BEFORE THE DIRECTOR OF COMMERCE AND CONSUMER AFFAIRS
OF THE STATE OF HAWAII

In the Application of McCAW CABLEVISION LIMITED PARTNERSHIP MAUI COUNTY/HAWAII COUNTY For Transfer of CATV Permits of MAUI CAMP CABLE TELEVISION, a Hawaii limited partnership, and CAMP, INC., a Hawaii corporation.	DOCKET NO. 00-84-01 ORDER NO. 110

DECISION AND ORDER

On September 20, 1984, the Hearings Officer's Recommended Decision was submitted to the Director and served on all parties. McCaw Cablevision Limited Partnership Maui County/Hawaii County (McCaw) accepted the provisions of the Recommended Decision, with certain clarifications, in its letter dated October 5, 1984. On October 11, 1984, the Director, through the Cable Television Administrator, sought clarification of this response. McCaw responded to this request by letter dated October 18, 1984.

Having reviewed the Recommended Decision, the McCaw letters dated October 5 and 18, 1984, and other pertinent information in this case, the Director hereby adopts the Hearings Officer's Recommended Decision (attached hereto as Attachment 1) as the final Decision in this proceeding, with the following clarifications and exceptions:

1. Additional debt financing. Condition 8 of the Recommended Decision suggested that the Director's approval be required for additional financing by McCaw in excess of $100,000. The intent of this condition is clarified as suggested in McCaw's October 5, 1984 response. Prior approval by the Director will be required for debt financing in excess of $100,000 which is over and above the proposed loan commitment amount at closing. McCaw's agreement to submit proposed debt financing instruments to the Director for prior approval also is incorporated in the final Order.

2. Management agreement. Condition 9 of the Recommended Decision is corrected by noting that the parties to the management agreement are McCaw and Communications, not McCaw and the general partner, McCaw Communications of Hawaii, Inc. (MCHI).

3. Acquisition costs. Condition 13 of the Recommended Decision suggested that Communications or its wholly-owned subsidiary MCHI, rather than the limited partnership McCaw, be required to pay acquisition costs in the total amount of

approximately $1.6 million. The Recommended Decision indicated that this requirement would 1) reduce the necessary amount of partnership loans, and therefore reduce the burden on subscribers attributable to the sale of the cable systems, and 2) demonstrate on the part of the new owner a greater commitment to the continued operation of the systems in Hawaii than appeared to be shown by MCHI's minimal equity contribution to the limited partnership.

The Recommended Decision suggests that if an additional $1.6 million were added to the sources of funds (by Communications' or MCHI's payment of the acquisition costs), the partnership debt could be reduced by this amount, and interest expenses borne by the partnership would also be reduced. McCaw's October 5 and 18, 1984 responses appear to indicate that it did not understand the intent of this recommended condition.

In its responses, McCaw stated that it will pay the acquisition costs with partners' equity contributions. McCaw suggested that this will mean that the acquisition costs will not result in interest expenses. McCaw noted that, since the partnership's financial projections were based on its payment of the acquisition fees, these projections will not change as a result of the equity financing of the acquisition costs.

Clearly, since moneys are fungible, if the partnership's financial structure remains the same, its interest expenses will not be affected by the designation of certain kinds of dollars to certain expenses. Therefore, the acquisition costs, like all other partnership expenses, will contribute to the partnership's interest burden, even if equity dollars are used to pay them.

However, McCaw also argued in its October 18, 1984 letter that the partnership's payment of the acquisition costs would benefit the partnership and subscribers because it would increase the rate of return to the limited partners and therefore reduce upward pressure on the rates. The Director understands this argument to be that a lower rate of return would discourage partners from investing additional funds, and therefore, there would be pressure to raise necessary funds through increased rate revenues. Conversely, it appears that there should be little pressure to raise rates unless revenues are needed for working capital, since increased revenues would tend to reduce partnership losses.

In its October 18, 1984 response, McCaw further indicated that it has agreed to waive consideration of the acquisition costs in any future request for rate increases. This may be of benefit if future rate cases are brought before the Director. However, on

October 30, 1984, federal cable television legislation was signed into law. Among other things, the law provides, under certain conditions, for the deregulation of certain aspects of cable television ratemaking for the next two years and possibly no regulation thereafter. McCaw has represented that its purchase of the Maui County and Ka'u cable systems will not in itself necessitate a rate increase. However, MCaw is expected to seek limited rate increases to offset inflation.

Based on testimony presented, the Director believes that success of the limited partnership syndication might be threatened if available losses were significantly reduced due to funding of the acquisition costs by MCHI or Communications. Further, the Director believes that the stability of the limited partnership would be decreased by this reduction of losses, as it would lead to earlier profitability and pressure to dissolve the partnership or to sell the system. Finally, the relationship of debt to equity as proposed for McCaw is already approximately 60 percent to 40 percent. This compares favorably with other successful cable operations in the state of Hawaii. For these reasons, the Director will not require MCHI's or Communications' funding of the acquisition costs as suggested in condition 13 of the Recommended Decision.

In its October 18, 1984 letter, MCHI also addressed the Hearings Officer's concern about the commitment of Communications to the continued operation of the cable systems in Hawaii. McCaw argued that Communications' commitment to the Hawaii cable systems is guaranteed by its desire to maintain credibility in the financial community. In addition, McCaw emphasized that since MCHI is a wholly-owned subsidiary of Communications, Communications has, in essence, committed resources equal to the obligations of the partnership to its operation in Hawaii. The Director notes that the partnership loan is secured in part by MCHI's guarantee and the pledge of 100 percent of its stock.

Finally, McCaw stated that it has waived its rights to withdraw as general partner of the partnership during the term of the partnership's operation of cable television systems in Hawaii. McCaw further stated that Communications has waived its rights to withdraw as manager of the Hawaii cable television system.

These representations satisfy the Director that Communications is committed to the continued operation of the Hawaii cable systems, and are included as condition 13 of the final Order. Additionally, the Director believes that the benefits promised the system by new ownership strongly favor the transfer and that the conditions of the Order, which include a requirement that all changes in management receive the Director's prior approval, provide the state with sufficient means to assure the cable systems' continued operation.

4. Maintenance of records. Condition 15 of the Recommended Decision is clarified as suggested in McCaw's October 5, 1984 letter. The partnership will be required to maintain records reflecting no step-up in basis in addition to the records the partnership is required to maintain which must show the full purchase price.

NOW, THEREFORE, IT IS HEREBY ORDERED that the application of McCaw Cablevision Limited Partnership Maui County/Hawaii County for transfer of CATV permits of Maui Camp Cable Television, a Hawaii limited partnership, and Camp, Inc., a Hawaii corporation, is APPROVED, with the following conditions:

1. By March 1, 1985, Communications shall submit, for the Director's prior approval, a list of investors who shall constitute the limited partners of McCaw.

2. Any and all changes in the limited or general partners or in the managerial and operating entities of McCaw shall require the Director's prior approval.

3. MCHI, the general partner of McCaw, shall be a corporation organized under the laws of the State of Hawaii. No fewer than fifty percent of the officers and directors of McCaw shall be residents of the state of Hawaii.

4. McCaw shall be a limited partnership organized under the laws of the State of Hawaii and shall have MCHI as its sole general partner.

5. MCHI as the general partner of McCaw shall be headed by a full-time, Hawaii-based executive possessing and exercising all powers traditionally vested in a chief executive officer.

6. All revenues of McCaw shall be deposited to, and all disbursements of McCaw shall be made from accounts maintained with a bank or other financial institution authorized under the laws of the State of Hawaii to engage in a general banking business in the state.

7. McCaw shall maintain complete accounting books and records, including invoices and other documentation and records of customer accounts at the system's headquarters to be located on the island of Maui. These records shall be maintained separately from those of any other business entity owned, controlled, managed or having any relationship with any general or limited partner of McCaw.

8. McCaw shall submit, for the Director's prior approval, copies of any agreements evidencing debt financing in excess of $100,000 over and above the amount at closing of the loan commitment described in section 4 of the Recommended Decision.

9. Any and all management agreements between McCaw and Communications, or any other managerial entity, shall require the Director's prior approval.

10. By March 1, 1985, McCaw shall submit, for the Director's prior approval, a plan for instituting a public awareness program to inform individuals, community associations and organizations that it provides cost-free cablecasting or re-cablecasting of social, cultural, ethnic, and athletic events and activities occurring in Hawaii. McCaw shall assist such organizations in video-taping, filming or otherwise recording these events and activities.

11. McCaw shall cablecast not less than seven hours per week of community programming. This programming may be material acquired from the sources described above or programming developed and produced by McCaw.

12. By October 1, 1985, McCaw shall either (1) enter into an agreement with Maui Community College for the shared use of the college's studio facilities by community access users or (2) in the event that such an agreement cannot be reached, construct, maintain or otherwise provide studio facilities and equipment capable of originating community access programming. The timing, determination of alternatives, and plans for studio facilities and equipment shall be subject to the Director's prior approval.

13. MCHI waives any rights it may have to withdraw as general partner of McCaw during the entire term of McCaw's operation of a cable television system in the state of Hawaii. Communications waives any rights it may have to withdraw as manager of the Hawaii cable television systems pursuant to the Management Agreement betweeen it and McCaw.

14. McCaw shall extend cable facilities to all potential subscribers in its permitted area on the terms described in Exhibit B, "Aid to Construction - Extension Policy Within Service Area," dated August 15, 1984, and attached hereto.

15. McCaw shall maintain accounts, ledgers and other documentation of its assets, liabilities, revenues and expenses which shall not reflect any "step up in basis" as a result of its acquisition of Camp and the additional expenses accruing thereunto.

16. McCaw shall complete all construction in accordance with the schedule entitled McCaw Exhibit A, "Plant Construction," dated 9/17/84, and attached hereto.

17. By January 1, 1986, McCaw shall submit to the Department an analysis of its financial condition upon completion of one year of operation, including as part of the analysis a summary of the actual or projected savings due to McCaw's limited partnership business form.

18. McCaw shall secure the Director's prior written approval before engaging in any type or form of business activity other than that allowed in its permits.

19. All conditions in Order 13, 47, 85, and 101, which are not superseded or amended by the Director's final Decision and Order shall remain in effect.

20. Any exercise by McCaw of the rights and privileges granted by transfer of Camp's permits will constitute agreement to these conditions.

RUSSEL S. NAGATA
Director of Commerce
and Commerce Affairs

Dated: November 14, 1984

CERTIFICATE OF SERVICE

I hereby certify that a copy of Decision and Order No. 110 was served upon each of the following by mailing the same, postage paid, on this 14th day of November, 1984:

John E. McCaw, Jr.
McCaw Communications Companies, Inc.
2000 - 116th Avenue, N.E.
Bellevue, Washington 98004

Monroe & Perry
Attention Wayne M. Perry, Esq. & Jennifer F. Marsh, Esq.
800 Fifth Avenue, Suite 4010
Seattle, Washington 98104

Robert S. Anderson
Maui Camp Cable Television
1977 Kaohu Street
Wailuku, Hawaii 96793

Case, Kay and Lynch
Attention Paul R. Mancini, Esq.
The Kahului Building, Suite 470
Kahului, Hawaii 96732

Rosemarie Takamoto
ROSEMARIE TAKAMOTO

BEFORE THE DIRECTOR OF COMMERCE AND CONSUMER AFFAIRS OF THE STATE OF HAWAII

In the Matter of the Application of McCAW CABLEVISION LIMITED PARTNERSHIP MAUI COUNTY/HAWAII COUNTY For Transfer of CATV Permits of MAUI CAMP CABLE TELEVISION, a Hawaii limited partnership, and CAMP, INC., a Hawaii corporation.	DOCKET NO. 00-84-01

RECOMMENDED DECISION

I. INTRODUCTION

On February 27, 1984, McCaw Cablevision Limited Partnership Maui County/Hawaii County ("McCaw") filed an application with the Department of Commerce and Consumer Affairs ("Department") to be the transferee of the permits and other assets of Maui Camp Cable Television ("Camp"), a Hawaii limited partnership, and Camp, Inc. ("Camp"), a Hawaii corporation.

Hearings were held to allow the public to participate in regulatory decision-making:

June 18, 1984	Ka'u High & Pahala Elementary School Cafetorium
June 19, 1984	Kahului School Cafetorium
June 20, 1984	Lanai Community-School Library
June 20, 1984	Kaunakakai School Cafetorium

Notices of the hearings were published in newspapers of statewide circulation on June 3 and June 10, 1984. All oral and written testimony offered at the public hearings and received by the Department is included in the record.

On June 21 and June 22, 1984, staff hearings were held at the Department of Commerce and Consumer Affairs, 1010 Richards Street, Honolulu, to examine McCaw's legal, technical, financial and administrative staff. A verbatim transcription of the hearings is included as part of the record.

II. LAW

Hawaii Revised Statutes (hereinafter "HRS") §440G-10 sets forth the authority of the Director to approve the transfer of a CATV permit. That section provides, in pertinent part:

ATTACHMENT 1

> No CATV permit may be assigned, sold, leased, encumbered, or otherwise transferred without the prior written consent of the director. Such consent shall be given only upon a written application therefor on forms to be prescribed by the director. The forms shall require from both the transferor and the proposed transferee substantially the same information as required by section 440G-6. The application shall also contain information concerning the consideration to be paid and such other matters as the director may deem appropriate or necessary, and shall be signed by both the transferor and the proposed transferee.

In the examination of transfer applications, the Department has been guided by the criteria provided in HRS S440G-8(b), relating to the issuance of new CATV permits. That section provides:

> The Director, after a public hearing as provided by this Chapter, shall issue a CATV permit to the applicant when he is convinced that it is in the public interest to do so. In determining whether a CATV permit shall be issued, the Director shall take into consideration, among other things, (1) the public need for the proposed service or acquisition, (2) the ability of the applicant to offer service at a reasonable cost to the subscribers, (3) the suitability of the applicant, (4) the financial responsibility of the applicant, (5) ability of the applicant to perform efficiently the service for which authority is requested, and (6) any objections arising from the public hearing, the CATV Advisory Committee, or elsewhere.

III. PUBLIC NEED FOR THE ACQUISITION

The primary goal of the cable program is the extension of quality cable communication services to all potential subscribers in the state.

Camp, in its original applications for permit areas, expressed a commitment to providing its subscribers with quality communication services. In the present application, Camp indicates that further expansion and improvements must be made to fulfill this commitment. Camp states, however, that its limited partners are small investors who, because of limited resources and an equally limited interest in cable communications, are unable or unwilling to invest the additional resources necessary to fund such expansion and improvements. Consequently, Camp states that it felt it necessary to look to new investors to finance the necessary changes and expansion and to provide the leadership of a mature cable communications system. This resulted in the present application by McCaw. Among the expansion and improvements which become economically possible as a result of the McCaw transfer are:

1. Expansion of 47.6 miles of plant according to the proposed construction schedule. This includes providing service to portions of Molokai and Lanai by year-end 1984. (See McCaw Exhibit A, attached.)

2. Completion of the inter-island microwave link network.

3. Construction of new earth station and microwave facilities.

4. Completion of a two-way microwave link between Wailuku and Molokai.

5. Plant rebuilding or reconstruction.

6. Provision of studio facilities and equipment to provide access and local origination capabilities.

Expansion of the Cable Systems and Aid-to-Construction Policy

Since receiving its permit to provide service on Maui eight years ago, Camp has generally followed a policy of requiring 35 subscribers per mile before extending cable communication services to a given geographic location. As of June 30, 1984, Camp had completed cable facilities to serve approximately 80% of potential subscribers.

McCaw Exhibit B, attached, describes its proposed aid-to-construction policy, that is, the conditions under which additional installation and/or monthly charges may be required for expansion of cable facilities to less densely populated areas. In essence, McCaw proposes to require such additional charges in areas where the number of subscribers per mile is less than 25.

McCaw's proposed aid-to-construction policy is more favorable to potential subscribers in less densely populated areas than Camp's existing policy as it reduces from 35 to 25 the number of subscribers per mile required for the minimum installation charge. Therefore, McCaw's proposed policy should expedite construction of cable systems to the less densely populated areas of the tri-island county.

Approval of the transfer to McCaw will make funding available to provide service to Lower Paia, Waikapu, Waihee, and Haiku sooner than would be possible without the transfer. Line extension charges for potential subscribers will continue to be required before services will be extended to Kaupo, Keanae, Olinda, and Ulupalakua. McCaw states it is uncertain when Kula will receive cable services as the economic viability of providing cable services to this area is dependent on the availability at reasonable cost of underground duct facilities.

In 1973, Camp constructed facilities to offer cable services to Pahala and Naalehu in the Ka'u District of the island of Hawaii. Camp now has the facilities to offer service to approximately 95% of potential subscribers in the Ka'u District. The Hawaiian Ocean View and Discovery Harbor subdivisions are presently without cable services and even under the changes in McCaw's proposed "aid-to-construction" formula will be subject to line extension charges.

Although Camp was awarded franchise authority in November 1983 to construct and operate cable systems on Lanai and Molokai, construction of cable facilities to serve these communities has not yet begun. However, Camp has indicated that cable facilities to those communities will be completed by year-end 1984 irrespective of the decision made in this proceeding, thus the desire for early cable service to these islands expressed by potential subscribers in the public hearings will be satisfied.

Interisland Microwave System

"Direct-feed" reception of broadcast signals, which is a means of enhancing the quality of signals transmitted throughout the cable system, is a condition of Camp's Maui permit. Camp has made limited progress in the construction and operation of the necessary microwave system to fulfill this condition.

Microwave facilities have been constructed on Lanai, Maui, and Molokai by Camp. Although tests have been made for a link between Oahu and Molokai, actual placement of equipment to achieve "direct-feed" transmission of broadcast signals has not become a reality.

McCaw has expressed a commitment to completing by mid-1985 the entire inter-island microwave system necessary for "direct-feed" transmission of broadcast signals to Camp's subscribers. However, the exact system to be constructed and operated from Oahu would be dependent upon the outcome of negotiations between McCaw and Group W/Kaiser Development Company for acquisition of Kaiser TelePrompter of Hawaii (the Hawaii Kai system operator). The outcome of these negotiations will determine whether the Maui system will get its initial signal transmission from Mauna Kapu or Koko Head, Oahu. The decision to be made is dependent upon whether McCaw will need a "direct-feed" signal in its operation of the Hawaii Kai cable communication system.

McCaw's proposals for an inter-island microwave network (without the Hawaii Kai acquisition) focuses on the completion of an RF link along the 63.14 mile path between Mauna Kapu, Oahu and Puu Nana, Molokai. McCaw proposes to use single channel equipment on the transmit site and a single multi-channel receiver at the receive site instead of the conventional method of using single FM transmitters as well as single channel receivers for the microwave link. This link will require a dedicated 702-foot discrete cable trunk from Oceanic Cablevision's Mauna Kapu site to the Hughes Microwave FM-AML transmitter at the Coast Guard's Mauna Kapu site and a receiving site at Puu Nana.

The dedicated cable link at Mauna Kapu will consist of five discrete video cables routed to the Coast Guard site. Composite baseband television signals will be fed into five single-channel FM modulators. Each will frequency-modulate a signal to a VHF frequency, which will then be upconverted to a microwave frequency by a simple heterodyne process. The five channels will be multiplexed together and transmitted to Molokai as 25-MHz FM signals, using microwave frequencies in the domestic services spectrum in the band 13.2 to 13.325 GHz. Each channel on the transmitter will provide the type-accepted power level of approximately 40 dBm. This high level of power is required for successful transmission on the long path between Mauna Kapu and Puu Nana.

The microwave signals will be received in Molokai by wideband receiver which will first block-downconvert all five channels from microwave frequencies to VHF frequencies, and then demodulate each channel back down to a composite baseband television signal. McCaw argues that unlike conventional FM microwave transmission and reception, a broadband receiver uses no receiving pre-selection filters or branching and all filtering and splitting will be done at IF stages; therefore, this will result in a stronger signal. McCaw further argues that this approach will yield a lower receiving system noise figure than that resulting from traditional FM video receiving techniques. In addition, the installation of a low-noise preamplifier will reduce the receiver noise figure from 8.0 dB to 5.0 dB, a substantial gain in the carrier-to-noise ratio. This will result in a signal which is more resistant to fading.

McCaw states that a high-powered FM-AML transmission system was chosen to ensure superior signal quality over an extended period of time. This transmission system can also be expanded to accommodate additional receive sites, channels, and two-way transmissions.

McCaw states that its proposed path studies show an expected signal reliability of 99.966% between Oahu and Puu Nianiau, Maui and a worst case reliability of 99.643% for the path from Oahu to Molokai, Lanai, Puu Nianiau and Maalaea, Maui. In general terms, this means that one could expect outage time of about 15 minutes a month for 99.966% reliability and two hours and 34 minutes a month for 99.643% reliability. In comparison, the telephone company designs its system for a reliability of about 99.996% on an outage time of less than two minutes per month.

There are methods that can be used to increase the microwave path's reliability, but all are costly. Therefore, McCaw proposes to utilize switching equipment that will substitute off-air signals for the microwave signals when there are microwave signal outages. This would provide continuous signals to subscribers, but at a lower quality, even when the microwave signals are lost. Therefore, the proposed system appears to provide a reasonable balance between improving the quality of cable signals and the cost of providing such service.

If McCaw acquires the Hawaii-Kai cable system, it does not plan to construct the Mauna Kapu facilities. Instead, it plans to arrange with Oceanic Cablevision to receive Oceanic's signals at Koko Head for transmission to its Hawaii-Kai system and for retransmission from that location to Molokai. All facilities mentioned above for Molokai, Lanai and Maui would remain the same as planned.

<u>Improvement of Maui Distribution Signals</u>

Camp presently distributes its cable signals through use of an AML microwave distribution network. Currently, a weak link in the distribution network is a path through Puu Nianiau to Hana. To clear a hill near the transmitter, this path employs a double passive reflector which results in signal loss. This leaves the Hana receiver with a fade margin which is inadequate to withstand the increased attenuation caused by rain in the transmission path. McCaw proposes to install a CARS LNA low noise preamplifier at the Hana AML receiver input to increase the system's fade margin and thereby provide greater protection from signal fading.

McCaw also proposes to upgrade the microwave network configuration of the existing transmission system from Wailuku to Puu Nianiau to provide increased flexibility in programming. Upon completion of the construction of the earth station at the AML transmitting site, the FM microwave uplink equipment now used to transmit satellite signals will be available to provide equal numbers of channels to all Maui hub systems and to provide new programming capacity.

<u>Construction of New Earth Station</u>

McCaw also proposes to replace Camp's existing Iao Valley earth station with a new installation located at the Puu Nianiau AML transmitter site. The present earth station signal transmission configuration requires modulation to VHF at the existing earth station site, transmission through a dedicated two-mile active cable plant, demodulation to video baseband, modulation to FM CARS, transmission to Puu Nianiau, demodulation to video baseband, modulation to VHF, and, finally, transmission via AML to the microwave hub sites for local distribution. Construction of a new earth station on Puu Nianiau will eliminate six of these signal-handling steps so that the noise level and the number of intermodulation distortion products present in the current system should be reduced.

The new earth station at the AML transmitting site will employ a seven-meter Simulsat antenna, manufactured by Antenna Technology Corporation. This antenna is capable of simultaneously receiving signals from all geosynchronous communications satellites within a 57-degree azimuthal arc, provided Hawaiian spot beams are employed or the main beam provides a 25.5 dBm effective isotropic radiated power. All but the Simulsat satellite antenna are designed to receive signals from only one satellite at a time. Use of the Simulsat antenna to receive signals from several satellites simultaneously is therefore a cost-effective way to increase the number of programming sources available to McCaw.

The Simulsat antenna uses an integrated feed structure design to compensate for spherical aberration loss to the extent that directivity, both E plane and H plane, closely approaches that of a parabolic antenna. The result is that this antenna, together with the Comsat Torus, is the only multiple-beam earth station antenna sufficiently directive to be licensed by the FCC for protection against terrestrial interference from future common carrier installations.

The Simulsat seven-meter antenna, when it is installed on the 32-yard concrete foundation, will operate without signal degradation in storms with wind speeds of 80 mph and will survive wind speeds of 125 mph without damage.

This earth-station antenna is manufactured with sufficient reflector surface dimensional tolerance to be capable of receiving the Ku band satellites as well as the C band satellites for which it is designed. The Ku band may be pressed into use for video transmission as the C band becomes congested. In addition to increasing the potential programming sources available to the system, this earth station will provide subscribers with near-studio picture quality.

Completion of Two-Way Microwave Link Between Wailuku, Lanai and Molokai

In the interest of furthering awareness and interest in community and access programming and serving the needs of its water-separated subscribers, McCaw has proposed the construction of two-way microwave transmission facilities between Wailuku, Lanai and Molokai. This will allow programming to be transmitted from Molokai throughout the Maui-Lanai systems. McCaw has indicated also that it intends to provide studio facilities and equipment to make possible effective use of microwave transmission capabilities between the islands.

Studio Facilities and Equipment for Community Origination and Access Programming

McCaw proposes, as part of its application, to construct a studio facility for local access and community programming if it is unable to reach an agreement with Maui Community College (MCC) for shared use of MCC's facilities. The studio to be constructed in the Maui system's office would have 500 square feet of air-conditioned space and be capable of transmitting live or taped programming.

Supporting these facilities would be a porta-pak camera and other programming equipment which would enable access and origination users to develop programming from different locations on the Valley Isle. McCaw also indicates that it will wire the Maui War Memorial Center so that programming can be transmitted from that facility to its entire cable system.

Further, McCaw indicates a willingness to develop plans to increase awareness of and interest in community programming among the residents of its service areas.

Given the isolated nature of the tri-island communities, the cable system serving them has a unique opportunity to promote a unifying community spirit by proving a vehicle for the sharing of news, activities and other communications. Active leadership demonstrated by regular programming of local events, activities and interests is needed to take full advantage of this opportunity.

The separation by approximately 13 miles of the major Ka'u communities of Naalehu and Pahala creates a need for a telecommunications system which would bring the two communities together to develop a "Ka'u" spirit. However, the small size of the Ka'u system hinders the economic development of a cable origination facility for Ka'u subscribers. McCaw has indicated to public hearing attendees that in the event public and private parties are willing to operate and provide a suitable location for local origination studio facilities, it would contribute equipment and cable facilities for program origination. Thus, the future development of local origination in Ka'u is dependent upon cable subscribers themselves.

IV. SUITABILITY OF THE APPLICANT

Ensuring operational stability of the State's cable systems is a primary objective of this Department. Two aspects of this application are of particular concern in this regard: 1) the method of financing chosen by McCaw to fund the purchase of Camp and 2) McCaw's management structure.

Financing the cable system.

McCaw proposes to finance the purchase of Camp through the combination of a loan to the partnership from the Bank of California (in which the Bank of Hawaii will be invited to participate) and equity raised by the sale of limited partnership interests.

Loan.

McCaw's loan commitment from the bank is for a total of $8 million. The initial revolving line of credit of $6,650,000 will become available when McCaw has obtained an equal amount in limited partnership subscriptions.

The loan terms are as follows:

1. $8,000,000 revolving line of credit to be converted on December 31, 1986 to a six-year term loan. As a term loan, the interest rate on the loan's outstanding balance will be at a floating rate of (a) 1.5% over prime rate when borrowing exceeds five times annualized cash flow; (b) 1.25% above prime rate when borrowing is equal to or less than five times annualized cash flow, but greater than four times cash flow; or (c) 1.0% above prime rate when borrowing is equal to or less than four times cash flow.
2. During the period when the loan is a revolving line of credit, McCaw will be required to pay only interest (no principal payments) at a rate of 0.5% on the unused balance of the credit line.
3. Principal payments on the term loan will be based on the original principal balance: (1) 5% in the first year, (2) 10% in the second year, (3) 15% in the third year, (4) 20% in the fourth year, (5) 25% in the fifth year, and (6) 25% in the sixth year.

4. Conditions affecting the maximum disbursement of funds will be as follows:

   a. A maximum of $6,650,000 may be disbursed initially, after an equal amount of equity has been contributed by the limited partnership.

   b. The total loan amount, including subsequent disbursement, shall not exceed five times the most recent quarter's cash flow.

   c. The ratio of bank debt per subscriber shall not exceed: (1) $630 until December 31, 1983; (2) $600 until June 30, 1985; (3) $550 until December 31, 1985; and (4) $500 thereafter.

5. There will be no secondary financing.

These terms appear to be acceptable and to provide adequately for the system's foreseeable funding requirements.

Limited partnership.

The Department has expressed reservations regarding the desirability of the limited partnership as a business form for holders of cable permits because it appears that this form inevitably leads to a restructuring of the company's ownership when the partnership begins to show profits. However, McCaw has proposed to create a limited partnership to purchase Camp. In support of its choice of business form, McCaw has made the following arguments:

1. A corporate business form would not encourage investment, as the venture, because of large capital expenditures and resulting book losses in the initial period, would be unable to provide reasonable returns on investment in the form of dividends. In the initial investment period, the limited partner is able to derive tax benefits from these losses, while a corporate shareholder gains nothing from these same losses.

2. As costs escalate, a corporation is pressured into raising subscriber rates to provide funding for improvements, taxes, and dividend payments as well as to show a positive "bottom line." This upward pressure on rates is not present with limited partners because their returns are in the form of tax benefits rather than dividends.

3. A limited partnership helps retain control of the cable system in the hands of a competent cable operator.

From the standpoint of financing, the limited partnership business form is an attractive one for encouraging investment in the cable system during the period of construction and improvement, when losses are likely to occur. The Department's concern, however, is that once the system becomes profitable, pressures build to dissolve the partnership or sell the system, because its tax advantages disappear. When the system's financial position becomes positive, generally, all profits in the limited partnership must be allocated to the partners. This creates a tax liability for them, even if the general partner decides to retain the earnings rather than pay the partners. This situation may in turn adversely affect the availability of funds to the partnership for future expansion and improvements. Additionally, the sale of a cable system to new owners is usually at an appreciated price, which may bear little relationship to past cost or depreciated value of the system's plant. The system's higher sale price often results in transfer applications which includes an increase in the system's debt burden. This tends to exert upward pressure on rates to meet expenses which are not directly related to increases in system costs for improvements in services or equipment.

In addition, these subsequent sales may result in changes in system leadership. McCaw's argument regarding using the limited partnership business form to ensure control of the system in the hands of a competent cable operator is not a compelling one for advocating use of that particular business form. The Hawaii Cable Television Systems Law places with the Director the authority to approve permit holders and the power to do all things necessary to ensure competent cable operations and control once a permit has been let. While a subsequent transfer process may offer a convenient vehicle for review of an operator, it would be more advantageous for the public to have cable services provided by a good operator on a continuing basis rather than risk losing this operator (and suffering the expense of processing another application) simply because the limited partnership form was chosen for financing purposes and that choice later resulted in the sale of the system.

<u>Depreciation.</u>

It should be noted that depreciation plays a substantial role in determining the profitability (and therefore, the stability) of a limited partnership. Non-cash depreciation expenses are used by a limited partnership to offset revenues and generate paper losses which can be passed on to the partners.

McCaw has submitted to the Department depreciation schedules based on two depreciation methods—Accelerated Cost Recovery System (ACRS) rules (for tax purposes) and Generally Accepted Accounting Principles (GAAP).

ACRS rules allow for shorter depreciation periods. Vehicles, other than construction vehicles, are depreciated over three years, cable plant, equipment, and furniture and fixtures are depreciated over five years. Under GAAP, vehicles are depreciated evenly over five years and cable plant, equipment, and furniture and fixtures over 12 years. In both methods, if an item is depreciated for only part of the first year, then the remaining part of its depreciation is reported in the year following the end of its depreciable life.

Since ACRS rules of depreciation allow higher yearly depreciation expenses, McCaw will utilize these rules to generate maximum tax benefits for its partners. Under this method, after six years, McCaw will have exhausted the major depreciation expenses available because of its purchase of Camp's assets. Depreciation expenses available thereafter will be much smaller because they will be based on the value of assets purchased since the transfer.

McCaw projects that it will increase its capital expenditures at that time (to approximately $900,000 in 1992 and $1 million in 1993). This will partially offset the tax consequences of losing its major depreciation expenses. However, the Department foresees that a change in the financial, and, possibly, ownership and operational, structure of McCaw may occur at that time.

Management capabilities.

McCaw testified that, through McCaw Communications Companies, Inc. (Communications), the parent of its general partner, McCaw has had a long-standing commitment and involvement in the telecommunications industry in Hawaii. Communications' predecessor companies were pioneer broadcasters in pre-statehood Hawaii. Among its early involvements was ownership of Island Broadcasting Company [licensee for radio stations KPOA-AM (Honolulu) and KILA-AM (Hilo)] from 1936 to 1959. Another early involvement was ownership of Radio Honolulu, Limited, the license holder of what is now KHON-TV, from 1953 to 1959.

McCaw also emphasized in its testimony Communications' experience in operating cable communications and paging services in sparsely populated areas which have natural barriers to operation (e.g., distance, mountains, over-water transmission requirements) similar to those encountered in providing cable services to the tri-island county of Maui. McCaw stressed Communications' successful development and use of microwave and other telecommunications equipment in serving such areas in Alaska and the Pacific Northwest.

McCaw cited Communications' ability and experience in serving the unique characteristics and needs of small, rural communities such as those found in Maui County. The company stressed the adaptability and sensitivity it could bring to providing the means for smaller communities to interact with the larger, more urban communities surrounding them.

Finally, McCaw noted in its application Communications' ability to keep pace with the demands of the fast-changing cable industry. It stressed the youth and vigor of its management and operating team while also emphasizing its experience and track record.

Communications' experience in providing cable services to communities similar to those now served by Camp and its expertise in microwave technology are well-suited to the Camp systems and should prove beneficial to its subscribers. However, one of the Department's concerns about Communications is the apparent lack of depth in its management team. The Department questions the team's ability to handle the substantial expansion into the additional telecommunications services that Communications is currently seeking. In the addition to the difficulties presented by the number of enterprises in which Communications is involved, these activities are geographically widely-separated. It appears that these demands will place severe strains on existing top management.

However, McCaw testified that it recognizes this possible weakness and therefore encourages strong regional leadership. Fortunately, McCaw plans to retain Robert S. Anderson, Camp's current president and general manager, for a minimum of five years, as McCaw's regional vice president. With Mr. Anderson's continuing leadership, weaknesses in Communication's management and leadership may be ameliorated. However, the Department's concern with the ability of Communications to provide adequate leadership and McCaw's decision to utilize the limited partnership form require that actual operational and administrative control of the cable system be maintained in

Hawaii. Consequently, the Hearings Officer recommends that McCaw be required to be operationally autonomous from Communications.

V. FINANCIAL RESPONSIBILITY AND ABILITY OF APPLICANT TO PROVIDE SERVICE AT REASONABLE COST

An important area of concern regarding Communications is that of its financial strength and capability to meet its commitments. As noted above, Communications' testimony indicates that it is an aggressive and fast-growing telecommunications company. With growth, however, comes a need to finance expansion. Communications' rapid growth has apparently precluded internal or stock financing of much of the expansion it has recently undertaken. Communications has come to rely heavily on institutional financing and limited partnership syndications.

As discussed in the previous section, the purchase of Camp will be made through a combination of loans and limited partnership subscriptions. Although Communications appears to have been successful in obtaining financing through these means, the Department is concerned that, as its loans come due and the tax advantages of its limited partnerships end, there will be increasing pressure on Communications to withdraw its commitment to continuing the operation of its Hawaiian cable systems. A greater financial investment by Communications in the purchase of Camp would demonstrate that Communications is committed to the cable system's long-term continuity and stability.

Cost of construction.

In its application for transfer, McCaw has proposed construction projects which will be of significant benefit to Camp subscribers. McCaw proposes to make capital expenditures of approximately \$2 million in 1984, \$1 million in 1985, and between \$400,000 and \$500,000 in the years 1986 through 1991.

The Department has developed several construction exhibits to illustrate changes in plant and expected investments by McCaw. Cable Exhibits 100 and 101 show gross plant investment by McCaw for the cable systems in the County of Maui and the County of Hawaii. Exhibit 101 shows that by year-end 1988 the gross investment by McCaw will be approximately \$11,500,000.

Cable Exhibit 102 shows that the estimated value of the system's fixed assets will be about \$7,064,000 at closing, \$2,536,000 less than the selling price of \$9,600,000.

Exhibit 102 also shows that the gross accumulated capital expenditures proposed by McCaw will approximate $4,500,000 by year-end 1988.

Cable Exhibit 103 shows capital expenditures from 1984 through 1988. Because of the timing of certain construction, McCaw expects that $570,000-worth of 1984 additions to plant will actually be paid for in 1985. Therefore, the amounts to be expended in 1984 and 1985 should be $1,913,883 and $1,155,280, respectively.

The following are approximate capital expenditures from 1984 through 1988:

1984	$1,913,900
1985	1,155,300
1986	511,500
1987	426,500
1988	441,900
TOTAL	$4,449,100

This schedule illustrates the large amounts of capital the limited partnership expects to spend in the first five years of operation.

McCaw's financial projections include rate increases during the first five years. However, Cable Exhibit 200 illustrates that McCaw should be able to meet its proposed requirements for capital and operational expenditures during these years even without rate increases. The Hearings Officer therefore believes McCaw has the ability to provide the proposed services at a reasonable cost to subscribers.

Acquisition Costs

McCaw's Sources and Uses exhibits show a requirement of $11,330,855 for the following purposes:

1.	Purchase Price	$ 9,600,000
2.	Acquisition Fee	480,000
3.	Miscellaneous Expenses	200,000
4.	Debt Acquisition Fee	80,000
5.	Investment Banker's Fee	855,855
6.	Legal Fees	115,000
	TOTAL	$11,330,855

Several of these costs will be incurred only because of the proposed transfer and the method selected by McCaw to finance the purchase of Camp. The Hearings

Officer does not believe that such costs should be borne by existing or future subscribers. Therefore, the Hearings Officer recommends that the general partner, McCaw Communications of Hawaii, Inc. (MCHI), or its parent, Communications, rather than the limited partnership, McCaw, be required to fund the following expenses:

1.	Acquisition Fee	$ 480,000
2.	Miscellaneous Expenses	200,000
3.	Debt Acquisition Fee	80,000
4.	Investment Banker's Fee	855,855
	TOTAL	$1,615,855

MCHI's or Communications' funding of these expenses will demonstrate the company's commitment to the Hawaiian system. Cable Exhibit 200 shows a Sources and Uses schedule adjusted to show the deletion of the four foregoing costs where McCaw's Time 0 and August-December 1984 columns have been combined into one column for 1984. Cash flow has also been adjusted to show no change in basic rates from 1984 through 1989. Furthermore, current borrowings were reduced by the amount of these costs, and required adjustments were made in interest due the bank, bank debt retired, unused bank funds and, of course, operational cash.

These adjustments result in savings to existing and future subscribers of about $1,704,000.

RECOMMENDATIONS

The Hearings Officer recommends approval of the request for transfer of the assets and permits of Camp to McCaw subject to the following conditions:

1. By March 1, 1985, Communications shall submit to the Director for his prior approval a list of investors who shall constitute the limited partners of McCaw.
2. Any and all changes in the limited or general partners or in the managerial and operating entities of McCaw shall require the prior approval of the Director.
3. MCHI, the general partner of McCaw, shall be a corporation organized under the laws of the State of Hawaii. No fewer than fifty percent of the officers and

directors of McCaw shall be residents of the State of Hawaii.

4. McCaw shall be a limited partnership organized under the laws of the State of Hawaii and shall have MCHI as its sole general partner.

5. MCHI as the general partner of McCaw shall be headed by a full-time, Hawaii-based executive possessing and exercising all powers traditionally vested in a chief executive officer.

6. All revenues of McCaw shall be deposited to, and all disbursements of McCaw shall be made from accounts maintained with a bank or other financial institution authorized under the laws of the State of Hawaii to engage in a general banking business in the state.

7. McCaw shall maintain complete accounting books and records, including invoices and other documentation and records of customer accounts at the system's headquarters to be located on the island of Maui. These records shall be maintained separately from those of any other business entity owned, controlled, managed or having any relationship with any general or limited partner of McCaw.

8. Any and all additional financing by McCaw in excess of $100,000 shall be subject to the approval of the Director.

9. Any and all management agreements between McCaw and its general partner, MCHI, or any other managerial entity shall require the prior approval of the Director.

10. By March 1, 1985, McCaw shall submit for the Director's prior approval a plan for instituting a public awareness program to inform individuals, community associations and organizations that it provides cost-free cablecasting

or re-cablecasting of social, cultural, ethnic, and athletic events and activities occurring in Hawaii. McCaw shall assist such organizations in video-taping, filming or otherwise recording these events and activities.

11. McCaw shall cablecast not less than seven hours per week of community programming. This programming may be material acquired from the sources described above or programming developed and produced by McCaw.

12. By October 1, 1985, McCaw shall either (1) enter into an agreement with Maui Community College for the shared use of the college's studio facilities by community access users or (2) in the event that such an agreement cannot be reached, construct, maintain or otherwise provide studio facilities and equipment capable of originating community access programming. The timing, determination of alternatives, and plans for studio facilities and equipment shall be subject to the prior approval of the Director.

13. All of the acquisition costs associated with the purchase of Camp by McCaw as described in section V of the Recommended Decision shall be the sole responsibility of MCHI or its parent, Communications, and shall not be paid by McCaw.

14. McCaw shall extend cable facilities to all potential subscribers in its permitted area on the terms described in Exhibit B, "Aid to Construction - Extension Policy Within Service Area," dated August 15, 1984, and attached hereto.

15. McCaw shall maintain accounts, ledgers and other documentation of its assets, liabilities, revenues and

expenses which shall not reflect any "step up in basis" as a result of its acquisition of Camp and the additional expenses accruing thereunto.

16. McCaw shall complete all construction in accordance with the schedule entitled Exhibit A, "Plant Construction," dated 9/17/84, and attached hereto.

17. By January 1, 1986, McCaw shall submit to the Department an analysis of its financial condition upon completion of one year of operation, including as part of the analysis a summary of the actual or projected savings due to McCaw's limited partnership business form.

18. McCaw shall secure the prior written approval of the Director before engaging in any type or form of business activity other than that allowed in its permits.

19. All conditions in Orders 13, 47, 85, and 101, which are not superseded or amended by the Director's final Decision and Order shall remain in effect.

20. Any exercise by McCaw of the rights and privileges granted by transfer of Camp's permits will constitute agreement to these conditions.

ROBERT A. ALM
Hearings Officer

Dated: September.20, 1984

PLANT CONSTRUCTION

Location	Miles	Construction Completion Date
Paia* (currently in construction)	9.1	2/85
Haiku*	1.0	12/84
Kahului		
6th Increment	1.0	12/84
12th Increment	4.0	12/84
Pukalani Terrace		
	3.0	2/85
	3.0	2/85
Lanai*	10.0	12/84
Molokai	12.0	12/84
Kahului		
9th Increment	1.3	4/85
Waikapu	1.7	3/85
Wailuku Heights	1.5	9.84
TOTAL	47.6	

*Per maps submitted to DCCA by Robert Anderson 7/11/84

McCAW EXHIBIT A

AID TO CONSTRUCTION

EXTENSION POLICY WITHIN SERVICE AREAS

Subscribers/Cable Mile	*Installation Fee Per Homes		
	Aerial	Underground with Conduit	Underground without Conduit
89 and Under			$25 plus Estimated Cost Divided by No. of Subscribers.
25 and Over	$25	$25	--
24 and Under	$25	$25	--
	Plus Charge of $.95 per foot over 200 feet and monthly fee will be increased proportionately for number of subscribers less than 25.		

*All fees are plus all applicable state and county taxes.

Policy applies to subscriber drops as well as plant extension.

McCAW EXHIBIT B

MAUI

CATEGORIES	1984	1985	1986	1987	1988	TOTALS
communications equipment	7800	0	0	0	0	7800
converters	627892	157310	132238	102393	112248	1132081
distribution system	5833262	305114	295762	234986	252879	6922003
furniture & fixtures	48122	1000	4900	1150	1251	56423
head-end	149000	3200	0	0	0	152200
leasehold	62818	1000	1070	1145	1225	67258
maintenance equipment	54530	2461	2633	2817	3014	65455
microwave equipment	741269	26200	12600	0	0	780069
origination equipment	27229	3000	3210	3435	3675	40549
satellite receive site	1081317	5100	0	0	0	1086417
test equipment	70730	2500	2675	2862	3062	81829
vehicles	415102	34985	37435	56593	42858	586973
TOTALS	9119071	541870	492523	405381	420212	10979057

KA'U

CATEGORIES	1984	1985	1986	1987	1988	TOTALS
communications equipment	0	0	0	0	0	0
converters	0	0	0	0	0	0
distribution system	363692	17496	18720	20031	21433	441372
furniture & fixtures	0	0	0	0	0	0
head-end	32387	0	0	0	0	32387
leasehold	0	0	0	0	0	0
maintenance equipment	4312	107	114	122	131	4786
microwave equipment	0	15000	0	0	0	15000
origination equipment	0	0	0	0	0	0
satellite receive site	21060	0	0	0	0	21060
test equipment	4312	107	114	122	131	4786
vehicles	3057	10700	0	800	0	14557
TOTALS	428820	43410	18948	21075	21695	533948

MAUI & KA'U

CATEGORIES	1984	1985	1986	1987	1988	TOTALS
communications equipment	7800	0	0	0	0	7800
converters	627892	157310	132238	102393	112248	1132081
distribution system	6196954	322610	314482	255017	274312	7363375
furniture & fixtures	48122	1000	4900	1150	1251	56423
head-end	181387	3200	0	0	0	184587
leasehold	62818	1000	1070	1145	1225	67258
maintenance equipment	58842	2568	2747	2939	3145	70241
microwave equipment	741269	41200	12600	0	0	795069
origination equipment	27229	3000	3210	3435	3675	40549
satellite receive site	1102377	5100	0	0	0	1107477
test equipment	75042	2607	2789	2984	3193	86615
vehicles	418159	45685	37435	57393	42858	601530
TOTALS	9547891	585280	511471	426456	441907	11513005

MAUI & KA'U

CATEGORIES	ALLOCATION	SPENDING	PLANT BALANCE
communications equipment	0	7800	7800
converters	0	1132081	1132081
distribution system	5164463	2198912	7363375
furniture & fixtures	31122	25301	56423
head-end	32387	152200	184587
leasehold	17818	49440	67258
maintenance equipment	56442	13799	70241
microwave equipment	385769	409300	795069
origination equipment	12229	28320	40549
satellite receive site	938577	168900	1107477
test equipment	56442	30173	86615
vehicles	368759	232771	601530
TOTALS	7064008	4448997	11513005

CABLE EXHIBIT 102

MAUI & KA'U

CATEGORIES	1984	1985	1986	1987	1988	TOTALS
communications equipment	7800	0	0	0	0	7800
converters	627892	157310	132238	102393	112248	1132081
distribution system	1032491	322610	314482	255017	274312	2198912
furniture & fixtures	17000	1000	4900	1150	1251	25301
head-end	149000	3200	0	0	0	152200
leasehold	45000	1000	1070	1145	1225	49440
maintenance equipment	2400	2568	2747	2939	3145	13799
microwave equipment	355500	41200	12600	0	0	409300
origination equipment	15000	3000	3210	3435	3675	28320
satellite receive site	163800	5100	0	0	0	168900
test equipment	18600	2607	2789	2984	3193	30173
vehicles	49400	45685	37435	57393	42858	232771
TOTALS	2483883	585280	511471	426456	441907	4448997

CABLE EXHIBIT 103

	1984	1985	1986	1987	1988	1989
SOURCES						
beginning balance	0	0	0	146461	337051	357569
cashflow	399824	1247920	1474173	1620355	1717179	1730161
equity contribution	6650000	0	0	0	0	0
asset sale	100000	0	0	0	0	0
current borrowing	4682976	631966	0	0	0	0
TOTAL SOURCES	11832800	1879886	1474173	1766816	2054230	2087730
USES						
purchase price	9600000	0	0	0	0	0
acquisition fee	0	0	0	0	0	0
misc. expenses	0	0	0	0	0	0
capital spending	1913883	1155280	511471	426456	441887	472505
interest-bank	193417	715196	809991	890990	872458	809376
bank debt retired	0	0	0	112319	382316	652313
debt acquisition	0	0	0	0	0	0
unused bank funds	10500	9410	6250	0	0	0
legal fees	115000	0	0	0	0	0
operational cash	0	0	146461	337051	357569	163536
TOTAL USES	11832800	1879886	1474173	1766816	2054230	2087730

CABLE EXHIBIT 200