032) | (3,384) | (2,032) |
| **Noncontrolling Interest** | | | | |
| Balance at beginning of period | 886 | 959 | 939 | 991 |
| Net loss attributable to noncontrolling interest | (23) | (12) | (76) | (84) |
| Contributions from noncontrolling interest | - | - | - | 40 |
| Balance at end of period | 863 | 947 | 863 | 947 |
| **Total Stockholders' Equity - Ending Balance** | $ 169,861 | $ 168,038 | $ 169,861 | $ 168,038 |

*See Notes to Condensed Consolidated Financial Statements*

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

| | Nine Months Ended September 30, 2019 | Nine Months Ended September 30, 2018 |
|---|---|---|
| Cash Flows from Operating Activities: | | |
| Net income | $ 2,208 | $ 7,276 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 27,425 | 25,336 |
| Loss on disposal of assets, net | 101 | 56 |
| Amortization of debt issuance costs and debt discount | 911 | 1,022 |
| Loss on extinguishment of debt | 2,830 | - |
| Amortization of deferred capacity revenue | (3,400) | (2,997) |
| Stock-based compensation | 766 | 1,209 |
| Income tax expense | 1,228 | 2,080 |
| Charge for uncollectible accounts | 275 | 2,371 |
| Amortization of right-of-use assets | 1,716 | - |
| Other non-cash expense, net | 52 | 168 |
| Income taxes receivable | (65) | (37) |
| Changes in operating assets and liabilities | 8,573 | 10,395 |
| Net cash provided by operating activities | 42,620 | 46,879 |
| | | |
| Cash Flows from Investing Activities: | | |
| Capital expenditures | (31,556) | (25,432) |
| Capitalized interest | (983) | (1,456) |
| Change in unsettled capital expenditures | 583 | (1,811) |
| Proceeds on sale of assets | 20 | 1 |
| Net cash used by investing activities | (31,936) | (28,698) |
| | | |
| Cash Flows from Financing Activities: | | |
| Repayments of long-term debt | (172,903) | (29,164) |
| Proceeds from the issuance of long-term debt | 180,000 | 14,000 |
| Debt issuance costs and discounts | (2,683) | - |
| Cash paid for debt extinguishment | (1,252) | - |
| Cash proceeds from noncontrolling interest | - | 40 |
| Payment of withholding taxes on stock-based compensation | (448) | (410) |
| Purchases of treasury stock | (1,812) | - |
| Proceeds from the issuance of common stock | 106 | 111 |
| Net cash provided (used) by financing activities | 1,008 | (15,423) |
| | | |
| Change in cash, cash equivalents and restricted cash | 11,692 | 2,758 |
| Cash, cash equivalents and restricted cash, beginning of period | 14,985 | 16,168 |
| | | |
| Cash, cash equivalents and restricted cash, end of period | $ 26,677 | $ 18,926 |
| | | |
| Supplemental Cash Flow Data: | | |
| Interest paid | $ 9,236 | $ 10,723 |
| Income taxes paid, net | $ 10 | $ 4 |

*See Notes to Condensed Consolidated Financial Statements*

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

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

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

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

In addition to the wholly-owned subsidiaries, the Company has a fifty percent controlling interest in ACS-Quintillion JV, LLC (“AQ-JV”), a joint venture formed by its wholly-owned subsidiary ACSC and Quintillion Holdings, LLC (“QHL”) in connection with the North Slope fiber optic network. See Note 3 “*Joint Venture*” for additional information.

*Basis of Presentation*

The accompanying unaudited condensed consolidated financial statements and notes included in this Quarterly Report on Form 10-Q have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2018. Certain information and note disclosures normally included in financial statements prepared in accordance with Generally Accepted Accounting Principles in the United States of America (“GAAP”) have been condensed or omitted pursuant to the rules and regulations of the SEC. The Company believes the disclosures made are adequate to make the information presented not misleading.

See Note 10 “*Leases*” for a summary of the Company’s lease accounting policies and related disclosures.

The Company consolidates the financial results of the AQ-JV based on its determination that, for accounting purposes, it holds a controlling financial interest in the joint venture and is the primary beneficiary of this variable interest entity. The Company has accounted for and reported QHL’s fifty percent ownership interest in the joint venture as a noncontrolling interest.

In the opinion of management, the unaudited condensed consolidated financial statements contain all normal, recurring adjustments necessary to present fairly the consolidated financial position, comprehensive income, stockholders’ equity and cash flows for all periods presented. Comprehensive income for the three and nine-month periods ended September 30, 2019, is not necessarily indicative of comprehensive income which might be expected for the entire year or any other interim periods. The balance sheet at December 31, 2018 has been derived from the audited financial statements as of that date but does not include all information and notes required by GAAP for complete financial statements. Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation.

*Employee Termination Benefits*

In the second quarter of 2019, the Company recorded a charge of $1,595 associated with cash-based termination benefits paid or to be paid to is former Chief Executive Officer who separated from the Company effective June 30, 2019. These benefits consist of special termination benefits as defined in Accounting Standards Codification (“ASC”) 712, “*Compensation – Nonretirement Postemployment Benefits*” and include the continuation of salary and certain benefits through December 31, 2019, and the payment of annual cash incentive and long-term cash awards, subject to certain conditions. Payments totaling $1,193 were made in the third quarter of 2019 and the balance will be paid in the fourth quarter of 2019 and in 2020 and 2021. The effect of the former Chief Executive Officer’s separation on the relevant equity awards were accounted for in accordance with ASC 718, “*Compensation – Stock Compensation.*” See Note 12 “*Stock Incentive Plans*.”

*Share Repurchase Program*

In the second quarter of 2017, the Company's Board of Directors authorized a share repurchase program pursuant to which the Company may repurchase up to $10,000 of its common stock effective March 13, 2017 through December 31, 2019. Under the program, repurchases may be conducted through open market purchases or through privately-negotiated transactions in accordance with all applicable securities laws and regulations, including through Rule 10b5-1 trading plans. The timing and amount of repurchases will be determined based on the Company's evaluation of its financial position including liquidity, the trading price of its stock, debt covenant restrictions, general business and market conditions and other factors. The Company intends to use cash on hand to fund share repurchases subject to, among other things, federal and state securities, corporate and other laws and regulations, and the Company's financing arrangements. Share repurchases are accounted for as treasury stock.

As of September 30, 2019, the Company had repurchased 1,000,000 shares under the program at a weighted average price of $1.81 per share with an aggregate value of $1,812.

*Use of Estimates*

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

*Recently Adopted Accounting Pronouncements*

Effective January 1, 2019, the Company adopted ASC 842, "*Leases*" ("ASC 842") on a modified retrospective basis. Accordingly, information presented for periods prior to 2019 have not been recast. Adoption of ASC 842 resulted in the establishment of right-of-use ("ROU") assets and associated liabilities totaling $82,020 representing the Company's right to use the underlying assets and the present value of the future lease payments over the terms of the Company's operating leases. The Company elected the package of practical expedients, which among other things, does not require reassessment of lease classification. Adoption of ASC 842 did not have a material effect on the Company's finance leases and its consolidated statements of Comprehensive Income and Cash Flows. See Note 10 "*Leases*" for a summary of the Company's lease accounting policies and other disclosures required under ASC 842.

Effective January 1, 2019, the Company adopted Accounting Standards Update ("ASU") No. 2017-12, "*Derivatives and Hedging (Topic 815), Targeted Improvements to Accounting for Hedging Activities*" (ASU 2017-12") on a prospective basis. The new guidance eliminates the requirement to separately measure and report hedge ineffectiveness and, for qualifying hedges, requires the entire change in the fair value of the hedging instrument to be presented in the same income statement line as the hedged item. The Company's hedges, consisting of a pay-fixed, receive-floating interest rate swaps, are fully effective. Therefore, adoption of ASU 2017-12 did not have any impact on the Company's financial statements. See Note 4 "Fair Value Measurements and Derivative Financial Instruments" for the disclosures required by ASU 2017-12.

Effective January 1, 2019, the Company adopted ASU No. 2018-16, "*Derivatives and Hedging (Topic 815), Inclusion of the Secured Overnight Financing Rate (SOFR) Overnight Index Swap (OIS) Rate as a Benchmark Interest Rate for Hedge Accounting Purposes*" ("ASU 2018-16"). Permitting use of the OIS rate based on SOFR as a U.S. benchmark interest rate for hedge accounting purposes will facilitate the London Interbank Offered Rate ("LIBOR") to SOFR transition and provide sufficient lead time for entities to prepare for changes to interest rate risk hedging strategies. ASU 2018-16 was required to be adopted concurrently with ASU 2017-12. Adoption of ASU 2018-16 did not affect the Company's financial statements and related disclosures.

*Accounting Pronouncements Issued Not Yet Adopted*

In June 2016, the Financial Accounting Standards Board ("FASB") issued ASU No. 2016-13, *"Financial Instruments – Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments"* ("ASU 2016-13"). The amendments in ASU 2016-13, and subsequent amendments, introduce a forward-looking approach, based on expected losses, to estimate credit losses on certain types of financial instruments, including trade receivables. ASU 2016-13 is expected to be effective for the Company's 2023 fiscal year. The Company is evaluating the effect ASU 2016-13 will have on its financial statements and related disclosures.

In August 2018, the FASB issued ASU No. 2018-13, "*Fair Value Measurement (Topic 820), Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement*" ("ASU 2018-13"). The amendments in ASU 2018-13 are intended to improve the effectiveness of fair value measurement disclosures in the notes to the financial statements. The new guidance eliminates the requirement to disclose (i) the amount and reasons for transfers between Level 1 and Level 2 of the fair value hierarch; (ii) the policy for timing of transfers between levels; and (iii) the valuation processes for Level 3 fair value measurements. The new guidance also requires the disclosure of (i) changes in unrealized gains and losses for the period included in other comprehensive income for recurring Level 3 fair value measurements held at the end of the reporting period; and (ii) the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements. ASU 2018-13 is effective for fiscal years beginning after December 15, 2019 and early adoption is permitted. The Company is evaluating ASU 2018-13 and, based on its existing assets and liabilities measured at fair value, does not currently believe that adoption will have a material effect on its financial statements and related disclosures.

In August 2018, the FASB issued ASU No. 2018-14, "*Compensation – Retirement Benefits – Defined Benefit Plans – General (Subtopic 715-20), Disclosure Framework – Changes to the Disclosure Requirements for Defined Benefit Plans*" ("ASU 2018-14"). The amendments in ASU 2018-14 are intended to improve the effectiveness of disclosures in the notes to the financial statements about employer-sponsored defined benefit plans. The new guidance eliminates, among other items, the requirement to disclose the amounts in accumulated other comprehensive income expected to be recognized as components of net periodic benefit cost over the next fiscal year. Expanded disclosures required under ASU 2018-14 include an explanation of the reasons for significant gains and losses related to changes in the benefit obligation for the period. ASU 2018-14 is effective for fiscal years beginning after December 15, 2020 and early adoption is permitted. The Company is evaluating the effect ASU 2018-14 will have on its disclosures.

In August 2018, the FASB issued ASU No. 2018-15, "*Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40), Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*" ("ASU 2018-15"). The amendments in ASU 2018-15 align the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with those incurred to develop or obtain internal-use software, including hosting arrangements that include an internal-use software license. ASU 2018-15 is effective for fiscal years beginning after December 15, 2019 and early adoption is permitted. The Company is evaluating the effect ASU 2018-15 will have on its financial statements and related disclosures.

## 2. REVENUE RECOGNITION

**Revenue Recognition Policies**

*Revenue Accounted for in Accordance with ASC 606, "Revenue from Contracts with Customers" ("ASC 606")*

At contract inception, the Company assesses the goods and services promised to the customer and identifies the performance obligation for each promise to transfer a good or service that is distinct. The Company considers all obligations whether they are explicitly stated in the contract or are implied by customary business practices.

**(Unaudited, In Thousands Except Per Share Amounts)**

The Company's broadband and voice revenue includes service, installation and equipment charges. Managed IT revenues include the sale, configuration and installation of equipment and the subsequent provision of ongoing IT services. The Company enters into contracts with its rural health care customers and is subject to various regulatory requirements associated with the provision of these services. Revenues associated with rural health care customers are recognized based on the amount the Company expects to collect as evidenced in its contract with the customer and the Company's and customer's agreement with the Federal Communications Commission ("FCC") as the relevant service is provided. Regulatory access revenue includes (i) special access, which is primarily access to dedicated circuits sold to wholesale customers, substantially all of which is generated from interstate services; and (ii) cellular access, which is the transport of tariffed local network services between switches for cellular companies based on individually negotiated contracts. Regulatory access revenue is recognized as the service is provided to the customer.

*Revenue Accounted for in Accordance with Other Guidance*

Deferred revenue capacity liabilities are established for indefeasible rights of use ("IRUs") on the Company's network provided to third parties and are typically accounted for as operating leases. Regulatory access revenue includes interstate and intrastate switched access, consisting of services based primarily on originating and terminating access minutes from other carriers. High-cost support revenue consists of interstate revenue streams structured by federal regulatory agencies that allow the Company to recover its cost of providing universal service in Alaska.

**Disaggregation of Revenue**

The following tables provide the Company's revenue disaggregated on the basis of its primary markets, customers, products and services for the three and nine-month periods ended September 30, 2019 and 2018:

| | Three Months Ended September 30, 2019 | | | Nine Months Ended September 30, 2019 | | |
|---|---|---|---|---|---|---|
| | **Accounted for Under ASC 606** | **Accounted for Under Other Guidance** | **Total Revenue** | **Accounted for Under ASC 606** | **Accounted for Under Other Guidance** | **Total Revenue** |
| Business and Wholesale Revenue | | | | | | |
| Business broadband | $ 15,595 | $ - | $ 15,595 | $ 46,181 | $ - | $ 46,181 |
| Business voice and other | 6,889 | - | 6,889 | 20,546 | - | 20,546 |
| Managed IT services | 1,789 | - | 1,789 | 4,965 | - | 4,965 |
| Equipment sales and installations | 942 | - | 942 | 2,830 | - | 2,830 |
| Wholesale broadband | 9,550 | - | 9,550 | 26,821 | - | 26,821 |
| Wholesale voice and other | 1,870 | - | 1,870 | 4,688 | - | 4,688 |
| Operating leases and other deferred revenue | - | 2,104 | 2,104 | - | 6,241 | 6,241 |
| Total Business and Wholesale Revenue | 36,635 | 2,104 | 38,739 | 106,031 | 6,241 | 112,272 |
| Consumer Revenue | | | | | | |
| Broadband | 6,718 | - | 6,718 | 19,880 | - | 19,880 |
| Voice and other | 2,567 | - | 2,567 | 7,947 | - | 7,947 |
| Total Consumer Revenue | 9,285 | - | 9,285 | 27,827 | - | 27,827 |
| Regulatory Revenue | | | | | | |
| Access (1) | 5,005 | - | 5,005 | 15,040 | - | 15,040 |
| Access (2) | - | 1,176 | 1,176 | - | 3,523 | 3,523 |
| High-cost support | - | 4,923 | 4,923 | - | 14,770 | 14,770 |
| Total Regulatory Revenue | 5,005 | 6,099 | 11,104 | 15,040 | 18,293 | 33,333 |
| Total Revenue | $ 50,925 | $ 8,203 | $ 59,128 | $ 148,898 | $ 24,534 | $ 173,432 |

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

| | Three Months Ended September 30, 2018 | | | Nine Months Ended September 30, 2018 | | |
|---|---|---|---|---|---|---|
| | Accounted for Under ASC 606 | Accounted for Under Other Guidance | Total Revenue | Accounted for Under ASC 606 | Accounted for Under Other Guidance | Total Revenue |
| Business and Wholesale Revenue | | | | | | |
| Business broadband | $ 15,309 | $ - | $ 15,309 | $ 45,859 | $ - | $ 45,859 |
| Business voice and other | 7,199 | - | 7,199 | 21,088 | - | 21,088 |
| Managed IT services | 1,480 | - | 1,480 | 3,936 | - | 3,936 |
| Equipment sales and installations | 1,488 | - | 1,488 | 3,870 | - | 3,870 |
| Wholesale broadband | 7,624 | - | 7,624 | 23,475 | - | 23,475 |
| Wholesale voice and other | 1,525 | - | 1,525 | 4,455 | - | 4,455 |
| Operating leases and other deferred revenue | - | 1,740 | 1,740 | - | 4,923 | 4,923 |
| Total Business and Wholesale Revenue | 34,625 | 1,740 | 36,365 | 102,683 | 4,923 | 107,606 |
| Consumer Revenue | | | | | | |
| Broadband | 6,539 | - | 6,539 | 19,726 | - | 19,726 |
| Voice and other | 2,719 | - | 2,719 | 8,355 | - | 8,355 |
| Total Consumer Revenue | 9,258 | - | 9,258 | 28,081 | - | 28,081 |
| Regulatory Revenue | | | | | | |
| Access (1) | 5,944 | - | 5,944 | 18,203 | - | 18,203 |
| Access (2) | - | 1,738 | 1,738 | - | 5,118 | 5,118 |
| High-cost support | - | 4,924 | 4,924 | - | 14,771 | 14,771 |
| Total Regulatory Revenue | 5,944 | 6,662 | 12,606 | 18,203 | 19,889 | 38,092 |
| Total Revenue | $ 49,827 | $ 8,402 | $ 58,229 | $ 148,967 | $ 24,812 | $ 173,779 |

(1) Includes customer ordered service and special access.
(2) Includes carrier of last resort and carrier common line.

Business broadband revenue includes revenue associated with rural health care customers. Consumer voice and other revenue includes revenue associated with the FCC's Lifeline program.

**Timing of Revenue Recognition**

Revenue accounted for in accordance with ASC 606 consisted of the following for the three and nine-month periods ended September 30, 2019 and 2018:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2019 | 2018 | 2019 | 2018 |
| Services transferred over time | $ 44,978 | $ 42,395 | $ 131,028 | $ 126,894 |
| Goods transferred at a point in time | 942 | 1,488 | 2,830 | 3,870 |
| Regulatory access revenue (1) | 5,005 | 5,944 | 15,040 | 18,203 |
| Total revenue | $ 50,925 | $ 49,827 | $ 148,898 | $ 148,967 |

(1) Includes customer ordered service and special access.

(Unaudited, In Thousands Except Per Share Amounts)

**Transaction Price Allocated to Remaining Performance Obligations**

The aggregate amount of the transaction price allocated to the remaining performance obligations for contracts with customers that are unsatisfied, or partially unsatisfied, accounted for in accordance with ASC 606 was approximately $85,212 at September 30, 2019. Revenue will be recognized as the Company satisfies the associated performance obligations. For equipment delivery, installation and configuration, and certain managed IT services, which comprise approximately $1,425 of the total, the performance obligation is currently expected to be satisfied during the next twelve months. For business broadband, voice and other managed IT services, which comprise approximately $83,787 of the total, the performance obligation will be satisfied as the service is provided over the terms of the contracts, which range from one to ten years. The Company's agreements with its consumer customers are typically on a month-to-month basis. Therefore, the Company's provision of future service to these customers is not reflected in the above discussion of future performance obligations.

**Contract Assets and Liabilities**

The Company incurs certain incremental costs to obtain contracts that it expects to recover. These costs consist primarily of sales commissions and other directly related incentive compensation payments (reported as contract additions in the table below) which are dependent upon, and paid upon, successfully entering into individual customer contracts.

The table below provides a reconciliation of the contract assets associated with contracts with customers accounted for in accordance with ASC 606 for the nine-month period ended September 30, 2019. Contract modifications did not have a material effect on contract assets in the nine-month period ended September 30, 2019. Contract assets are classified as "Other assets" on the consolidated balance sheet.

| | | |
|---|---|---|
| Balance at January 1 | $ | 8,052 |
| Contract additions | | 2,192 |
| Amortization | | (2,864) |
| Impairments | | (83) |
| Balance at September 30 | $ | 7,297 |

The Company recorded a charge for uncollectible accounts receivable of $275 in the nine-month period ended September 30, 2019 associated with its contracts with customers. See Note 5 "*Accounts Receivable*."

The table below provides a reconciliation of the contract liabilities associated with contracts with customers accounted for in accordance with ASC 606 for the nine-month period ended September 30, 2019. Contract liabilities consist of deferred revenue and are included in "Accounts payable, accrued and other current liabilities" and "Other long-term liabilities, net of current portion."

| | | |
|---|---|---|
| Balance at January 1 | $ | 2,766 |
| Contract additions | | 1,535 |
| Revenue recognized | | (1,045) |
| Balance at September 30 | $ | 3,256 |

**3. JOINT VENTURE**

The table below provides certain financial information about the AQ-JV included on the Company's consolidated balance sheet at September 30, 2019 and December 31, 2018. Cash may be utilized only to settle obligations of the joint venture. Because the joint venture is an LLC, and the Company has not guaranteed its operations, the joint venture's creditors do not have recourse to the general credit of the Company.

| | 2019 | | 2018 | |
|---|---|---|---|---|
| Cash | $ | 270 | $ | 270 |
| Property, plant and equipment, net of accumulated depreciation of $383 and $309 | $ | 1,758 | $ | 1,832 |

The operating results and cash flows of the joint venture in the three and nine-month periods of 2019 and 2018 were not material to the Company's consolidated financial results.

**(Unaudited, In Thousands Except Per Share Amounts)**

## 4. FAIR VALUE MEASUREMENTS AND DERIVATIVE FINANCIAL INSTRUMENTS

*Fair Value Measurements*

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

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

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

The fair values of cash equivalents, restricted cash, other short-term monetary assets and liabilities and financing leases approximate carrying values due to their nature. The carrying values of the Company's senior credit facilities and other long-term obligations of $179,207 and $172,494 at September 30, 2019 and December 31, 2018, respectively, approximate fair value primarily as a result of the stated interest rates of the 2019 Senior Credit Facility approximating current market rates (Level 2).

The following table presents the Company's financial assets measured at fair value on a recurring basis as of September 30, 2019 and December 31, 2018, at each hierarchical level. There were no transfers into or out of Levels 1 and 2 during the first nine months of 2019:

| | September 30, 2019 | | | | December 31, 2018 | | | |
|---|---|---|---|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 |
| Other assets: | | | | | | | | |
| Interest rate swaps | $ - | $ - | $ - | $ - | $ 458 | $ - | $ 458 | $ - |
| Other long-term liabilities: | | | | | | | | |
| Interest rate swaps | $ 552 | $ - | $ 552 | $ - | $ - | $ - | $ - | $ - |

*Derivative Financial Instruments*

The Company currently uses interest rate swaps to manage variable interest rate risk. At low LIBOR rates, payments under the swaps increase the Company's cash interest expense, and at high LIBOR rates, they have the opposite effect.

The outstanding amount of the swaps as of a period end are reported on the balance sheet at fair value, represented by the estimated amount the Company would receive or pay to terminate the swaps. They are valued using models based on readily observable market parameters for all substantial terms of the contracts and are classified within Level 2 of the fair value hierarchy.

Under the terms of the 2019 Senior Credit Facility, the Company is required to enter into or obtain an interest rate hedge sufficient to effectively fix or limit the interest rate on borrowings under the agreement of a minimum of $90,000 with a weighted average life of at least two years. In 2017, as required under the terms of its 2017 Senior Credit Facility, the Company entered into a pay-fixed, receive-floating interest rate swap in the notional amount of $90,000, with an interest rate of 6.49425%, inclusive of a 5.0% LIBOR spread, and a maturity date of June 28, 2019. Upon repayment of the outstanding principal balance of the 2017 Senior Credit Facility on January 15, 2019, this swap was assigned to the 2019 Senior Credit Facility through its maturity date of June 28, 2019. On June 28, 2019, the Company entered into two pay-fixed, receive-floating, interest rate swaps. Each swap is in the notional amount of $67,500, has an interest rate of 6.1735% inclusive of a 4.5% LIBOR spread, and a maturity date of June 30, 2022. The swaps are with different counter parties. Changes in fair value of interest rate swaps are recorded to accumulated other comprehensive loss and reclassified to interest expense when the hedged transaction is recognized in earnings. Cash payments and receipts associated with interest rate swaps are classified as cash flows from operating activities. See Note 8 "*Long-Term Obligations*" and Note 11 "*Accumulated Other Comprehensive Loss.*"

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The following table presents the notional amount, fair value and balance sheet classification of the Company's derivative financial instruments designated as cash flow hedges as of September 30, 2019 and December, 31, 2018. The fair values of both interest rate swaps were liabilities at September 30, 2019 and were hedges of the same interest rate risk.

| | Balance Sheet Location | Notional Amount | Fair Value |
|---|---|---|---|
| At September 30, 2019: | | | |
| Interest rate swaps | Other long-term liabilities | $ 135,000 | $ 552 |
| | | | |
| At December 31, 2018: | | | |
| Interest rate swaps | Other assets | $ 90,000 | $ 458 |

The following table presents gains and losses before income taxes on the Company's interest rate swaps designated as a cash flow hedge for the three and nine-month periods ending September 30, 2019 and 2018.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2019 | 2018 | 2019 | 2018 |
| (Loss) gain recognized in accumulated other comprehensive loss | $ (396) | $ 17 | $ (362) | $ 429 |
| Gain reclassified from accumulated other comprehensive loss to income | 197 | 136 | 648 | 258 |

The following table presents the effect of cash flow hedge accounting on the Company's Statements of Comprehensive Income for the three and nine-month periods ending September 30, 2019 and 2018:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2019 | 2018 | 2019 | 2018 |
| Recorded as Interest Expense: | | | | |
| Hedged interest payments | $ (2,327) | $ (1,628) | $ (5,524) | $ (4,690) |
| Gain on interest rate swap | 197 | 136 | 648 | 258 |

## 5. ACCOUNTS RECEIVABLE

Accounts receivable, net, consists of the following at September 30, 2019 and December 31, 2018:

| | 2019 | 2018 |
|---|---|---|
| Retail customers | $ 19,340 | $ 21,732 |
| Wholesale carriers | 6,615 | 9,315 |
| Other | 4,290 | 4,361 |
| | 30,245 | 35,408 |
| Less: allowance for doubtful accounts | (4,807) | (3,936) |
| Accounts receivable, net | $ 25,438 | $ 31,472 |

(Unaudited, In Thousands Except Per Share Amounts)

The following table presents the activity in the allowance for doubtful accounts for the nine-month period ended September 30, 2019, which is associated entirely with the Company's contracts with customers:

| | 2019 |
|---|---|
| Balance at January 1 | $ 3,936 |
| Provision for uncollectible accounts | 275 |
| Charged to other accounts | 1,252 |
| Deductions | (656) |
| Asset at September 30 | $ 4,807 |

USAC has issued funding commitment letters for all of the Company's rural health care customer applications for Funding Year 2018 (July 1, 2018 through June 30, 2019). Accounts receivable, net, associated with rural health care customers was $4,012 and $8,122 at September 30, 2019 and December 31, 2018, respectively. Rural health care accounts are a component of the retail customers category in the above table.

## 6. OTHER CURRENT ASSETS

Prepayments and other current assets consist of the following at September 30, 2019 and December 31, 2018:

| | 2019 | 2018 |
|---|---|---|
| Income tax receivable | $ 7,559 | $ 5,087 |
| Prepaid expense | 3,003 | 3,878 |
| Other | 2,629 | 3,204 |
| Total prepayments and other current assets | $ 13,191 | $ 12,169 |

## 7. CURRENT LIABILITIES

Accounts payable, accrued and other current liabilities consist of the following at September 30, 2019 and December 31, 2018:

| | 2019 | 2018 |
|---|---|---|
| Accounts payable - trade | $ 15,392 | $ 14,627 |
| Accrued payroll, benefits, and related liabilities | 13,018 | 13,473 |
| Deferred capacity and other revenue | 6,588 | 6,095 |
| Other | 5,319 | 6,762 |
| Total accounts payable, accrued and other current liabilities | $ 40,317 | $ 40,957 |

Advance billings and customer deposits consist of the following at September 30, 2019 and December 31, 2018:

| | 2019 | 2018 |
|---|---|---|
| Advance billings | $ 3,760 | $ 3,992 |
| Customer deposits | 31 | 32 |
| Total advance billings and customer deposits | $ 3,791 | $ 4,024 |

(Unaudited, In Thousands Except Per Share Amounts)

## 8. LONG-TERM OBLIGATIONS

Long-term obligations consist of the following at September 30, 2019 and December 31, 2018:

| | 2019 | 2018 |
|---|---|---|
| 2019 senior secured credit facility due 2024 | $ 178,875 | $ - |
| Debt discount | (2,408) | - |
| Debt issuance costs | (1,992) | - |
| 2017 senior secured credit facility due 2023 | - | 171,750 |
| Debt discount | - | (2,024) |
| Debt issuance costs | - | (2,182) |
| Capital leases and other long-term obligations | 2,740 | 2,768 |
| Total long-term obligations | 177,215 | 170,312 |
| Less current portion | (5,674) | (2,289) |
| Long-term obligations, net of current portion | $ 171,541 | $ 168,023 |

As of September 30, 2019, the aggregate maturities of long-term obligations were as follows:

| | |
|---|---|
| 2019 (October 1 - December 31) | $ 1,136 |
| 2020 (January 1 - December 31) | 6,802 |
| 2021 (January 1 - December 31) | 9,067 |
| 2022 (January 1 - December 31) | 11,333 |
| 2023 (January 1 - December 31) | 15,851 |
| 2024 (January 1 - December 31) | 135,122 |
| Thereafter | 2,304 |
| Total maturities of long-term obligations | $ 181,615 |

*2019 Senior Credit Facility*

On January 15, 2019, the Company entered into an amended and restated credit facility consisting of an Initial Term A Facility in the amount of $180,000, a Revolving Facility in an amount not to exceed $20,000 and a Delayed-Draw Term A Facility in an amount not to exceed $25,000 (together the “2019 Senior Credit Facility” or “Agreement”). The Agreement also provides for Incremental Term A Loans up to an aggregate principal amount of the greater of $60,000 and trailing twelve month EBITDA, as defined in the Agreement. On January 15, 2019, proceeds from the Initial Term A Facility of $178,335, net of discounts of $1,665, were used to repay in full the outstanding principal balance of the Term A-1 Facility and Term A-2 Facility under the Company’s 2017 Senior Credit Facility of $112,500 and $59,250, respectively, pay accrued and unpaid interest of $590, and pay fees and expenses associated with the transaction totaling $2,216. The 2017 Senior Credit Facility was terminated on January 15, 2019. Discounts, debt issuance costs and fees associated with the 2019 Senior Credit Facility totaling $2,683 were deferred and will be charged to interest expense over the term of the agreement.

Amounts outstanding under the Initial Term A Facility, Revolving Facility, Delayed-Draw Facility and Incremental Term A Loans bear interest at LIBOR plus 4.5% per annum. The Company may, at its discretion and subject to certain limitations as defined in the Agreement, select an alternate base rate at a margin that is 1.0% lower than the counterpart LIBOR margin.

Principal payments on the Initial Term A Facility, Delayed-Draw A Facility and any amounts outstanding under the Incremental Term A Loans are due commencing in the third quarter of 2019 as follows: the third quarter of 2019 through the second quarter of 2020 – 0.625% per quarter; the third quarter of 2020 through the second quarter of 2022 – 1.25% per quarter; the third quarter of 2022 through the second quarter of 2023 – 1.875% per quarter; and the third quarter of 2023 through the fourth quarter of 2023 – 2.5% per quarter. The remaining outstanding principal balance, including any amounts outstanding under the Revolving Facility, is due on January 15, 2024.

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There were no amounts outstanding under the Revolving Facility, Delayed-Draw Term A Facility and Incremental Term A Loans at September 30, 2019.

The obligations under the 2019 Senior Credit Facility are secured by substantially all the personal property and real property of the Company, subject to certain agreed exceptions.

The 2019 Senior Credit Facility contains customary representations, warranties and covenants, including covenants limiting the incurrence of debt, the payment of dividends and repurchase of the Company's common stock.

The 2019 Senior Credit Facility provides for events of default customary for credit facilities of this type, including non-payment defaults on other debt, misrepresentation, breach of covenants, representations and warranties, change of control, and insolvency and bankruptcy.

Under the terms of the 2019 Senior Credit Facility, the Company is required to enter into or obtain an interest rate hedge sufficient to effectively fix or limit the interest rate on borrowings under the agreement of a minimum of $90,000 with a weighted average life of at least two years. Upon repayment of the outstanding principal balance of the 2017 Senior Credit Facility on January 15, 2019, the pay-fixed, receive-floating interest rate swap in the notional amount of $90,000, with an interest rate of 6.49425%, inclusive of a 5.0% LIBOR spread, and a maturity date of June 28, 2019 was assigned to the 2019 Senior Credit Facility. On June 28, 2019, the Company entered into two pay-fixed, receive-floating, interest rate swaps. Each swap is in the notional amount of $67,500, has an interest rate of 6.1735% inclusive of a 4.5% LIBOR spread, and a maturity date of June 30, 2022. The swaps are with different counter parties.

*2017 Senior Credit Facility*

On January 15, 2019, the Company utilized proceeds from the 2019 Senior Credit Facility to repay in full the outstanding principal balance of its 2017 Senior Credit Facility in the amount of $171,750. The Company recorded a loss of $2,830 on the extinguishment of debt associated with this transaction, including the write-off of debt issuance costs and third-party fees.

*6.25% Convertible Notes Due 2018*

On May 1, 2018, the Company repurchased the outstanding balance of its 6.25% Notes. The cash settlement totaled $10,358, including principal of $10,044 and accrued interest of $314. Settlement was funded utilizing restricted cash of $10,044 and cash on hand of $314. There was no gain or loss associated with the repurchase.

## 9. OTHER LONG-TERM LIABILITIES

Other long-term liabilities, consisting primarily of deferred capacity and other revenue, was as follows at September 30, 2019 and December 31, 2018:

| | 2019 | 2018 |
|---|---|---|
| Deferred GCI capacity revenue, net of current portion | $ 29,558 | $ 31,113 |
| Other deferred IRU capacity revenue, net of current portion | 27,083 | 25,732 |
| Other deferred revenue, net of current portion | 4,605 | 2,113 |
| Other | 10,004 | 8,869 |
| Total other long-term liabilities | $ 71,250 | $ 67,827 |

## 10. LEASES

The Company adopted the provisions of ASC 842 effective in the first quarter of 2019 on a modified retrospective basis. Refer to Note 1 "*Summary of Significant Accounting Policies*" for a summary of the effect of initial adoption on the Company's consolidated financial statements.

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The Company applied the following practical expedients as provided for under ASC 842:

(i) The determination of whether expired or existing contracts contain leases at the date of adoption was not reassessed;
(ii) The classification of existing or expired leases at the date of adoption was not reassessed;
(iii) The provisions of ASC 842 were not applied to lease agreements with a term of 12 months or less;
(iv) Non-lease components, which are not material, were combined with lease components and, accordingly, consideration was not allocated between these two elements;
(v) Existing lease agreements were not reassessed to identify any initial direct costs; and
(vi) Hindsight was applied to determine changes in lease terms and assess for the impairment of ROU assets.

**Lease Agreements Under Which the Company is the Lessee**

The Company enters into agreements for land, land easements, access rights, IRUs, co-located data centers, buildings, equipment, pole attachments and personal property. These assets are utilized in the provision of broadband and telecommunications services to the Company's customers. An agreement is determined to be a lease if it conveys to the Company the right to control the use of an identified asset for a period of time in exchange for consideration. Control is defined as the Company having both the right to obtain substantially all of the economic benefits from the use of the asset and the right to direct the use of the asset. This determination is made at contract inception. Operating leases are included in operating lease ROU assets and current and noncurrent operating lease liabilities on the consolidated balance sheet. Finance leases are included in property, plant and equipment and current portion of long-term obligations and long-term obligations on the consolidated balance sheet.

ROU assets represent the Company's right to use the underlying asset for the term of the operating lease and operating lease liabilities represent the Company's obligation to make lease payments over the term of the lease. ROU assets and operating lease liabilities are recognized at the lease commencement date based on the estimated present value of the lease payments over the term of the lease.

The terms of the Company's leases are primarily fixed. A limited number of leases include a variable payment component based on a pre-determined percentage or index.

Most of the Company's lease agreements include extension options which vary between leases but are generally consistent with industry practice. Extension options are exercised as required to meet the Company's service obligations and other business requirements. Extension options are included in the determination of the ROU asset if, at lease inception, it is reasonably certain that the option will be exercised.

Certain leases include a provision for early termination, typically in return for an agreed amount of consideration. The terms of these provisions vary by contract. Upon the exercise of an early termination option, the ROU asset and associated liability are remeasured to reflect the present value of the revised cash flows. Early terminations recorded in the nine-month period ended September 30, 2019 were not material.

The Company's operating and financing lease agreements do not include residual value guarantees, embedded leases or impose material restrictions or covenants on the Company's operations. It has no lease arrangements with related parties. The Company has subleases associated with certain leased assets. Such arrangements are not material.

The Company entered into additional operating lease commitments that had not yet commenced as of September 30, 2019 with a present value totaling approximately $922. These leases are primarily associated with the Company's CAF Phase II services, are expected to commence in 2019 and 2020, and have terms of 7 to 25 years.

The discount rate applied to determine the present value of the future lease payments is based on the Company's incremental borrowing rate which is derived from recent secured borrowing arrangements entered into by the Company and publicly available information for instruments with similar terms.

Short-term and variable lease cost recorded during the three and nine-month periods ended September 30, 2019 were not material.

The Company did not enter into any sale and leaseback transactions during the nine-month period ended September 30, 2019.

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The following tables provide certain quantitative information about the Company’s lease agreements under which it is the lessee as of and for the three and nine-month periods ended September 30, 2019. The maturities of lease liabilities are presented in twelve-month increments beginning October 1, 2019.

| | Three Months Ended September 30, 2019 | Nine Months Ended September 30, 2019 |
|---|---|---|
| **Lease Cost** | | |
| Finance lease cost: | | |
| Amortization of right-of-use assets | $ 20 | $ 59 |
| Interest on lease liabilities | 67 | 203 |
| Operating lease costs | 1,972 | 5,882 |
| Total lease cost | $ 2,059 | $ 6,144 |

| | At September 30, 2019 |
|---|---|
| **Balance Sheet Information** | |
| Operating leases: | |
| ROU assets | $ 80,748 |
| Liabilities - current | $ 2,626 |
| Liabilities - noncurrent | 78,362 |
| Total liabilities | $ 80,988 |
| Finance leases: | |
| Property, plant and equipment | $ 2,519 |
| Accumulated depreciation and amortization | (1,430) |
| Property, plant and equipment, net | $ 1,089 |
| Current portion of long-term obligations | $ 49 |
| Long-term obligations, net of current portion | 2,691 |
| Total finance lease liabilities | $ 2,740 |

| | At September 30, 2019 | |
|---|---|---|
| | Operating Leases | Financing Leases |
| **Maturities of Lease Liabilities** | | |
| Year 1 | $ 7,236 | $ 316 |
| Year 2 | 7,464 | 325 |
| Year 3 | 7,364 | 334 |
| Year 4 | 7,140 | 343 |
| Year 5 | 6,884 | 352 |
| Thereafter | 159,470 | 3,562 |
| Total lease payments | 195,558 | 5,232 |
| Less imputed interest | (115,317) | (2,492) |
| Total present value of lease obligations | 80,241 | 2,740 |
| Present value of current obligations | (1,879) | (49) |
| Present value of long-term obligations | $ 78,362 | $ 2,691 |

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| **Other Information** | | |
|---|---|---|
| Cash paid for amounts included in the measurement of lease liabilities: | | |
| Operating cash flows from finance leases | $ | 203 |
| Operating cash flows from operating leases | | 5,645 |
| Financing cash flows from finance leases | | 28 |
| Right-of-use assets obtained in exchange for new operating lease liabilities | | 592 |
| Weighted-average remaining lease term (in years): | | |
| Finance leases | | 14 |
| Operating leases | | 30 |
| Weighted-average discount rate: | | |
| Finance leases | | 9.8% |
| Operating leases | | 6.9% |

**Lease Agreements Under Which the Company is the Lessor**

The Company's agreements under which it is the lessor are primarily associated with the use of its network assets, including IRUs for fiber optic cable, colocation and buildings. An agreement is determined to be a lease if it coveys to the lessee the right to control the use of an identified asset for a period of time in exchange for consideration. Control is defined as the lessee having both the right to obtain substantially all of the economic benefits from the use of the asset and the right to direct the use of the asset. This determination is made at contract inception. Exchanges of IRUs with other carriers are accounted for as leases if the arrangement has commercial substance. All of the Company's agreements under which it is the lessor have been determined to be operating leases.

Lease payments are recognized as income on a straight-line basis over the term of the agreement, including scheduled changes in payments not based on an index or otherwise determined to be variable in nature. Any changes in payments based on an index are reflected in income in the period of the change. The underlying leased asset is reported as a component of property, plant and equipment on the balance sheet.

Initial direct costs associated with the lease incurred by the Company are deferred and expensed over the term of the lease.

Certain of the Company's operating lease agreements include extension options which vary between leases but are generally consistent with industry practice. Extension options are not included in the determination of lease income unless, at lease inception, it is reasonably certain that the option will be exercised.

The Company's operating leases do not include purchase options.

Certain leases include a provision for early termination, typically in return for an agreed amount of consideration. The terms of these provisions vary by contract. Upon the exercise of an early termination option, any deferred rent receivable, deferred income and unamortized initial direct costs are written off. The underlying asset is assessed for impairment giving consideration to the Company's ability to utilize the asset in its business. There were no early terminations recorded in the nine-month period ended September 30, 2019.

The Company does not have material sublease arrangements as the lessor or lease arrangements with related parties.

The Company did not have sales-type leases or direct financing leases as of September 30, 2019.

The underlying assets associated with the Company's operating leases are accounted for under ASC 360, '*Property, Plant and Equipment.*" The assets are depreciated on a straight-line basis over their estimated useful life, including any periods in which the Company expects to utilize the asset subsequent to termination of the lease.

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**(Unaudited, In Thousands Except Per Share Amounts)**

The Company's operating lease agreements may include a non-lease component associated with operation and maintenance services. Consideration received for these services are recognized as income on a straight-line basis consistently with the lease components. Certain operating lease arrangements include a separate maintenance and service agreement. Consideration received under these separate agreements are recognized as income when the relevant service is provided to the lessee.

The following tables provide certain quantitative information about the Company's operating lease agreements under which it is the lessor as of and for the three and nine-month periods ended September 30, 2019. Lease income is classified as revenue on the Statement of Comprehensive Income. The carrying value of the underlying leased assets is not material.

| | Three Months Ended September 30, 2019 | Nine Months Ended September 30, 2019 |
|---|---|---|
| **Lease Income** | | |
| Total lease income | $ 879 | $ 2,595 |

| | At September 30, 2019 |
|---|---|
| **Maturities of Future Undiscounted Lease Payments** | |
| Year 1 | $ 1,228 |
| Year 2 | 1,154 |
| Year 3 | 544 |
| Year 4 | 385 |
| Year 5 | 383 |
| Thereafter | 2,933 |
| Total future undiscounted lease payments | $ 6,627 |

## 11. ACCUMULATED OTHER COMPREHENSIVE LOSS

The following table summarizes the activity in accumulated other comprehensive income (loss) for the nine-month period ended September 30, 2019:

| | Defined Benefit Pension Plan | Interest Rate Swaps | Total |
|---|---|---|---|
| Balance at December 31, 2018 | $ (3,003) | $ 328 | $ (2,675) |
| Other comprehensive income before reclassifications | (22) | (260) | (282) |
| Reclassifications from accumulated comprehensive income (loss) to net income | 37 | (464) | (427) |
| Net other comprehensive income (loss) | 15 | (724) | (709) |
| Balance at September 30, 2019 | $ (2,988) | $ (396) | $ (3,384) |

**(Unaudited, In Thousands Except Per Share Amounts)**

The following table summarizes the reclassifications from accumulated other comprehensive income (loss) to net income for the three and nine-month periods ended September 30, 2019 and 2018:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2019 | 2018 | 2019 | 2018 |
| Amortization of defined benefit plan pension items: | | | | |
| Amortization of loss | $ (192) | $ (13) | $ 51 | $ 169 |
| Income tax effect | 55 | 4 | (14) | (48) |
| After tax | (137) | (9) | 37 | 121 |
| | | | | |
| Amortization of gain on interest rate swap: | | | | |
| Reclassification to interest expense | (197) | (136) | (648) | (258) |
| Income tax effect | 56 | 39 | 184 | 74 |
| After tax | (141) | (97) | (464) | (184) |
| Total reclassifications, net of income tax | $ (278) | $ (106) | $ (427) | $ (63) |

Amounts reclassified to net income from our defined benefit pension plan and interest rate swaps have been presented within “Other income (expense), net” and “Interest expense,” respectively, in the Statements of Comprehensive Income. The estimated amount to be reclassified from accumulated other comprehensive income as a reduction in interest expense within the next twelve months is $19. See Note 4 “*Fair Value Measurements and Derivative Financial Instruments*.”

## 12. STOCK INCENTIVE PLANS

Under the Company’s stock incentive plan, stock options, restricted stock, stock-settled stock appreciation rights, performance share units and other awards may be granted to officers, employees, consultants, and non-employee directors. Long-term incentive awards (“LTIP”) were granted to executive management annually through 2010.

*2011 Incentive Award Plan*

On June 10, 2011, Alaska Communications shareholders approved the 2011 Incentive Award Plan, which was amended and restated on June 30, 2014 and June 25, 2018, and which terminates in 2021. Following termination, all shares granted under this plan, prior to termination, will continue to vest under the terms of the grant when awarded. All remaining unencumbered shares of common stock previously allocated to the Prior Plans were transferred to the 2011 Incentive Award Plan. In addition, to the extent that any outstanding awards under the Prior Plans are forfeited or expire or such awards are settled in cash, such shares will again be available for future grants under the 2011 Incentive Award Plan. The Company grants Restricted Stock Units (“RSUs”) and Performance Stock Units (“PSUs”) as the primary equity based incentive for executive and certain non union-represented employees. The disclosures below are primarily associated with RSU and PSU grants awarded in 2017, 2018 and 2019.

*Restricted Stock Units*

The Company measures the fair value of RSUs based on the number of shares granted and the quoted closing market price of the Company’s common stock on the date of grant. RSUs granted in 2019 vest ratably over the three-year period ending March 1, 2022.

In the second quarter of 2019, RSU’s granted to the Company’s former Chief Executive Officer in 2017 and 2018 were modified. The vesting dates were accelerated from 2020 and 2021 to June 2019, and the awards were revalued. The modification resulted in a net increase in share-based compensation expense of $112 in the second quarter. The modification is included in grants and cancellations in the table below.

**(Unaudited, In Thousands Except Per Share Amounts)**

The following table summarizes the RSU, LTIP and non-employee director stock compensation activity for the nine-month period ended September 30, 2019.

| | Number of Units | Weighted Average Grant Date Fair Value |
|---|---|---|
| Nonvested at December 31, 2018 | 1,185 | $ 1.88 |
| Granted | 443 | 1.69 |
| Vested | (768) | 1.86 |
| Canceled or expired | (208) | 1.96 |
| Nonvested at September 30, 2019 | 652 | $ 1.76 |

*Performance Stock Units*

PSUs granted in the third quarter of 2019 will vest proportionally over the three-year period ending in March 2022 subject to the achievement of certain Company performance targets.

In the second quarter of 2019, certain PSU's granted to the Company's former Chief Executive Officer in 2017 and 2018 were modified. The vesting dates were accelerated from 2019, 2020 and 2021 to June 2019, and the awards were revalued. The modification resulted in a net decrease in share-based compensation expense of $165 in the second quarter. The modification is included in grants and cancellations in the table below.

The following table summarizes the PSU activity for the nine-month period ended September 30, 2019.

| | Number of Units | Weighted Average Grant Date Fair Value |
|---|---|---|
| Nonvested at December 31, 2018 | 2,070 | $ 0.85 |
| Granted | 1,188 | 0.77 |
| Vested | - | - |
| Canceled or expired | (1,722) | 0.78 |
| Nonvested at September 30, 2019 | 1,536 | $ 0.87 |

The following table provides selected information about the Company's share-based compensation as of and for the three and nine-month periods ended September 30, 2019 and 2018:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2019 | 2018 | 2019 | 2018 |
| Total compensation cost for share-based payments | $ 277 | $ 642 | $ 766 | $ 1,209 |
| Weighted average grant-date fair value of equity instruments granted (per share) | $ 1.71 | $ 0.80 | $ 1.02 | $ 0.97 |
| Total fair value of shares vested during the period | $ - | $ - | $ 1,427 | $ 1,524 |
| | | | | |
| At September 30: | | | | |
| Unamortized share-based payments | | | $ 971 | $ 2,039 |
| Weighted average period (in years) to be recognized as expense | | | 1.8 | 1.2 |

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

## 13. EARNINGS PER SHARE

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

Effective in 2015, the Company discontinued use of the “if converted” method in calculating diluted earnings per share in connection with its contingently convertible debt. Accordingly, zero and 429 shares related to the 6.25% Notes were excluded from the calculation of diluted earnings per share for the three and nine-month periods ended September 30, 2018. On May 1, 2018, the Company repurchased the outstanding balance of the 6.25% Notes. See Note 8 “*Long-Term Obligations*.”

The calculation of basic and diluted earnings per share for the three and nine-month periods ended September 30, 2019 and 2018 are as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | **2019** | **2018** | **2019** | **2018** |
| Net income attributable to Alaska Communications | $ 2,022 | $ 1,817 | $ 2,284 | $ 7,360 |
| Weighted average common shares outstanding: | | | | |
| Basic shares | 53,328 | 53,184 | 53,503 | 52,994 |
| Effect of stock-based compensation | 663 | 932 | 902 | 893 |
| Diluted shares | 53,991 | 54,116 | 54,405 | 53,887 |
| Net income per share attributable to Alaska Communications: | | | | |
| Basic | $ 0.04 | $ 0.03 | $ 0.04 | $ 0.14 |
| Diluted | $ 0.04 | $ 0.03 | $ 0.04 | $ 0.14 |

**(Unaudited, In Thousands Except Per Share Amounts)**

## 14. RETIREMENT PLANS

*Multi-employer Defined Benefit Plan*

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

*Defined Benefit Plan*

The Company has a separate defined benefit plan that covers certain employees previously employed by Century Telephone Enterprise, Inc. ("CenturyTel Plan"). This plan was transferred to the Company in connection with the acquisition of CenturyTel, Inc.'s Alaska properties, whereby assets and liabilities of the CenturyTel Plan were transferred to the ACS Retirement Plan (the "Plan") on September 1, 1999. In the third quarter of 2019, the Company concluded that almost all participants in the Plan are inactive through either retirement or termination. In accordance with ASC 715, "*Compensation – Retirement Benefits*," the amortization period for certain costs associated with the Plan will be changed from the expected future working lifetime of current active employees covered by the Plan to the expected future lifetime of inactive participants. This change was applied effective January 1, 2019. The amortization of loss in the table below reflects a $352 credit recorded in the third quarter of 2019 for the cumulative effect of the change. As of September 30, 2019, this plan is not fully funded under the Employee Retirement Income Security Act of 1974, as amended.

The following table presents the net periodic pension expense for the ACS Retirement Plan for the three and nine-month periods ended September 30, 2019 and 2018:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | **2019** | **2018** | **2019** | **2018** |
| Interest cost | $ 153 | $ 143 | $ 453 | $ 425 |
| Expected return on plan assets | (169) | (198) | (508) | (594) |
| Amortization of loss | (176) | 42 | 106 | 338 |
| Net periodic pension expense | $ (192) | $ (13) | $ 51 | $ 169 |

Net periodic pension expense is included in the line item "Other income, net" in the Statements of Comprehensive Income.

## 15. SUPPLEMENTAL CASH FLOW INFORMATION

Restricted cash of $1,631 at September 30, 2019 consisted of certificates of deposit of $1,600 required under the terms of certain contracts to which the Company is a party and other restricted cash of $31. Restricted cash of $1,634 at December 31, 2018 consisted of certificates of deposit of $1,600 required under the terms of certain contracts to which the Company is a party and other restricted cash of $34.

The following table provides a reconciliation of cash and cash equivalents and restricted cash reported within the statement of financial position at September 30, 2019 and 2018 that sum to the total of these items reported in the statement of cash flows:

| | September 30, | |
|---|---|---|
| | **2019** | **2018** |
| Cash and cash equivalents | $ 25,046 | $ 17,292 |
| Restricted cash | 1,631 | 1,634 |
| Total cash, cash equivalents and restricted cash | $ 26,677 | $ 18,926 |

**(Unaudited, In Thousands Except Per Share Amounts)**

The following table presents supplemental non-cash transaction information for the nine-month periods ended September 30, 2019 and 2018:

| | 2019 | 2018 |
|---|---|---|
| Supplemental Non-cash Transactions: | | |
| Capital expenditures incurred but not paid at September 30 | $ 5,823 | $ 3,350 |
| Additions to ARO asset | $ 58 | $ 752 |

## 16. BUSINESS SEGMENTS

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

## 17. COMMITMENTS AND CONTINGENCIES

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

The Company is involved in various claims, legal actions and regulatory proceedings arising in the ordinary course of business. The Company establishes an accrual when a particular contingency is probable and estimable, and has recorded litigation accruals totaling $1,365 at September 30, 2019 against certain current claims and legal actions. The Company also faces contingencies that are reasonably possible to occur that cannot currently be estimated. The Company believes that the disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, comprehensive income or cash flows. It is the Company's policy to expense costs associated with loss contingencies, including any related legal fees, as they are incurred.

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

### FORWARD-LOOKING STATEMENTS AND ANALYSTS' REPORTS

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

- Our ability to continue to develop and fund attractive, integrated products and services to evolving industry standards, and meet the pressure from competition to offer these services at lower prices
- unforeseen challenges when entering new markets and our ability to recognize and react to actions, products or services of competitors that threaten our competitive advantage in the marketplace
- our size, because we are a smaller sized competitor in the markets we serve and we compete against large competitors with substantially greater resources
- governmental and public policy changes and investigations, including on-going changes in our revenues, or obligations for current and prior periods related to these programs, resulting from regulatory actions affecting inter-carrier compensation, on-going support for state programs such as Essential Network Support obligations, and federal programs such as the rural health care universal service support mechanism, including ascertainment of the "urban rate" and "rural rate" used to determine federal support payments for services we provide to our rural health care customers for current and prior periods
- our ability to comply with the regulatory requirements to contribute to the Universal Service Fund and receive support payments from that fund
- our ability to obtain and appropriately allocate resources to support our growth objectives
- our ability to maintain successful arrangements with our represented employees
- our ability to keep pace with rapid technological developments and changing standards in the telecommunications industry, including on-going capital expenditures needed to upgrade our network to industry competitive speeds, particularly in light of expected 5G deployments by mobile wireless carriers
- our ability to maintain our cost structure as a focused broadband and managed IT services company. Maintaining our cost structure is key to generating cash flow from operating activities. If we fail to effectively manage our costs, our financial condition will be impacted
- disruptions or failures in the physical infrastructure or operating systems that support our businesses and customers, or cyber-attacks or security breaches of the physical infrastructure, operating systems or devices that our customers use to access our products and services
- our ability to adequately invest in the maintenance and upgrade of our networks and other information technology systems
- the Alaskan economy, which has been impacted by continued low crude oil prices which are creating a significant impact on both the level of spending by the State of Alaska and the level of investment in resource development projects by natural resource exploration and development companies in Alaska. The cuts to the state 2020 budget and resulting spending reductions may impact the economy in the markets we serve and impact our future financial performance

- our ability to invest sufficiently in our underlying physical infrastructure, including buildings, fleet and related equipment
- the ability to attract, recruit, retain and develop our workforce, and implement succession planning necessary for achieving our business plan
- structural declines for voice and other legacy services within the telecommunications industry
- the success or failure of any future acquisitions or other major transactions
- our business and operations could be negatively affected as a result of the actions of activist stockholders, which could cause us to incur significant expense, hinder execution of our business strategy and impact our stock price
- unanticipated damage to one or more of our undersea fiber optic cables resulting from construction or digging mishaps, fishing boats or other reasons
- a maintenance or other failure of our network or data centers
- a failure of information technology systems
- a third-party claim that the Company is infringing upon their intellectual property, resulting in litigation or licensing expenses, or the loss of our ability to sell or support certain products
- unanticipated costs required to fund our post-retirement benefit plans, or contingent liabilities associated with our participation in a multi-employer pension plan
- geologic or other natural disturbances relevant to the location of our operations
- our ability to meet the terms of our financing agreements and to draw down additional funds under the facility to meet our liquidity needs
- the cost and availability of future financing, at the terms, and subject to the conditions necessary, to support our business and pursue growth opportunities; our debt could also have negative consequences for our business; for example, it could increase our vulnerability to general adverse economic and industry conditions, or limit our flexibility in planning for, or reacting to, changes in our business and the telecommunications industry; in addition, our ability to borrow funds in the future will depend in part on the satisfaction of the covenants in our credit facilities; if we are unable to satisfy the financial covenants contained in those agreements, or are unable to generate cash sufficient to make required debt payments, the lenders and other parties to those arrangements could accelerate the maturity of some or all of our outstanding indebtedness
- our success in providing broadband solutions to the North Slope and western Alaska
- the success of the Company’s expansion into managed IT services, including the execution of those services for customers
- our internal control over financial reporting may not be effective, which could cause our financial reporting to be unreliable
- the matters described under Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2018 and this Quarterly Report on Form 10-Q.

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

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

**OVERVIEW**

We are a fiber broadband and managed IT services provider, offering technology and service enabled customer solutions to business and wholesale customers in and out of Alaska. We also provide telecommunication services to consumers in the most populated communities throughout the state. Our facilities based communications network extends through the economically significant portions of Alaska and connects to the contiguous states via our two diverse undersea fiber optic cable systems. Our network is among the most expansive in Alaska and forms the foundation of service to our customers. We operate in a largely two-player terrestrial wireline market and we estimate our market share to be less than 25% statewide. However, we sponsored a third-party market study which suggests that our market share in “near net”, that is, within one mile of our fiber footprint, may be closer to 40%. This is consistent with our hypothesis that from a revenue performance perspective, relative to our largest competitor we are gaining market share in the markets we are serving.

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

**The Alaska Economy**

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

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

The population of Alaska, which declined marginally in 2018, is approximately 740,000 with Anchorage, Fairbanks and Juneau serving as the primary population and economic centers in the state.

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

Alaska's economy is dependent on investment by oil companies, and state tax revenues correlate with the price of oil as the State assesses a tax based on the price of oil that transits the pipeline from the North Slope. The price of crude oil dropped substantially during 2014 through 2016, and increased marginally in 2017 and 2018. Public and private industry forecasts currently indicate a gradual price decline through 2022. The decline in the price of crude oil has impacted the state in two ways:

1. Resource based companies reduced their level of spending in the state, and in particular the North Slope, through reducing their operating costs.
2. The State of Alaska budget represents approximately 15% of the State's total economy. The State's budget deficit was reduced from $3.7 billion in 2015 to $0.7 billion in 2019 primarily through spending reductions and utilization of interest earned on the state's permanent fund. Reduced spending by the state has had a dampening effect on overall economic activity in the state. Reductions to the state's 2020 budget and the resulting lower spending may impact the economy in the markets we serve.

In spite of lower oil prices, there has been new development and increased activity on the North Slope in 2019 driven by tightened production in other countries and expectations about global economic growth and availability of supply. Volume is currently expected to decline after 2020 before rebounding in the late-2020s.

Economists believe the Alaskan economy entered a moderate recession beginning in the second half of 2015. Certain areas of the economy showed improvement beginning in 2018. Employment levels in the state declined approximately 0.3% in 2018 (compared with a 1.3% decline in 2017) driven by declines in the oil and gas industry, construction, and Federal and state government, offset by increases in health care and local government. The negative effects of the recession have been mitigated by diversity in the Alaskan economy, including growth in the health care and tourism industries. However, economists believe that, given the ongoing state budget reductions and expected lower oil prices, the recession may continue for two to three more years.

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

**Regulatory Update**

The items reported under Part I, Item 1. Business – Regulation in our Annual Report on Form 10-K for the year ended December 31, 2018, are updated as follows. This section should be read in conjunction with the corresponding items previously disclosed in our Annual Report.

***US Federal Regulatory Matters***

*Rural Health Care Support Program*

As described in our most recent Form 10-K, in November 2018, USAC approved the rural rates for the services we provide to our rural health care customers for Funding Year 2018, which began on July 1, 2018 and ended on June 30, 2019. Rural Health Care revenues represented 6.3% of the Company's consolidated revenue in the nine-month period ended September 30, 2019.

In November 2018, in an attempt to shorten the USAC funding request approval process and bring greater certainty to the competitive bidding process for rural health care provider services, we requested FCC approval for rural rates for Funding Year 2019, which began July 1, 2019. Even though the FCC did not act on this request before the start of Funding Year 2019, we expect that the rates, when approved, will apply to services we have provided to rural health care customers beginning on July 1, 2019.

On August 1, 2019, the FCC adopted an order making comprehensive changes to the rules governing the competitive bidding process and the method for determining the urban and rural rates used to calculate the amount of Rural Health Care Telecommunications Program support payments for which a health care provider is eligible. The changes to the urban and rural rate rules do not take effect until Funding Year 2021, which will begin July 1, 2021, and USAC will need to conduct a lengthy implementation process over the next 12-18 months before eligible rates and associated support levels can be known. In the meantime, it remains impossible to predict the impact the new rules will have. We are continuing to evaluate the impact of the funding cap constraints, ongoing uncertainty and unpredictability in the Rural Health Care Universal Service Support Mechanism, and the impact of the rule changes on our rural health care customers and revenues in light of these developments. On October 21, 2019, an appeal challenging the new method of setting rates for supported services was filed in the United States Court of Appeals for the District of Columbia Circuit, adding further uncertainty to the ultimate outcome of this proceeding.

As a result of USAC's more rigorous review in recent years of requests for support from the Telecommunications Program (see Item 1A. Risk Factors), the Company has received inquiries and requests for information from USAC about compliance with service eligibility and rate requirements, both with respect to current funding requests and in a letter dated June 2, 2017 from USAC auditors concerning past funding requests. To the Company's knowledge, it has responded fully to USAC's auditors' inquires and requests as of December 21, 2018. In addition, the Company received a Letter of Inquiry on March 18, 2018, from the FCC Enforcement Bureau for historical information regarding the Company's participation in the FCC's Rural Health Care program. On November 5, 2019, the Company received another letter from the FCC Enforcement Bureau requesting additional information.

*USF Contributions*

Under the Communications Act of 1934, as amended (the "Communications Act") and FCC rules, telecommunications carriers and certain providers of telecommunications must contribute to the federal Universal Service Fund. These contributions are based on end-user revenues from interstate and international revenues from assessable services.

In September 2018, the Company received questions and a request for information from USAC regarding the Company's treatment for USF contribution purposes of certain 2017 revenues from services provided to rural healthcare providers under the Rural Health Care Telecommunications Program. To the Company's knowledge, it has responded fully to USAC's questions and information requests regarding the USF contribution issue as of April 2019, and the Company has not received notice of any further action by USAC about this subject.

In its August 2019 Rural Health Care order, the FCC clarified that Telecommunications Program support is only available for services that are characterized as "Telecommunications Services," as defined in the Communications Act. Because the FCC has not definitively resolved the regulatory classification of certain packet-switched data services that the Company provides to rural healthcare providers, the Company is now reviewing the USF-supported services it will offer in the future. However, it is possible that the FCC may disagree with the Company's regulatory classifications.

*CAF Phase II*

CAF Phase II requires recipients to provide broadband service to unserved locations throughout the designated coverage area by the end of a specified build-out period, as well as to meet interim milestone build-out obligations.

On October 31, 2016, the FCC released its order adopting CAF Phase II ("CAF II") support levels and deployment requirements for the Company, as the only price cap carrier in Alaska. Under that order, we receive approximately $19.7 million annually (the same amount we received as CAF I high cost frozen support) for the ten-year period starting January 1, 2016 and continuing through December 31, 2025. To receive this support, we committed to provide voice and broadband Internet access service to 31,571 locations in census blocks that are unserved or only partially served by any unsubsidized competitor. These will include approximately 26,000 locations that did not previously have any recognized access to broadband Internet access service.

The Company filed notices with the FCC as part of a challenge process to include partially served locations within census blocks supported by an unsubsidized competitor. As a result, the Company was able to include over 1,700 additional locations toward meeting its deployment obligations.

We are continuing to work toward meeting our CAF II obligations in a capital-efficient manner, including the potential to deliver broadband Internet access services meeting CAF II requirements using our fixed wireless platform. To date, we have complied with all required deployment milestones.

As part of our participation in CAF Phase II, the Company will be required to test the broadband service it provides to a sample of its customers for compliance with speed and latency requirements imposed by the FCC. Under an Order on Reconsideration adopted on October 25, 2019, the FCC modified these testing requirements and established a commencement date for the testing requirements. We expect that we will be required to begin conducting tests on January 1, 2020, although the FCC will not impose penalties for noncompliance with the CAF Phase II speed and latency metrics based on tests conducted before July 1, 2020. If these tests show that our broadband services supported by CAF Phase II do not meet the required speed and latency metrics, we could be subject to FCC penalties, including reductions in our CAF Phase II support.

*Satellite Services*

On February 16, 2018, the FCC granted our application for a license to operate a network of C-band satellite earth stations to be used to serve our customers that cannot be reached by terrestrial middle mile facilities. Under that license, we are authorized to use up to 72 MHz of C-band spectrum on Eutelsat's satellite, E115WB, for a term of 15 years. In June 2018, the FCC granted our application to expand that network to include new customer sites, and we have since requested authority to double the amount of spectrum we are authorized to use, up to 144 MHz, and serve additional sites. We expect this arrangement to provide us with greater predictability and stability in the availability and cost of long-haul transport connectivity to our customers that must be served by satellite. Since that time, we have continued to expand our C-band network, and our application for a license to serve additional sites is pending at the FCC.

Our C-band satellite earth stations use the 3.7 - 4.2 GHz band to receive downlink transmissions from geostationary satellites. On April 19, 2018, the Wireless Telecommunications, International, and Public Safety Bureaus of the FCC announced an immediate, temporary freeze on the filing of new or modification applications for fixed-satellite service earth station licenses, receive-only earth station registrations, and fixed microwave licenses in the 3.7 - 4.2 GHz portion of the C-band spectrum, in order to preserve the current landscape of authorized operations in that band while the Commission continues to examine opportunities to permit expanded terrestrial use of that band for mobile broadband and additional fixed services. On June 26, 2018, we filed an application for modification of our license to add ten additional earth station sites to serve the Kuspuk School District and requested a waiver of the FCC's freeze on such filings. These requests were granted by an order released by the FCC on August 1, 2019.

On July 13, 2018, the FCC issued a Notice of Proposed Rulemaking seeking comment on options for expanding terrestrial use of the 3.7 - 4.2 GHz band for “5G” mobile services. In response, we have advocated strongly for continued access to this spectrum for satellite downlink operations in Alaska. We are unable to predict the outcome of this proceeding. If the FCC adopts rules that limit our ability to license or register additional satellite earth stations in this band, or expands terrestrial transmissions in the 3.7 - 4.2 GHz band, it may become more difficult or costly for us to use this band, or necessitate relocation of our services to alternative spectrum bands or service technology.

In October 2018, the FCC also opened a proceeding to examine possible new terrestrial uses of the 6 GHz band, including the 5.925-6.425 GHz spectrum used for C-band satellite uplink transmissions originating from terrestrial earth stations to geostationary satellites in orbit. Because C-band earth stations are transmitting in that band, not receiving, we expect any increase in terrestrial use of the 6 GHz band to have a less severe impact on our satellite C-band network than would use of the 3.7 - 4.2 GHz receive band. Nevertheless, we are unable at this time to predict the outcome of these proceedings, or to assess any potential future impact on our C-band satellite services.

***State of Alaska Regulatory Matters***

*Alaska Universal Service Fund*

The Alaska Universal Service Fund (“AUSF”) complements the federal Universal Service Fund, but is focused on obligations to meet intrastate service obligations. The RCA opened a rulemaking to review the regulations specific to AUSF shortfalls. A final decision in that matter was issued in late December, 2017. These rules were transmitted to the Lt. Governor for signature and became effective April, 2018. They eliminate the hierarchy of shortfall payments except for Lifeline and administrative operating expenses.

In January, 2018, the RCA opened a rulemaking to repeal the AUSF effective July 31, 2019, and sought comments and reply comments. The Alaska Telephone Association and its members filed a plan to cap the fund and distributions. AT&T, GCI, and Alaska Communications also filed comments and reply comments. A hearing was scheduled in April. A final order was issued by the RCA on October 24, 2018 with changes to the distribution to be effective January 1, 2019.

Prior to changes to the AUSF distribution, AUSF supported a portion of certain higher cost carriers’ costs through the Carrier of Last Resort (“COLR”) support program. This funding mechanism was eliminated and replaced with a new funding mechanism called Essential Network Support (“ENS”). In addition, the AUSF surcharge has been capped at 10%.

In response to the FCC’s order eliminating Lifeline qualifying programs approved by state regulatory commissions, the Alaskan telecommunications industry has proposed a waiver of the state qualifying programs to align the state and federal qualifying programs. The RCA granted that waiver prior to December 2, 2016 when the new rules went into effect. In August 2017, the RCA opened a docket, R-17-002, on Lifeline to align the programs with the federal rules and revise the certification and verification procedures to reflect revised federal procedures. Lifeline service providers have been operating under an RCA order that aligns some issues and companies made tariff filings to align their procedures. This rulemaking is somewhat ministerial in nature but may become moot depending on the outcomes of the AUSF docket R-18-001. Comments were submitted in September 2017.

*Other State Regulatory Matters*

On August 29, 2019, Governor Dunleavy signed SB83 which starts the clock for implementation of this new state legislation. The bill will eliminate the requirement for Alaska Communications to maintain RCA-filed tariffs for rates, terms, and conditions for legacy phone and networking services in Alaska. However, rates, terms, and conditions for basic residential local telephone service must, under the bill, be uniform within each study area. We are studying the likely effects of the bill and have begun to prepare for its implementation on November 27, 2019.

**Business Plan Core Principles**

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

- ***Create a Workplace That Develops Our People and Celebrates Success*** We believe an engaged workforce is critical to our success. We are deeply committed to the development of our people and creating opportunities for them.

- ***Create a Consistent Customer Experience Every Time*** We strive to deliver service as promised to our customers, and make it right if our customers are not satisfied with what we delivered. We track virtually every customer interaction and we utilize the Net Promoter Score framework for assessing the satisfaction of our customers.

- ***Develop Our Network Focusing on Efficient Delivery and Management*** We are moving toward higher efficiencies and improved customer experience through automation, new technology and expanded geographic service areas. Our network architecture is a simpler mix of our fiber backbone, supported with fixed wireless ("FiWi"), WiFi and satellite.

- ***Relentlessly Simplify and Transform How We Do Business*** We believe we must reduce waste, which is defined as any activity that does not add value to its intended customer. Doing so improves the experience we deliver to our customers. We make investments in technology and process improvement, utilize the LEAN framework, and expect these efforts to meaningfully impact our financial performance in the long-term.

- ***Offer Broadband and Managed IT Solutions that Create Market Differentiation*** We are building on strength in designing and providing new products and solutions to our customers.

We believe we can create value for our shareholders by:

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

**2019 Operating Initiatives**

- Continue our focus on robust broadband growth as the foundation of our other initiatives.
- Ignite success in the Consumer customer market, including the Mass Market group, through the expansion and enhancement of our products, services and the supporting infrastructure.
- Continue to strengthen our Enterprise and Carrier customer group, which is the primary driver of our Business and Wholesale group, through increased focus on specific products and services.
- Improve market penetration of our MIT products and services.
- Build on our work in 2018 in the areas of network modernization through SD-WAN, Fixed Wireless Access, fiber fed Multi-Dwelling Units, Optical Transport Network modernization, and adding product capabilities that leverage our network.
- Effectively manage operating expenses and capital spending to improve our margin profile over the long term.
- Continue to meet our CAF II deployment obligations.
- Successful implementation of an IT project targeted at replacing several of our legacy IT systems.
- Continued emphasis on employee engagement and effective communication.
- Evaluate strategic opportunities in and out of Alaska that address scale and geographic diversification and reduce the risk of investments made in our company.

**Revenue Sources by Customer Group**

We operate our business under a single reportable segment. We manage our revenues based on the sale of services and products to the three customer categories listed below. Revenue in the following management's discussion and analysis is presented by customer and product category, combining revenue accounted for under ASC 606 and other guidance.

- **Business and Wholesale (broadband, voice and managed IT services)**

- **Consumer (broadband and voice services)**

- **Regulatory (access services, high cost support and carrier termination)**

***Business and Wholesale***

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

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

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

***Consumer***

We also provide broadband, voice and IT services to residential customers, including residential homes and multi-dwelling units. Given that our primary competitor has extensive quad play capabilities (video, voice, wireless and broadband) we target how and where we offer products and services to this customer group in order to maintain our returns. Our focus is to leverage the capabilities of our existing network and sell customers our highest available bandwidth. Our primary competitive advantage is that we offer reliable internet service without data caps, while our competitor, with certain exceptions, charges customers or throttles customers’ speeds for exceeding given levels of data usage. We experienced consistent growth in consumer broadband revenues in 2018. More recently, we expanded product and service offerings to this customer group and have implemented fiber fed WiFi and certain fixed wireless technology solutions for providing broadband, all of which have provided a basis for continued growth in this market in 2019.

***Regulatory***

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

The following table summarizes our primary sources of regulatory revenue and their contribution to total revenue in 2018 (dollars in thousands).

| Source | Description | 2018 Revenue | As a % of Regulatory Revenue | As a % of Total Revenue |
|---|---|---|---|---|
| **Access Charges** | | | | |
| | Interstate and intrastate switched access are services based primarily on originating and terminating access minutes from other carriers. Special access is primarily access to dedicated circuits sold to wholesale customers, substantially all of which is generated from interstate services. Cellular access is the transport of local network services between switches for cellular companies based on individually negotiated contracts. Access revenue has declined at an average of approximately 9% annually over the past three years. | $ 4,548 | 9.0% | 2.0% |
| ***Total Access Charges*** | | $ 4,548 | 9.0% | 2.0% |
| ***Surcharges*** | | | | |
| Pass-Through | We assess our customers for surcharges, typically on a monthly basis, as required by various state and federal regulatory agencies, and remit these surcharges to these agencies. These pass-through surcharges include Federal Universal Access and State Universal Access. These surcharges vary from year to year, and are primarily recognized as revenue, and the subsequent remittance to the state or federal agency as a cost of sale and service. The rates imposed by the regulators continue to increase. However, because the charges are only assessed on a portion of our services, and that portion continues to decline, we expect these revenue streams to decline over time as the revenue base declines. | $ 7,874 | 15.6% | 3.4% |
| Other | Other non-pass-through surcharges are collected from our customers as authorized by the regulatory body. The amount charged is based on the type of line: single line business, multi-line business, consumer or lifeline. The rates are established based on federal or state orders. These charges are recorded as revenue and do not have a direct associated cost. Rather, they represent a revenue recovery mechanism established by the FCC or the Regulatory Commission of Alaska. | $ 11,560 | 22.8% | 5.0% |
| ***Total Surcharges*** | | $ 19,434 | 38.4% | 8.4% |
| ***Federal and State Support*** | | | | |
| CAF II | In 2016, the FCC released the CAF Phase II order specific to Alaska Communications which transitioned from CAF Phase I frozen support to CAF Phase II. Funding under the new program generally requires the Company to provide broadband service to unserved locations throughout the designated coverage area by the end of a specified build-out period, and meet interim milestone build-out obligations. CAF II revenues are expected to be relatively stable through 2026. | $ 19,694 | 39.0% | 8.5% |
| COLR and CCL | The Company was designated by the State of Alaska as a COLR in five of the six study areas. In addition to COLR, the Company received CCL support. We did not receive COLR or CCL funding for the ACS of Anchorage study area. As a COLR we were required to provide services essential for retail and carrier-to-carrier telecommunication throughout the applicable coverage area. Effective in 2019, the COLR and CCL funding mechanisms were eliminated and replaced with the ENS funding mechanism. Funding levels under ENS are approximately half of those under the prior mechanisms. | $ 6,896 | 13.6% | 2.9% |
| ***Total Federal and State Support*** | | $ 26,590 | 52.6% | 11.4% |
| ***Total Regulatory Revenue*** | | $ 50,572 | | 21.8% |
| ***Total Revenue*** | | $ 232,468 | | |

**Executive Summary**

***Operating Revenues***

Total revenue of $59.1 million increased $0.9 million, or 1.5%, in the third quarter of 2019 compared with the third quarter of 2018. Business and wholesale revenue increased $2.4 million including a $2.0 million increase in wholesale broadband revenue. Rural health care revenue of $3.4 million in the third quarter 2019 compares with $3.8 million in 2018. Consumer revenue of $9.3 million was unchanged year over year. Regulatory access revenue declined $1.5 million due to the restructuring and contribution capping (and thereby reducing) of AUSF support. This decline was anticipated.

***Operating Income***

Operating income was $5.8 million in both the third quarter of 2019 and 2018. The growth in revenue was offset by higher operating expenses, consisting primarily of increased depreciation expense. These items are discussed in more detail below.

***Operating Metrics***

Business broadband average monthly revenue per user ("ARPU") of $346.97 in the third quarter of 2019 increased from $332.37 in the third quarter of 2018. Business broadband connections of 14,942 at September 30, 2019 declined marginally from connections of 15,372 at September 30, 2018. We count connections on a unitary basis regardless of the size of the bandwidth. For example, a customer that has a 10MB connection is counted as one connection as is a customer with a 1MB connection. While we present metrics related to Business connections, we note that we manage Business and Wholesale in terms of new Monthly Recurring Charges ("MRC") sold. Achievement of sales performance in terms of MRC is the primary operating metric used by management to measure market performance. For competitive reasons, we do not disclose our sales or performance in MRC.

Consumer broadband connections of 31,466 at September 30, 2019 declined from 32,741 at September 30, 2018, and consumer broadband ARPU of $69.87 in the third quarter of 2019 increased from $65.61 in the third quarter of 2018.

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

| | September 30, 2019 | September 30, 2018 |
|---|---|---|
| **Voice:** | | |
| At quarter end: | | |
| Business access lines | 67,606 | 70,110 |
| Consumer access lines | 23,565 | 26,497 |
| Quarter: | | |
| ARPU - business | $ 27.10 | $ 25.35 |
| ARPU - consumer | $ 33.98 | $ 32.05 |
| Year-to-date: | | |
| ARPU - business | $ 26.56 | $ 25.26 |
| ARPU - consumer | $ 34.41 | $ 32.21 |
| | | |
| **Broadband:** | | |
| At quarter end: | | |
| Business connections | 14,942 | 15,368 |
| Consumer connections | 31,466 | 32,773 |
| Quarter: | | |
| ARPU - business | $ 346.97 | $ 332.37 |
| ARPU - consumer | $ 69.87 | $ 65.58 |
| Year-to-date: | | |
| ARPU - business | $ 342.26 | $ 333.08 |
| ARPU - consumer | $ 68.28 | $ 65.55 |

***Liquidity***

We generated cash from operating activities of $42.6 million in the first nine months of 2019 compared with $46.9 million in the first nine months of 2018. Lower earnings in 2019 and increases in material and supplies were partially offset by lower accounts receivable associated with rural health care customers.

In the first nine months of 2019 and 2018, we invested a total of $32.0 million and $28.7 million, respectively, in capital, including capitalized interest and net of the settlement of items accrued in previous periods. Success based capital spending was $20.6 million in 2019 compared with $14.4 million in 2018.

Net debt (defined as total debt excluding debt issuance costs, less cash and cash equivalents) at September 30, 2019 was $156.6 million compared with $161.2 million at December 31, 2018. The decrease reflects cash generated from operating activities during in the first three quarters and net cash proceeds from the refinancing transaction, largely offset by capital spending and the increased principal balance of the 2019 Senior Credit Facility.

As described in more detail below, on January 15, 2019, the Company entered into an amended and restated credit facility which provides for a reduction in interest rates, extension of principal payment terms, increased borrowing capacity and resetting and widening of key covenant thresholds.

**RESULTS OF OPERATIONS**

**Three Months Ended September 30, 2019 Compared to Three Months Ended September 30, 2018**

The following table summarizes our results of operations for the three-month periods ended September 30, 2019 and 2018. Revenue and the associated analysis is presented by customer and product category, combining revenue accounted for under ASC 606 and other guidance.

| | Three Months ended September 30, | | | |
|---|---|---|---|---|
| (in thousands) | 2019 | 2018 | Change | % Change |
| Operating revenues: | | | | |
| Business and wholesale revenue | | | | |
| Business broadband | $ 15,654 | $ 15,368 | $ 286 | 1.9% |
| Business voice and other | 7,200 | 7,199 | 1 | 0.0% |
| Managed IT services | 1,789 | 1,480 | 309 | 20.9% |
| Equipment sales and installations | 942 | 1,488 | (546) | -36.7% |
| Wholesale broadband | 11,284 | 9,305 | 1,979 | 21.3% |
| Wholesale voice and other | 1,870 | 1,525 | 345 | 22.6% |
| Total business and wholesale revenue | 38,739 | 36,365 | 2,374 | 6.5% |
| Consumer revenue | | | | |
| Broadband | 6,718 | 6,539 | 179 | 2.7% |
| Voice and other | 2,567 | 2,719 | (152) | -5.6% |
| Total consumer revenue | 9,285 | 9,258 | 27 | 0.3% |
| Total business, wholesale and consumer revenue | 48,024 | 45,623 | 2,401 | 5.3% |
| *Growth in broadband revenue* | *7.8%* | | | |
| Regulatory revenue | | | | |
| Access | 6,181 | 7,682 | (1,501) | -19.5% |
| High cost support | 4,923 | 4,924 | (1) | 0.0% |
| Total regulatory revenue | 11,104 | 12,606 | (1,502) | -11.9% |
| Total operating revenues | $ 59,128 | $ 58,229 | $ 899 | 1.5% |
| Operating expenses: | | | | |
| Cost of services and sales (excluding depreciation and amortization) | 26,785 | 27,220 | (435) | -1.6% |
| Selling, general and administrative | 16,832 | 16,879 | (47) | -0.3% |
| Depreciation and amortization | 9,546 | 8,352 | 1,194 | 14.3% |
| Loss on disposal of assets, net | 198 | 15 | 183 | NM |
| Total operating expenses | 53,361 | 52,466 | 895 | 1.7% |
| Operating income | 5,767 | 5,763 | 4 | 0.1% |
| Other income and (expense): | | | | |
| Interest expense | (2,997) | (3,286) | 289 | -8.8% |
| Interest income | 121 | 36 | 85 | NM |
| Other income, net | 192 | 66 | 126 | NM |
| Total other income and (expense) | (2,684) | (3,184) | 500 | -15.7% |
| Income before income tax expense | 3,083 | 2,579 | 504 | 19.5% |
| Income tax expense | (1,084) | (774) | (310) | 40.1% |
| Net income | 1,999 | 1,805 | 194 | 10.7% |
| Less net loss attributable to noncontrolling interest | (23) | (12) | (11) | 91.7% |
| Net income attributable to Alaska Communications | $ 2,022 | $ 1,817 | $ 205 | 11.3% |

***Operating Revenue***

*Business and Wholesale*

Business and wholesale revenue of $38.7 million increased $2.3 million, or 6.5%, in the third quarter of 2019 from $36.4 million in the third quarter of 2018. Wholesale broadband revenue increased $2.0 million, Managed IT services increased $0.3 million and voice and other revenue increased $0.3 million. Business broadband revenue increased $0.3 million due primarily to an increase in ARPU to $346.97 in the third quarter of 2019 from $332.37 in the third quarter of 2018, partially offset by a decline in connections from 15,368 to 14,942 and lower rural health care revenue. Rural health care revenue of $3.4 million in the third quarter of 2019 decreased from $3.8 million in 2018, and represented 5.7% and 6.4% of consolidated revenue in 2019 and 2018, respectively. Equipment sales and installations were down $0.5 million. While connections and ARPU serve as data points to support the analysis of period-over-period changes in revenue, they are not critical indicators utilized by the Company to manage the Business and Wholesale customer group.

Business and wholesale revenue includes the amortization of deferred revenue for the three-month periods ended September 30, 2019 and 2018 as follows:

| | Three Months Ended September 30, | |
|---|---|---|
| | **2019** | **2018** |
| GCI capacity revenue | $ 522 | $ 522 |
| Other deferred capacity revenue | 619 | 545 |
| Total deferred capacity revenue | 1,141 | 1,067 |
| Other deferred revenue | 979 | 857 |
| Total | $ 2,120 | $ 1,924 |

*Consumer*

Consumer revenue of $9.3 million in the third quarter of 2019 was unchanged from the third quarter of 2018. Broadband revenue increased $0.2 million year over year as lower connections were offset by an increase in ARPU to $69.87 from $65.61. Voice and other revenue decreased $0.2 million due to 2,932 fewer connections, partially offset by an increase in ARPU to $33.98 from $32.05 in the prior year.

*Regulatory*

Regulatory revenue of $11.1 million decreased $1.5 million year over year due to lower access revenue resulting from reduced funding from the Alaska Universal Service Fund.

***Operating Expenses***

*Cost of Services and Sales (excluding depreciation and amortization)*

Cost of services and sales (excluding depreciation and amortization) of $26.8 million decreased $0.4 million, or 1.6%, in the third quarter of 2019 from $27.2 million in the third quarter of 2018. A $0.6 million decrease in access charges was partially offset by a $0.1 million increase in circuit installation costs and increases in network support, labor, permitting and other costs totaling $0.1 million.

*Selling, General and Administrative*

Selling, general and administrative expenses of $16.8 million decreased $0.1 million, or 0.3%, in the third quarter of 2019 from $16.9 million in the third quarter of 2018. This decrease reflects a $1.0 million decrease in the provision for doubtful accounts receivable, largely offset by a $0.8 million increase in labor costs.

*Depreciation and Amortization*

Depreciation and amortization expense of $9.5 million increased $1.2 million, or 14.3%, in the third quarter of 2019 from $8.3 million in the third quarter of 2018. This increase was due primarily to the completion of various capital projects, partially offset by certain assets reaching the end of their depreciable life.

***Other Income and Expense***

Interest expense of $3.0 million in the third quarter of 2019 declined from $3.3 million in the third quarter of 2018 due primarily to a lower average interest rate.

***Income Taxes***

Income tax expense and the effective tax rate in the third quarter of 2019 were $1.1 million and 35.2%, respectively, and include the impact of permanent book to tax differences of $0.2 million and 6.5%, respectively. Income tax expense and the effective tax rate in the third quarter of 2018 were $0.8 million and 30.0%, respectively.

***Net Loss Attributable to Noncontrolling Interest***

The net loss attributable to the noncontrolling interest of the AQ-JV was $23 thousand and $12 thousand in the third quarter of 2019 and 2018, respectively.

***Net Income Attributable to Alaska Communications***

Net income attributable to Alaska Communications of $2.0 million in the third quarter of 2019 compares with $1.8 million in the same period of 2018. The year over year results reflect the revenue and expense items discussed above.

**Nine Months Ended September 30, 2019 Compared to Nine Months Ended September 30, 2018**

The following table summarizes our results of operations for the nine-month periods ended September 30, 2019 and 2018. Revenue and the associated analysis is presented by customer and product category, combining revenue accounted for under ASC 606 and other guidance.

| | Nine Months ended September 30, | | | |
|---|---|---|---|---|
| (in thousands) | 2019 | 2018 | Change | % Change |
| Operating revenues: | | | | |
| Business and wholesale revenue | | | | |
| Business broadband | $ 46,358 | $ 46,036 | $ 322 | 0.7% |
| Business voice and other | 21,442 | 21,088 | 354 | 1.7% |
| Managed IT services | 4,965 | 3,936 | 1,029 | 26.1% |
| Equipment sales and installations | 2,830 | 3,870 | (1,040) | -26.9% |
| Wholesale broadband | 31,989 | 28,221 | 3,768 | 13.4% |
| Wholesale voice and other | 4,688 | 4,455 | 233 | 5.2% |
| Total business and wholesale revenue | 112,272 | 107,606 | 4,666 | 4.3% |
| Consumer revenue | | | | |
| Broadband | 19,880 | 19,726 | 154 | 0.8% |
| Voice and other | 7,947 | 8,355 | (408) | -4.9% |
| Total consumer revenue | 27,827 | 28,081 | (254) | -0.9% |
| Total business, wholesale and consumer revenue | 140,099 | 135,687 | 4,412 | 3.3% |
| *Growth in broadband revenue* | *4.5%* | | | |
| Regulatory revenue | | | | |
| Access | 18,563 | 23,321 | (4,758) | -20.4% |
| High cost support | 14,770 | 14,771 | (1) | 0.0% |
| Total regulatory revenue | 33,333 | 38,092 | (4,759) | -12.5% |
| Total operating revenues | $ 173,432 | $ 173,779 | $ (347) | -0.2% |
| Operating expenses: | | | | |
| Cost of services and sales (excluding depreciation and amortization) | 78,768 | 79,595 | (827) | -1.0% |
| Selling, general and administrative | 52,206 | 49,398 | 2,808 | 5.7% |
| Depreciation and amortization | 27,425 | 25,336 | 2,089 | 8.2% |
| Loss on disposal of assets, net | 101 | 56 | 45 | 80.4% |
| Total operating expenses | 158,500 | 154,385 | 4,115 | 2.7% |
| Operating income | 14,932 | 19,394 | (4,462) | -23.0% |
| Other income and (expense): | | | | |
| Interest expense | (9,149) | (10,191) | 1,042 | -10.2% |
| Loss on extinguishment of debt | (2,830) | - | (2,830) | NM |
| Interest income | 291 | 74 | 217 | NM |
| Other income, net | 192 | 79 | 113 | NM |
| Total other income and (expense) | (11,496) | (10,038) | (1,458) | 14.5% |
| Income before income tax expense | 3,436 | 9,356 | (5,920) | -63.3% |
| Income tax expense | (1,228) | (2,080) | 852 | -41.0% |
| Net income | 2,208 | 7,276 | (5,068) | -69.7% |
| Less net loss attributable to noncontrolling interest | (76) | (84) | 8 | -9.5% |
| Net income attributable to Alaska Communications | $ 2,284 | $ 7,360 | $ (5,076) | -69.0% |

***Operating Revenue***

*Business and Wholesale*

Business and wholesale revenue of $112.3 million increased $4.7 million, or 4.3%, in the nine-month period of 2019 from $107.6 million in the nine-month period of 2018. Wholesale broadband revenue increased $3.8 million, Managed IT services increased $1.0 million and voice and other revenue increased $0.6 million. Business broadband revenue increased $0.3 million due primarily to an increase in ARPU from $328.81 (excluding the estimated effect of the $0.6 million favorable rural health care adjustment described below) in 2018 to $342.26 in 2019, largely offset by lower rural health care revenue. Rural health care revenue of $10.9 million in the nine-month period of 2019 decreased $2.9 million from $13.8 million in 2018, and represented 6.3% and 8.0% of consolidated revenue in 2019 and 2018, respectively. Rural health care revenue in 2018 was favorably impacted by a $0.6 million cumulative adjustment for the effect of Funding Year 2017 funding increases. Equipment sales and installations were down $1.0 million.

Business and wholesale revenue includes the amortization of deferred revenue for the nine-month periods ended September 30, 2019 and 2018 as follows:

| | Nine Months Ended September 30, | |
|---|---|---|
| | **2019** | **2018** |
| GCI capacity revenue | $ 1,549 | $ 1,549 |
| Other deferred capacity revenue | 1,851 | 1,448 |
| Total deferred capacity revenue | 3,400 | 2,997 |
| Other deferred revenue | 2,799 | 2,429 |
| Total | $ 6,199 | $ 5,426 |

*Consumer*

Consumer revenue of $27.8 million in the nine-month period of 2019 declined $0.3 million from $28.1 million in the nine-month period of 2018. Broadband revenue increased $0.1 million year over year as lower connections were offset by an increase in ARPU to $68.28 from $65.55. Voice and other revenue decreased $0.4 million due to 2,932 fewer connections, partially offset by an increase in ARPU to $34.41 from $32.21 in the prior year.

*Regulatory*

Regulatory revenue of $33.3 million decreased $4.8 million year over year due to lower access revenue resulting from reduced funding from the Alaska Universal Service Fund.

***Operating Expenses***

*Cost of Services and Sales (excluding depreciation and amortization)*

Cost of services and sales (excluding depreciation and amortization) of $78.8 million decreased $0.8 million, or 1.0%, in the nine-month period of 2019 from $79.6 million in the nine-month period of 2018. A $2.3 million decrease in access charges and $0.7 million decrease in circuit installation costs were partially offset by increases in network support, labor, permitting and other costs totaling $2.2 million.

*Selling, General and Administrative*

Selling, general and administrative expenses of $52.2 million increased $2.8 million, or 5.7%, in the nine-month period of 2019 from $49.4 million in the nine-month period of 2018. This increase reflects a $5.1 million increase in labor costs, including $1.6 million of termination benefit expense for the Company’s former CEO, offset by a $2.1 million decrease in the provision for doubtful accounts receivable.

*Depreciation and Amortization*

Depreciation and amortization expense of $27.4 million increased $2.1 million, or 8.2%, in the nine-month period of 2019 from $25.3 million in the nine-month period of 2018. This increase was due primarily to the completion of various capital projects, partially offset by certain assets reaching the end of their depreciable life.

***Other Income and Expense***

Interest expense of $9.1 million in the nine-month period of 2019 declined from $10.2 million in the nine-month period of 2018 due to a lower average interest rate and borrowing levels. The loss on extinguishment of debt of $2.8 million in 2019 was associated with the settlement of the 2017 Senior Credit Facility in the first quarter.

***Income Taxes***

Income tax expense and the effective tax rate in the nine-month period of 2019 were $1.2 million and 35.7%, respectively, and includes the impact of permanent book to tax differences of $0.2 million and 6.7%, respectively. Income tax expense in the nine-month period of 2018 of $2.1 million reflects a $0.7 million benefit recorded in the first quarter to correct an overstatement of the income tax provision in 2017. Excluding this out-of-period adjustment, the income tax provision was $2.8 million and the effective tax rate was 29.7%.

***Net Loss Attributable to Noncontrolling Interest***

The net loss attributable to the noncontrolling interest of the AQ-JV was $76 thousand and $84 thousand in the nine-month periods of 2019 and 2018, respectively.

***Net Income Attributable to Alaska Communications***

Net income attributable to Alaska Communications of $2.3 million in the nine-month period of 2019 compares with $7.4 million in the same period of 2018. The year over year results reflect the revenue and expense items discussed above.

## FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

### Cash Flows

We satisfied our cash requirements for operations and capital expenditures in the first nine months of 2019 through internally generated funds and cash on hand. At September 30, 2019, we had $25.0 million of cash and cash equivalents, $1.6 million of restricted cash and $20.0 million available under our revolving credit facility.

On January 15, 2019, we completed a refinancing transaction. See the discussion under "Liquidity and Capital Resources" below.

Our major sources and uses of funds in the nine months ended September 30, 2019 and 2018 were as follows:

| | Nine Months Ended September 30, | | | |
|---|---|---|---|---|
| (in thousands) | | 2019 | | 2018 |
| Net cash provided by operating activities | $ | 42,620 | $ | 46,879 |
| Capital expenditures | $ | (31,556) | $ | (25,432) |
| Change in unsettled capital expenditures | $ | 583 | $ | (1,811) |
| Repayments of long-term debt | $ | (172,903) | $ | (29,164) |
| Proceeds from the issuance of long-term debt | $ | 180,000 | $ | 14,000 |
| Debt issuance costs and discounts | $ | (2,683) | $ | - |
| Cash paid for debt extinguishment | $ | (1,252) | $ | - |
| Purchase of treasury stock | $ | (1,812) | $ | - |
| Interest paid [1] | $ | (9,236) | $ | (10,723) |

[1] Included in net cash provided by operating activities.

***Cash Flows from Operating Activities***

Cash provided by operating activities of $42.6 million in the first nine months of 2019 reflects net income excluding non-cash items (defined as cash provided by operating activities excluding changes in operating assets and liabilities) of $34.0 million, a $5.8 million decrease in accounts receivable primarily associated with rural health care customers and $8.9 million of cash receipts associated with deferred revenue arrangements, partially offset by a $2.4 million increase in materials and supplies due to timing of construction projects.

Cash provided by operating activities of $46.9 million in the first nine months of 2018 reflects net income excluding non-cash items (defined as cash provided by operating activities excluding changes in operating assets and liabilities) of $36.5 million, cash receipts from the rural health program of $14.5 million (approximately $10.0 million of which was recorded as revenue in 2017) and $7.0 million of cash receipts associated with deferred revenue lease arrangements.

***Cash Flows from Investing Activities***

Cash used by investing activities of $31.9 million in the first nine months of 2019 consisted of expenditures on capital. Of $31.6 million incurred in 2019, $20.6 million was success based.

Cash used by investing activities of $28.7 million in the first nine months of 2018 consisted primarily of expenditures on capital totaling $27.2 million. Of $25.4 million incurred in 2018, $14.4 million was success based.

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

***Cash Flows from Financing Activities***

Cash provided by financing activities was $1.0 million in the first nine months of 2019. Proceeds from the issuance of long-term debt of $180.0 million consisted of Term A Facility of the 2019 Senior Credit Facility. Repayments of long-term debt of $172.9 million consisted primarily of settlement of the 2017 Senior Credit Facility and the initial principal payment of $1.1 million on the 2019 Senior Credit Facility. Debt discount, issuance and extinguishment payments totaling $3.9 million were associated with the refinancing transaction. Cash payments of $1.8 were associated with the Company's share repurchase program initiated in the second quarter of 2019.

Cash used by financing activities was $15.4 million in the first nine months of 2018. Repayments of long-term debt of $29.2 million included scheduled principal payments on the term loan components of our 2017 Senior Credit Facility of $5.0 million, repayment of draws totaling $14.0 million on the revolving credit facility and repurchase of the 6.25% Notes of $10.0 million. Proceeds from the issuance of long-term debt of $14.0 million consisted of draws on the revolving credit facility.

**Liquidity and Capital Resources**

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

We are responding to these challenges by (i) driving top line growth in broadband service revenues outside the rural health care market with a focus on business and wholesale customers; (ii) managing our cost structure to deliver consistent Adjusted EBITDA and Adjusted Free Cash flow performance; and (iii) prioritizing our capital spending.

On January 15, 2019, we entered into the 2019 Senior Credit Facility, consisting of an Initial Term A Facility in the amount of $180 million, a Revolving Facility in an amount not to exceed $20 million and a Delayed-Draw Term A Facility in an amount not to exceed $25 million. The 2019 Senior Credit Facility also provides for Incremental Term A Loans up to an aggregate principal amount of the greater of $60 million and trailing twelve month EBITDA, as defined. On January 15, 2019, proceeds from the Initial Term A Facility of $180 million were used to repay in full the outstanding principal balance of the Term A-1 Facility and Term A-2 Facility under the Company's 2017 Senior Credit Facility totaling $171.8 million, plus accrued and unpaid interest, pay fees and expenses associated with the Agreement and for general corporate purposes.

Principal payments on the Initial Term A Facility, Delayed-Draw A Facility and any amounts outstanding under the Incremental Term A Loans are due commencing in the third quarter of 2019 as follows: the third quarter of 2019 through the second quarter of 2020 – 0.625% per quarter; the third quarter of 2020 through the second quarter of 2022 – 1.25% per quarter; the third quarter of 2022 through the second quarter of 2023 – 1.875% per quarter; and the third quarter of 2023 through the fourth quarter of 2023 – 2.5% per quarter. The remaining outstanding principal balance, including any amounts outstanding under the Revolving Facility, is due on January 15, 2024.

The obligations under the 2019 Senior Credit Facility are secured by substantially all of the personal property and real property of the Company, subject to certain agreed exceptions. The 2019 Senior Credit Facility provides for events of default customary for credit facilities of this type, including non-payment defaults on other debt, misrepresentation, breach of covenants, representations and warranties, change of control, and insolvency and bankruptcy. The 2019 Senior Credit Facility contains customary representations, warranties and covenants, including covenants limiting the incurrence of debt, the payment of dividends and repurchase of the Company's common stock.

Financial covenants as defined in the Agreement are summarized below.

*Maximum Net Total Leverage Ratio*: The ratio of our (a) total debt, less unrestricted cash and cash equivalents held in pledged accounts, less cash drawn under the Delayed-Draw Term A Facility held for specified capital projects to (b) Consolidated EBITDA (as defined more specifically below) for the consecutive four fiscal quarters ending as of the calculation date. The maximum allowable net total leverage ratio is provided in the table below.

| **Period** | **Ratio** |
|---|---|
| January 15, 2019 through March 30, 2020 | 3.50 to 1.00 |
| March 31, 2020 through September 29, 2020 | 3.35 to 1.00 |
| September 30, 2020 through June 29, 2021 | 3.25 to 1.00 |
| June 30, 2021 through June 29, 2022 | 3.00 to 1.00 |
| June 30, 2022 and thereafter | 2.50 to 1.00 |

The actual net total leverage ratio was 2.90 at September 30, 2019.

*Fixed Charge Coverage Ratio:* The ratio of our (a) Consolidated EBITDA for the applicable period (as defined below) to (b) (i) the sum of, for the same period, consolidated interest expense, capital expenditures (with certain exceptions), long term indebtedness (with certain exceptions) required to be paid, capital lease obligations required to be paid, restricted payments, cash payments for income taxes, (ii) minus, for the same period, specified capital expenditures. The applicable periods for purposes of calculating this ratio are the fiscal quarter ending March 31, 2019; the two consecutive fiscal quarters ending June 30, 2019; the three consecutive fiscal quarters ending September 30, 2019; and the four consecutive fiscal quarters ending December 31, 2019 and thereafter. The minimum fixed charge coverage ratio is 1.10 to 1.00. The actual fixed charge coverage ratio was 1.32 at September 30, 2019.

*Consolidated EBITDA*, as defined in the 2019 Senior Credit Facility, is not a GAAP measure and is defined as consolidated net income attributable to Alaska Communications, plus (to the extent deducted in calculating net income) the sum of:

- cash and non-cash interest expense;
- depreciation and amortization expense;
- income taxes;
- other non-cash charges and expenses, including equity-based compensation expense;
- the write down or write off on any assets, other than accounts receivable;
- subject to limitation, fees, premiums, penalty payments and out-of-pocket transaction costs incurred in connection with the 2019 refinancing transactions;
- non-cash cost of goods sold associated with certain projects;
- subject to limitation, unusual, non-recurring losses, charges and expenses;
- one-time costs associated with permitted acquisitions;
- cost savings from synergies in connection with permitted acquisitions or dispositions;
- certain costs required to be expensed in connection permitted acquisitions; and
- investment losses of unconsolidated entities.

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

- unusual, non-recurring gains on permitted sales or dispositions of assets and casualty events;
- cash and non-cash interest income;
- other unusual nonrecurring items;
- the write up of any asset;
- patronage refunds or similar distributions from any lender;
- deferred revenue associated with certain projects; and
- investment income of unconsolidated entities.

The Initial Term A Facility, Revolving Facility, Delayed-Draw Facility and Incremental Term A Loans bear interest at LIBOR plus 4.5% per annum.

The weighted interest rate on the 2019 Senior Credit Facility was 6.26% at September 30, 2019.

Under the terms of the 2019 Senior Credit Facility, the Company is required to hedge interest payments on a minimum of $90.0 million, or 50%, of the outstanding principal. On June 28, 2019, the Company entered into interest rate swaps in the total notional amount of $135.0 million, effectively fixing the interest payments on 75% of the outstanding principle.

All terms are defined in the Agreement. See the "First Amended and Restated Credit Agreement, dated as of January 15, 2019, by and among Alaska Communications, as the borrower, the Company and certain of its direct and indirect subsidiaries, as guarantors, ING Capital LLC, as administrative agent, and the lenders party thereto," filed as Exhibit 10.1 to the Current Report on Form 8-K filed on January 22, 2019.

USAC has issued funding commitment letters for all of the Company's rural health care customer applications for Funding Year 2018 (July 1, 2018 through June 30, 2019). As of the date of this report, the Company's cost-based rural rates for Funding Year 2019 (July 1, 2019 through June 30, 2020) had not been approved by the FCC. Our accounts receivable balance for rural health care customers, net of amounts reserved, was $4.0 million at September 30, 2019 and $8.1 million at December 31, 2018.

We believe that we will have sufficient cash on hand, cash provided by operations and availability under our 2019 Senior Credit Facility to service our debt and fund our operations, capital expenditures and other obligations over the next twelve months. However, our ability to make such an assessment is dependent upon our future financial performance, which is subject to future economic conditions and to financial, business, regulatory, competitive entry and many other factors, many of which are beyond our control and could impact us during the time period of this assessment. See Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2018 for further information regarding these risks.

**OUTLOOK**

We expect to see continued strength in business and wholesale revenues, led by broadband revenue and managed IT services, focused on the larger enterprise and carrier customer segments. These revenue increases are driven by continued demand for broadband as businesses migrate their IT infrastructure to the cloud, deployment of small cell networks, expansion into managed IT services, investments by Federal agencies in long haul broadband infrastructure and continued progress in serving new school districts. We expect the rural health care segment to begin to stabilize in 2019 as a result of program funding increases announced by the FCC in 2018. However, the pricing methodology for funding year 2019 and beyond is uncertain. We expect to see solid performance from our carrier and federal customers as well as opportunities in markets enabled by the North Slope networks. Driven by our network investments in fiber fed WiFi and fixed wireless, we expect to become more competitive serving small business and residential customers, while we focus on improving profitability by enhancing our online and self-serve capabilities. Growth in these areas is expected to be somewhat offset by reduced regulatory access revenue and continued pressure in the rural health care program.

Additionally, we are focused on continued implementation of the CAF II program and expect to meet our obligations for 2019 by providing broadband coverage to an additional 10%, or approximately 3,200, of our target locations by the end of the year.

We also expect continued attention by our Board of Directors on the evaluation of value creating strategic opportunities that address our scale and geographic concentration issues.

**LEGAL**

We are involved in various claims, legal actions, personnel matters and regulatory proceedings arising in the ordinary course of business and as of September 30, 2019, we have recorded litigation accruals of $1.4 million against certain of those claims and legal actions. Estimates involved in developing these litigation accruals could change as these claims, legal actions and regulatory proceedings progress. See also Part II, Item 1. Legal Proceedings.

**EMPLOYEES**

As of September 30, 2019, we employed 555 regular full-time employees, 11 regular part-time employees and 5 temporary employees, compared with 584, 8 and 4, respectively at December 31, 2018. Approximately 53% of our employees are represented by the IBEW. Our Master Collective Bargaining Agreement (“CBA”) with the IBEW, which is effective through December 31, 2023, governs the terms and conditions of employment for all IBEW represented employees working for us in the state of Alaska. Management considers employee relations to be generally good.

**CRITICAL ACCOUNTING POLICIES AND ACCOUNTING ESTIMATES**

We have identified certain policies and estimates as critical to our business operations and the understanding of our past or present results of operations. For additional discussion on the application of significant accounting policies, see “Critical Accounting Policies and Estimates” in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2018. These policies and estimates are considered critical because they had a material impact, or have the potential to have a material impact, on our financial statements and because they require significant judgments, assumptions or estimates.

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

*New Accounting Pronouncements*

See Note 1 “*Summary of Significant Accounting Polices*” to the condensed consolidated financial statements for a description of recently adopted accounting pronouncements and recently issued pronouncements not yet adopted.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

As a smaller reporting company, the Company is not required to provide the information called for by this Item.

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

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

**Changes in Internal Control Over Financial Reporting**

Under the supervision and with the participation of our management, including our Principal Executive Officer and our Principal Financial Officer, we have evaluated any changes in our internal control over financial reporting that occurred during the third quarter of 2019 and have concluded that there were no changes to our internal control over financial reporting that materially affect, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

We are involved in various claims, legal actions, personnel matters and regulatory proceedings arising in the ordinary course of business. As of September 30, 2019, we have recorded litigation accruals of $1.4 million against certain current claims and legal actions. Other than as described above and as disclosed previously in Item 3. Legal Proceedings in our Annual Report on Form 10-K for the year ended December 31, 2018, we believe that the disposition of these matters will not have a material adverse effect on our consolidated financial position, results of operations or cash flows.

### ITEM 1A. RISK FACTORS

Other than as described below, there have been no material changes to the Company's risk factors as previously disclosed in Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2018. The changes to the risk factors described below, the first of which is an additional disclosure and the second of which is an updated disclosure, should be read in conjunction with those disclosed in our Annual Report on Form 10-K.

*We make substantial contributions to the Universal Service Fund and our methods for computing our contributions to that fund may be challenged.*

We make substantial contributions to the Universal Service Fund in the ordinary course of business. However, our services are continuing to evolve, and there is a lack of clarity about whether the FCC considers certain services to be “Telecommunications Services” subject to USF contributions, or “Information Services” not subject to such contributions. Given the lack of a comprehensive approach by the FCC to classify services, it is possible that our characterization of our services, past, present and future, may ultimately prove to be inconsistent with the FCC’s views, which could trigger additional USF contribution obligations.

We are unable to predict the duration, scope, or outcome of any investigation into these matters and any remedial action taken against the Company in connection with them could have a material adverse effect on our business, financial position, results of operations or liquidity.

*We may not receive some of the subsidies for Rural Health Care for which our customers have applied and amounts previously received may be challenged by the FCC.*

In response to the demand for support under the Rural Health Care Universal Service Support Program exceeding the available budget for Funding Year 2016 (July 1, 2016 – June 30, 2017) and Funding Year 2017 (July 1, 2017 – June 30, 2018), the FCC raised the annual program funding cap from $400 million to $571 million. The revised cap was initially applied to Funding Year 2017 to fully fund eligible funding requests for that year. The FCC also provided annual adjustments to the cap to reflect inflation and established a process to carry forward unused funds from past funding years, effective with Funding Year 2018.

The increased demand also prompted USAC, which administers the program, to engage in substantially more rigorous reviews of rural health care support, raising compliance costs and delaying issuance of support payments. In connection with that review, the Company received certain inquiries and requests for information from USAC, in connection with both current funding requests and, in a letter dated June 2, 2017 from USAC auditors concerning past support payments. To the Company’s knowledge, it responded fully to the USAC’s auditors’ inquires and requests as of December 21, 2018. In addition, the Company also received a letter of inquiry from the FCC’s Enforcement Bureau on March 23, 2018 regarding the Company’s participation in the Rural Healthcare Program. On November 5, 2019, the Company received another letter from the FCC Enforcement Bureau requesting additional information.

The rising uncertainty and unpredictability in the Rural Health Care program negatively impacted the Company’s revenue in 2017 and 2018, and may have a negative impact on future revenue and demand for our services from rural healthcare providers.

Also, we may be subject to further investigation of the Company’s compliance with FCC rules governing the Rural Healthcare Program for prior periods. Similar investigations of other companies have resulted in the FCC recouping certain previously awarded support funds, as well as imposing penalties.

We are unable to predict the duration, scope, or outcome of any investigation into these matters and any remedial action taken against the Company in connection with them could have a material adverse effect on our business, financial position, results of operations, or liquidity.

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

**Issuer Purchases of Equity Securities**

The following table presents the Company's repurchase of its common stock based on the date of trade during the three-month period ended September 30, 2019.

| Period | Total Number of Shares Purchased | Average Price Paid per Share (1) | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2) | Maximum Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (2) |
|---|---|---|---|---|
| July 1 - 31, 2019 | 395,338 | $ 1.84 | 395,338 | $ 9,069,319 |
| August 1 - 31, 2019 | 485,837 | $ 1.81 | 485,837 | $ 8,188,071 |
| September 1 - 30, 2019 | - | $ - | - | $ 8,188,071 |
| Total | 881,175 | $ 1.82 | 881,175 | |

(1) The average price paid per share includes brokerage commissions.
(2) In the second quarter of 2017, the Company's Board of Directors authorized a share repurchase program pursuant to which the Company may repurchase up to $10.0 million of its common stock effective March 31, 2017 through December 31, 2019.

**Working Capital Restrictions and Other Limitations on the Payment of Dividends**

Our 2019 Senior Credit Facility contains a number of restrictive covenants and events of default, including covenants limiting capital expenditures, incurrence of debt and the payment of dividends. The 2019 Senior Credit Facility also requires that we maintain certain financial ratios.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

## ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

## ITEM 5. OTHER INFORMATION

None.

**ITEM 6. EXHIBITS**

| Exhibit Number | Exhibit Description | Location |
|---|---|---|
| 3.1 | Amended and Restated By-Laws of Alaska Communications Systems Group, Inc., as Amended and Restated as of April 5, 2019. | Exhibit 3.1 to Form 8-K (filed April 9, 2019) |
| 4.1 | Amendment No. 1, dated as of October 15, 2019, to the Tax Benefits Preservation Plan, dated as of January 8, 2018, by and between Alaska Communications Systems Group, Inc. and Computershare Trust Company, N.A., as Rights Agent. | Exhibit 4.1 to Form 8-K (filed October 18, 2019) |
| 4.2 | Certificate of Elimination of the Series A Junior Participating Preferred Stock. | Exhibit 4.2 to Form 8-K (filed October 18, 2019) |
| 10.1* | Compensation Letter from Alaska Communications Systems Group, Inc. to Leonard Steinberg dated March 26, 2019. | Exhibit 10.2 to Form 10-Q (filed May 10, 2019) |
| 10.2* | Compensation Letter from Alaska Communications Systems Group, Inc. to Laurie Butcher dated March 26, 2019. | Exhibit 10.3 to Form 10-Q (filed May 10, 2019) |
| 10.3* | Separation Agreement and Officer's Release between Alaska Communications Systems Group, Inc. and Anand Vadapalli dated June 12, 2019. | Exhibit 10.4 to Form 10-Q (filed August 8, 2019) |
| 10.4* | Employment Agreement between Alaska Communications Systems Group, Inc. and Diedre L Williams dated September 20, 2019. | Exhibit 10.1 to Form 8-K (filed September 26, 2019) |
| 10.5* | Compensation Letter between Alaska Communications Systems Group, Inc. and William H. Bishop dated July 5, 2019 | Exhibit 10.1 to Form 8-K (filed July 5, 2019) |
| 10.6* | Employment Agreement between Alaska Communications Systems Group, Inc. and William H. Bishop effective October 14, 2019 | Exhibit 10.1 to Form 8-K (filed October 15, 2019) |
| 31.1 | Certification of William Bishop, Interim President and Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. | Filed herewith |
| 31.2 | Certification of Laurie Butcher, Senior Vice President of Finance, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. | Filed herewith |
| 32.1 | Certification of William Bishop, Interim President and Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. | Furnished herewith |
| 32.2 | Certification of Laurie Butcher, Senior Vice President of Finance, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. | Furnished herewith |
| 101.INS | XBRL Instance Document | Filed herewith |
| 101.SCH | XBRL Taxonomy Extension Schema Document | Filed herewith |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document | Filed herewith |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document | Filed herewith |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document | Filed herewith |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document | Filed herewith |
| * | Indicates a management contract or compensatory plan or arrangement. | |

**SIGNATURES**

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

**ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.**

| | |
|---|---|
| Date: November 7, 2019 | /s/ William Bishop<br>William Bishop<br>President and Chief Executive Officer<br>(Principal Executive Officer) |
| Date: November 7, 2019 | /s/ Laurie Butcher<br>Laurie Butcher<br>Chief Financial Officer<br>(Principal Financial and Accounting Officer) |

**Exhibit 31.1**

**Sarbanes-Oxley Section 302(a) Certification**

I, William Bishop, certify that:

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

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

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

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

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

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

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

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

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

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

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

Date: November 7, 2019

/s/ William Bishop
William Bishop
President and Chief Executive Officer
Alaska Communications Systems Group, Inc.

**Exhibit 31.2**

**Sarbanes-Oxley Section 302(a) Certification**

I, Laurie Butcher, certify that:

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

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

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

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

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

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

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

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

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

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

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

Date: November 7, 2019

/s/ Laurie Butcher
Laurie Butcher
Chief Financial Officer
Alaska Communications Systems Group, Inc.

**Exhibit 32.1**

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

In connection with the Quarterly Report of Alaska Communications Systems Group, Inc. (the "Company") on Form 10-Q for the period ending September 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, William Bishop, Interim President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

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

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

Date: November 7, 2019

/s/ William Bishop
William Bishop
President and Chief Executive Officer
Alaska Communications Systems Group, Inc.

**Exhibit 32.2**

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

In connection with the Quarterly Report of Alaska Communications Systems Group, Inc. (the "Company") on Form 10-Q for the period ending September 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Laurie Butcher, Senior Vice President of Finance of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

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

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

Date: November 7, 2019

/s/ Laurie Butcher
Laurie Butcher
Chief Financial Officer
Alaska Communications Systems Group, Inc.