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Public Utilities Commission

BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF HAWAII

Joint Application of CINCINNATI BELL, INC. HAWAIIAN TELCOM, INC. HAWAIIAN TELCOM SERVICES COMPANY, INC. AND WAVECOM SOLUTIONS CORPORATION for Approval (1) to Transfer Indirect Control of Licensees to Cincinnati Bell Inc.; (2) for *Pro Forma* Transfer of Control; (3) for Licensees to Participate in Certain Financing Arrangements and (4) to Modify and Extend Certain Waivers.	DOCKET NO. 2017-0208

DIVISION OF CONSUMER ADVOCACY'S
STATEMENT OF POSITION

Pursuant to the Hawaii Public Utilities Commission's ("Commission") Rules of Practice and Procedure, Hawaii Administrative Rules ("HAR") § 6-61-62, the Division of Consumer Advocacy ("Consumer Advocate") informs the Commission that it has completed its review of the joint application. Based upon that review, the Consumer Advocate hereby states that it does not object to the Joint Applicants'[1]

1 Hereinafter, Cincinnati Bell, Inc. ("CB"), Hawaiian Telcom, Inc. ("HTI"), Hawaiian Telcom Services Company, Inc. ("HTSC"), and Wavecom Solutions Corporation ("Wavecom") will be collectively referred to as "Joint Applicants".

requested relief described in the instant application subject to the Commission's adoption of recommended conditions that are meant to serve the consumers' interests. In summary, the Consumer Advocate recommended conditions that would require Joint Applicants to: 1) improve service quality; 2) provide greater clarity on its capital expenditures, or "CAPEX," commitment and to better illustrate how that commitment will benefit Hawaii, including the neighbor islands; and 3) provide reports or plans that will allow reasonable regulatory review of HTI's financial condition. The bases for the Consumer Advocate's recommendations are discussed below.

I. BACKGROUND.

A. APPLICANTS.

1. Hawaiian Telcom, Inc., Hawaiian Telcom Services, Inc., and Wavecom.

As described in greater detail in the application, HTI is a Hawaii corporation that is a wholly owned subsidiary of Hawaiian Telcom Communications, Inc. ("HTC"), which, in turn, is wholly owned by Hawaiian Telcom Holdco, Inc. ("Holdco"). Holdco is a Delaware corporation that is publicly traded on the NASDAQ stock exchange. HTI is the incumbent local exchange carrier in Hawaii that was originally chartered in 1883. HTI is a public utility that is subject to regulation by the Commission under Hawaii Revised Statutes ("HRS") Chapter 269. HTI provides local and intraLATA telecommunications services on a statewide basis. The Commission has approved a number of changes in ownership of HTI, including the changes approved in Docket Nos. 04-0140[2] and 98-0345.[3]

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2 Decision and Order No. 21696, Docket No. 04-0140, filed on March 16, 2005.

3 Decision and Order No. 17377, Docket No. 98-0345, filed on November 17, 1999.

HTSC is a Delaware corporation that is a wholly owned subsidiary of HTC that is also a Commission regulated provider of telecommunications services. HTSC received its Certificate of Authority to operate as a telecommunications carrier in the state of Hawaii as part of the approval in Docket No. 04-0140[4] and provides facilities-based intrastate telecommunications services throughout the State. The Commission also granted HTSC a Certificate of Registration to offer commercial mobile radio services in its Decision and Order No. 21892, filed on June 24, 2005, in Docket No. 05-0097. As a result of also receiving Federal Communications Commission ("FCC") authority to provide interstate toll service, HTSC provides interstate and intrastate long distance, high speed Internet, video services, and other data and telecommunications services.

Wavecom is a Hawaii corporation that is a HTI subsidiary, where the Commission approved the acquisition of Wavecom by HTI in its Decision and Order No. 30930, filed on December 28, 2012, in Docket No. 2012-0174. Wavecom was formerly known as Pacific Lightnet, Inc.[5] and received their Certificate of Authority to provide local exchange and intrastate long distance services within the State of Hawaii as a result of the Commission's approval in Decision and Order No. 18868, filed on August 31, 2001, in Docket No. 01-0157.

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4 The Commission authorized the expansion of the services that HTSC could provide in Decision and Order No. 24114, filed on March 31, 2008, in Docket No. 2007-0423.

5 Pacific Lightnet, Inc. was created as a result of the transaction where TM Communications, Hawaii, LLC, acquired the assets of GST Telcom Hawaii, Inc., a Commission regulated telecommunications services provider, who had filed for protection under Chapter 11 of the U.S. Bankruptcy Code.

2. Cincinnati Bell Inc.

CB is an Ohio corporation that, through its various subsidiaries, provides high-speed data, video, and voice solutions as an incumbent local exchange carrier to residential and business consumers in Cincinnati and other areas in Ohio, Indiana, and Kentucky. In addition, CB also provides telecommunications services as a competitive local exchange carrier in Ohio. CB also provides, through subsidiaries, other services, such as video, interstate long distance, and voice over internet protocol. CB is also in the process of acquiring OnX Enterprise Solutions Ltd. ("OnX"), a technology services and solutions provider in North America and the United Kingdom that provides IT and IT solution services.

B. PROPOSED TRANSACTION.

As described in greater detail in the application, the Applicants seek Commission approval of a combination whereby as a result of the Agreement and Plan of Merger ("Agreement")[6] by and among CB, Twin Acquisition Corp. ("Merger Sub"),[7] and Holdco, CB will acquire all of the equity interests in Holdco and will thus control HTI and its affiliates. Applicants assert that the transaction is valued at approximately $650 million.[8] Under the Agreement, Holdco shareholders will have the option to elect receiving either $30.75 in cash, 1.6305 shares of CB common stock, or a mix of $18.45 in cash, and 0.6522 shares of CB common stock for each share of Holdco, subject to proration

6 A copy of the Agreement, dated July 9, 2017, was provided as Exhibit A.

7 Merger Sub is a Delaware corporation formed for the purposes of the proposed transaction.

8 Application, at 8.

requirements that the aggregate consideration that CB pays to Holdco shareholders will be 60 percent cash and 40 percent CB common stock. After all of the outstanding stock of Holdco is acquired, Merger Sub will merge with and into Holdco, after which Merger Sub will cease to exist and Holdco will be the surviving corporation. This will result in Holdco being a direct, wholly-owned subsidiary of CB. The proposed transaction will not otherwise affect the corporate structure of Holdco.[9]

Joint Applicants assert that the transaction will occur entirely at the holding company level and will not affect the day-to-day operations, billing systems, or operational support systems of HTI.[10] HTI will retain its name and brand identity. Joint Applicants assert that the proposed transaction should be transparent to customers and will not result in any service changes to Hawaii customers. Joint Applicants further assert that the proposed transaction will not require any procedures to notify customers nor require other filings or authorizations that might otherwise be required under the FCC's carrier selection rules or under HRS § 269-16.92.[11]

It should be noted that Joint Applicants indicate that, if the proposed combination is approved, HTI and CB are considering merging Holdco and HTC into CB. If merged,

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9 In its review of most other merger/acquisition transactions, the Consumer Advocate will evaluate the proposed transaction, including the sale price, to determine whether, if the proposed transaction is approved, existing shareholders may be getting a windfall or a premium that might ultimately be passed on to consumers in the form of higher rates. In this instance, since HTI operates in a fully competitive retail market, HTI would not be able to pass on any transaction premium or transaction costs to consumers without encouraging existing or potential customers to find more cost-effective alternatives from HTI's competitors. Thus, the Consumer Advocate will not be offering an analysis of the transaction and whether there may be a premium in the price offered. Joint Applicants have asserted, however, that the customers will not bear any merger, transition, and integration costs. See response to CA-IR-28.

10 Application, at 9.

11 Application, at 9.

this restructuring would result in a pro forma transfer of direct stock ownership of HTI and HTSC to CB. Thus, in addition to the transaction already described, Applicants are also seeking Commission approval of this transaction even if this transaction is only being contemplated at this time. If this transaction is to occur, it is not expected to occur simultaneously with the closing of the combination. The Consumer Advocate does not object to this possible reorganization as described since it does not appear to create the potential for any adverse impacts on Hawaii customers.[12] If, however, this possible future reorganization will be implemented differently, the Consumer Advocate recommends that the Commission require the Joint Applicants to file an application, which should identify and describe the differences in the reorganization as compared to what is described in the instant application to determine whether there might be any adverse effects on HTI, HTSC, or Wavecom or the companies' customers.

II. DISCUSSION.

A. REVIEW STANDARD.

In seeking Commission approval of the requested relief, Applicants indicate that their application is filed pursuant to HRS §§ 269-7(a), 269-17, 269-17.5, and 269-19 as well as HAR §§ 6-61-101 and -105.

The Consumer Advocate respectfully submits the following comments and analyses that examine the Joint Applicants' proposed merger application. In deciding whether to recommend that the Commission should approve the merger application, it is necessary to find that the Joint Applicants are fit, willing, and able to pursue the merger

[12] Response to CA-IR-23.

and that the merger is in the public interest. In the past, this review standard has been referred to as the "Fitness and Public Interest" standards.[13] In general, when the Commission has reviewed proposed mergers or acquisitions, the Commission applied the standard of review of HRS §269-7.5, which requires that the applicant must be "fit, willing, and able properly to perform the service proposed."[14]

Recently, the Commission has provided further guidance as to how the Commission will review proposed mergers and/or acquisitions in its Order No. 33795, filed on July 15, 2016, in Docket No. 2015-0022 ("Order No. 33795"), wherein the Commission provided its *Appendix A – Commission Guidance for Any Future Merger or Acquisition Proceedings* ("Appendix A"), wherein the Commission's guidance to future merger applicants that the determination of its public interest standard would focus on the following six key areas: (1) ratepayer benefit, (2) mitigation of risks, (3) achievement of the State's clean energy goals, (4) competition; (5) corporate governance, and (6) corporate transformation.[15] While Appendix A contains provisions that are clearly focused on the electric industry , the Commission made clear in Order No. 33795 that it set forth the "specific guidance concerning the elements and issues that should be included and addressed in any future application addressing a proposed merger, acquisition, or other change or corporate control involving the HECO Companies <u>or other utilities</u> in the

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13 <u>See</u>, <u>e.g.</u>, Decision and Order No. 21696, Docket No. 04-0140, at 13.

14 <u>See</u>, <u>e.g.</u>, Decision and Order No. 21696, Docket No. 04-0140, and Decision and Order No. 19658, Docket No. 02-0060, filed on September 17, 2002.

15 Order No. 33795, Docket No. 2015-0022, Appendix A, at 2 – 17, filed on July 15, 2016. It should be noted that the Consumer Advocate's analysis will apply the Commission's guidance where feasible or practical but will not discuss areas where the Commission's guidance clearly does not apply to the Joint Applicants' request, such as the achievement of the State's clean energy goals.

State"[16] (emphasis added). Thus, the Consumer Advocate's review sought to ensure analysis of the issues relating to both the Fitness and Public Standard as well as Appendix A.

B. FIT, WILLING, AND ABLE.

1. Fitness.

In reviewing whether an applicant is fit, the Commission should review financial fitness as well as technical fitness to determine whether they are capable of providing the services in a safe and reliable manner. Given that the Joint Applicants each separately have a long history of providing telecommunications services, it appears that they are capable of doing so on a going forward basis. Given the assertion that the proposed transaction should not affect local management should provide assurances that the existing fitness should not be adversely affected. However, as will be discussed further when the Consumer Advocate is discussing the ability of the Joint Applicants, there are concerns with the customer service that is being provided.

The Consumer Advocate's financial fitness review encompasses an evaluation of whether Joint Applicants have the ability to raise funds in the capital markets to successfully complete the merger as well as sufficient financial fitness to continue to exist as a going concern after the proposed transaction is consummated.

In order to provide support for finding that the Joint Applicants have the ability to finance the proposed transaction, Exhibit C was provided. Exhibit C provides copies of relevant documents, such as the commitment letter with Morgan Stanley Senior Funding,

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16 Order No. 33795, at 6.

Inc., for the refinancing of existing debt and additional funds needed for the proposed transaction. The nature of the documents provided is further described on pages 10 and 11 of the application. Based on a review of attached Exhibit C, the Joint Applicants have the ability to finance the merger.

Perhaps more importantly, the evaluation of financial fitness should also consider whether the Joint Applicants can successfully run the business after the merger. Based on review of publicly available financial statements, CB appears to be financially fit and should be able to sustain itself and existing subsidiaries. Joint Applicants assert that the proposed transaction will facilitate HTI's ability to obtain and maintain financing on more favorable terms than on a stand-alone basis and that the proposed transaction will improve HTI's financial health. To support their ability to successfully run HTI on a post-transaction basis, the Joint Applicants filed Exhibit K, which, as discussed on pages 25 and 26 of the application, is a confidential document that reflects "data regarding the combined companies' financial performance."[17] After reviewing Exhibit K, the Consumer Advocate determined that Exhibit K alone is inadequate for the purpose of determining whether a finding of financial fitness has conclusively been addressed.

The Joint Applicants' Schedule K is a pro forma [redacted] for the [redacted] in support of the merger application[18] but, by itself, this analysis is inadequate for the purpose of determining or understanding the impact of the merger on HTI and its customers. It is inadequate, first, because the exhibit provides data on a total combined company basis. The combined company includes HTI, CB, and all other CB affiliates.

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17 Application, footnote 25 on page 25.

18 Confidential Exhibit K: Hawaiian Telecommunications

There is no [redacted] that provides data on [redacted] after the merger transaction has been completed. Since the results only provide [redacted] results, Exhibit K may provide the means by which to review CB's [redacted] pro forma and CB's [redacted] health, but the Consumer Advocate contends that Joint Applicants should provide [redacted] data that would allow the Commission and Consumer Advocate to determine, with more specificity, where and when financial assistance might be needed (if at all) by HTI and how CB's financial performance can meet HTI's specific needs and/or improve its condition. Second, the analysis is inadequate because it does not provide any data on [redacted]. Since Joint Applicants have only provided its pro forma [redacted] in Exhibit K, regulators are also unable to evaluate the pro forma [redacted] and other information that support the pro forma [redacted]. Without such support, in order to evaluate the pro forma analyses, either gross assumptions will have to be made regarding whether the pro forma analyses are reliable or regulators will be required to adopt a "trust me" position and simply accept the analyses at face value.

The pro forma information is integral to the Commission's evaluation of whether future operations will be able to support the necessary capital expenditures that will be required to reliably, cost-effectively, and safely serve customers. Capital expenditures include the purchase and installation of equipment and facilities. Expenditures are necessary not only to maintain the current network in order to provide safe and reliable service but also to upgrade HTI's network to provide high speed data service, video service, advanced business, and wholesale services.

According to the Joint Applicant's [redacted], total company [redacted] starts at [redacted] and is [redacted] to approximately [redacted]. The sum of annual [redacted] for the [redacted] is [redacted]. Comparing these amounts to the [redacted] shows that [redacted] is estimated to be [redacted] in [redacted] of the forecast. Over the [redacted], [redacted] are estimated to be [redacted]. Over the [redacted] period [redacted] by [redacted]. This observation suggests that, since [redacted] are [redacted], the combined companies will have [redacted] the forecasted [redacted]. While there is no requirement that [redacted] should be greater than or less than [redacted], if [redacted] need to be increased to support the provision of next generation services, Schedule K provides information that suggests that [redacted] would be a readily available source of funds. This conclusion, however, relates to the pro forma projections for the combined companies and, as mentioned earlier, demonstrating the potential benefit that the proposed transaction might have on HTI's pro forma operations and CAPEX is impossible to evaluate using only Schedule K.

In responses to data requests, the Consumer Advocate obtained information regarding the CAPEX of HTI on a stand-alone basis. Actual CAPEX for [redacted] were [redacted] respectively.[19] Estimated CAPEX are expected to be [redacted] in the post-merger years [redacted].[20] These

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19 Confidential Restricted Exhibit CA-IR-42(a), page 125 of 778.

20 Confidential Restricted Exhibit CA-IR-42(a), page 165 of 778.

estimates indicate that CB [redacted] years [redacted]. During the forecasted [redacted], HTI estimated [redacted] is estimated to be [redacted] compared to an estimated [redacted]. Thus, as discussed earlier, this comparative relationship between forecasted [redacted] and the forecasted [redacted] suggests that the entire HTI [redacted] is [redacted].

As part of its financial fitness review, the Consumer Advocate sought to analyze actual and forecasted results of operations, including revenues. Revenue growth is estimated for three major groups of customers: [redacted], and [redacted]. As mentioned earlier, since Schedule K was limited to a pro forma [redacted], all of the revenue estimates were obtained from responses to data requests.

CB management estimated that HTI revenue would grow at a [redacted] annual growth rate of [redacted]. After that the growth in revenue would [redacted]. Each of the [redacted]. [redacted] revenue growth [redacted]. [redacted] revenue growth [redacted], and [redacted] revenue growth [redacted].[21]

Net [redacted] are forecasted to [redacted], with approximately [redacted] lines [redacted] than [redacted]. However, due to a [redacted] in

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21 Confidential Restricted Exhibit CA-IR-42(a), page 203 of 778.

[redacted], revenue associated with [redacted].[22] [redacted] revenue growth will be centered on [redacted]. These services are projected to [redacted].[23] The [redacted] in revenue in these services appears [redacted] because: (1) the [redacted] national projections;[24] (2) the number of [redacted] in Hawaii is [redacted],[25] and (3) [redacted] were [redacted] amounts in recent years.[26]

[redacted] revenue [redacted] is driven by the projected [redacted] in [redacted]. HTI is projected to [redacted] the number of [redacted]. This amounts to an average annual [redacted]. Currently, [redacted] levels are approximately [redacted].[27] Because HTI serves [redacted], the number of [redacted], [redacted], represents [redacted].[28] Because [redacted] in Hawaii, serving approximately [redacted], HTI must [redacted] customers in order to

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22 Id.

23 Confidential Restricted Exhibit CA-IR-42(a), page 354 of 778.

24 Confidential Restricted Exhibit CA-IR-42(a), page 298 of 778.

25 Confidential Restricted Exhibit CA-IR-42(a), page 294 of 778.

26 Confidential Restricted Exhibit CA-IR-42(a), page 320 of 778.

27 Confidential Restricted Exhibit CA-IR-42(b), page 31 of 337.

28 Confidential Restricted Exhibit CA-IR-42(b), page 31 and 32 of 337.

meet its [redacted]. In addition, it is not clear if HTI CAPEX will expand its [redacted] fast enough to meet its [redacted] goals.[29]

HTI also projects that its [redacted] revenue will grow. This growth is associated with [redacted] in the historic period to approximately [redacted].[30] In addition, HTI projects an increase in its [redacted]. HTI again [redacted]. The Internet download speeds available on HTI's network depend on whether fiber-to-the-home ("FTTP") or fiber-to-the-curb ("FTTC") networks are available. Where the FTTP exists, HTI can provide a maximum download speed of 1000 Mbps. This speed is faster than Charter's maximum speed of 300 Mbps. However, Charter can provide that speed (300 Mbps) to all of its customers, while HTI can supply that speed to only 47% of its broadband capable customers.[31] Moreover, 44.9% of HTI's customers cannot obtain service at 25 Mbps, the FCC standard for reasonable broadband service. In census blocks where both HTI and Charter provide broadband service, 43.6% of HTI's customer cannot obtain service at 25 Mbps, while all of Charter's customers can obtain 300 Mbps service.[32] Attachment 3 shows the limited number of census blocks where HTI provides service and Charter does not. Comparative service areas are depicted on maps on Attachments 5 to 8. These maps on

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[29] Confidential Restricted Exhibit CA-IR-42(a), page 323 of 778.

[30] Confidential Restricted Exhibit CA-IR-42(a) page 203 of 778, and Confidential Restricted Exhibit CA-IR-42(b), page 32 of 337.

[31] See Table 1. The source data for tables 1, 2, 3 and 4 are the FCC 477 reports found at https://www.fcc.gov/general/broadband-deployment-data-fcc-form-477 and Census data found at https://www.census.gov/geo/maps-data/data/tiger-data.html.

[32] See Table 2.

Attachments 5 to 8 show the areas where both Charter and HTI provide broadband service, where only HTI provides broadband service and where only Charter provides broadband service.[33] Clearly the tables and maps on Attachments 1 through 8 demonstrate that HTI faces significant competitive pressure as it attempts to meet its projected growth in Internet service revenue.

The wholesale market is dependent on sales to other telecommunications services providers, including wireless carriers. The demand for special access service should increase as wireless carriers roll out 5G service. However, HTI may have a [redacted] because its [redacted] is generally [redacted] and [redacted] may require carriers to [redacted].[34]

The Consumer Advocate also evaluated pro forma income taxes. In the future, HTI's federal taxes will be filed jointly with CB. The future federal tax liabilities of the combined entity can be reduced by applying HTI net operating losses. As of December 31, 2016, HTI's available net operating losses were $166 million. These losses will be available through 2036.[35] CB plans to use these net operating losses to offset its tax liability. For [redacted], an estimated [redacted].[36] Because HTI's [redacted] has not been

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33 The source data for the maps are the FCC 477 reports.

34 Confidential Restricted Exhibit CA-IR-42(a), page 314 and 315 of 778.

35 Exhibit I, Hawaiian Telecom Holdco, Inc., Form 10-Q for the quarterly period ended June30, 2017, page 28.

36 Confidential Restricted Exhibit CA-IR-42(a), page 228 of 778.

provided, it is not clear whether the net operating losses will offset [redacted].[37]

The Consumer Advocate also evaluated possible economies of scale, which refers to the reduction in cost associated with functioning at larger scale of activity. Synergies refer to the cost reductions which occurs because the costs of the merged company are less than the costs of the two companies operating separately. Obviously, the synergies can be caused by economies of scale that occur when the merger leads to a larger scale of activity. "Due to distance and separate operations, this merger is not expected to materially impact jobs in Hawai'i."[38] That is, jobs associated with network build-out and maintenance and customer-facing jobs will remain in Hawaii. Therefore, for those major cost categories, there will not be any cost savings associated with the merger. However, "post-combination management for parent company Cincinnati Bell will generally include all corporate responsibilities such as investor relations, treasury, capital markets, payroll, general counsel and corporate governance. Other duties such as financial and operational governance will also occur at the parent level."[39] Thus, all of the cost savings will be associated with these management activities. One estimate of these savings suggests that [redacted]

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37 Since HTI, HTSC, and Wavecom operate in a fully competitive retail market as well as the realization that HTI and its affiliates cannot, and have not, relied on cost of service regulation and general rate increases to improve its financial condition, the Consumer Advocate believes that the issues related to the recent passage of Tax Cuts and Jobs Act that are being examined in Docket No. 2018-0012 are not applicable to HTI and its affiliates. Thus, the Consumer Advocate does not address those issues here or in the public interest discussion.

38 Exhibit CA-IR-9(e), page 2 of 5.

39 Joint Applicants' Response to CA-IR-7.

[redacted].[40] Another estimate of the savings includes the [redacted].[41]

Thus, the Consumer Advocate offers that while conclusions can be reached about the combined operations of CB and HTI based on Exhibit K, only general conclusions about HTI and how the proposed transaction might provide quantifiable benefits to HTI and, ultimately to HTI's customers, can be supported by the evidence in the record. The Consumer Advocate also takes note of Commission required conditions resulting from prior proceedings that were placed upon HTI in order to address concerns about HTI's financial fitness or ability. For instance, in Decision and Order No. 21696, the Commission placed restrictions on the total amount of debt that the HTI could reflect in its capital structure to no more than 65% and also limited HTI's ability to issue dividends.[42]

In the application, the Joint Applicants discuss the current telecommunications industry and the market and discuss the debt limiting restriction and how it may no longer be appropriate. Given some of the remaining questions related to financial fitness and ability coupled with the fact that HTI remains the carrier of last resort whose infrastructure still remains an important backbone of Hawaii's telecommunications and data services, the Consumer Advocate believes that it is still important to ensure that HTI remains financially viable. Thus, as it relates to the Commission's finding of financial fitness, the

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40 Confidential Restricted Exhibit CA-IR-42(a), page 162 of 778.

41 Confidential Restricted Exhibit CA-IR-42(a), page 385 of 778.

42 On page 57, of Decision and Order 21696, the Commission states that, "Unless prior Commission approval is obtained, any dividend proceeds of Hawaiian Telcom shall be earmarked specifically and used only for debt repayment and that HT Communications shall not make any dividend repayments, until a target consolidated capital structure of sixty-five percent (65%) debt and thirty-five percent (35%) equity is achieved."

Consumer Advocate contends that it would be reasonable to: 1) review existing conditions to determine which of those conditions should be eliminated, modified, and/or retained; and 2) establish certain conditions to provide the Commission and Consumer Advocate sufficient information to take regulatory action, if needed, in the future. First, the Consumer Advocate believes that, for the reasons articulated in Decision and Order No. 32193, filed on July 7, 2014, in Docket No. 2014-0033, it would be appropriate to allow the existing waivers and flexibility granted by the Commission as it relates to HRS sections 269-17 and -19 as well as HAR sections 6-61-101 and -105. The flexibility granted by the Commission in Decision and Order No. 32193 is still important to allow Joint Applicants to take advantage of market conditions to obtain reasonable financing terms. In addition, the Consumer Advocate believes that the prior condition from Decision and Order No. 21696 relating to the capital structure should be modified. Rather than maintaining a "hard cap" of no more than 65% debt, as discussed and requested by Joint Applicants, modifying that condition appears reasonable. The Consumer Advocate believes that adopting a requirement that examines the debt to earnings before income taxes, depreciation, and amortization ("EBITDA") is appropriate, but it is also important to be aware of the overall and net debt that the Joint Applicants are holding to evaluate the potential effects of over-reliance on debt might have on HTI's financial viability. Joint Applicants assert that lenders are willing to extend credit up to a ratio of 5.0 or 5x EBITDA and recommends that a cap of 5x EBITDA be adopted. The Consumer Advocate does not believe adopting the threshold under which lenders are willing to make capital available as the cap is prudent; if the upper threshold is set as the benchmark or parameter, by the time the ratio hits that mark, the financial options for HTI will be limited. Instead, the Consumer Advocate recommends that the Commission should require that if the debt to EBITDA ratio exceeds 3.5x <u>or</u> the debt/equity ratio exceeds 65/35 (i.e., its overall debt exceeds 65% of total capitalization), the Joint Applicants should be required to provide, on a semi-annual basis, its plan (and, where applicable, the results of previously identified actions in the Joint Applicants' plan) to ensure that HTI's financial health and ability to cover existing debt obligations are adequate. If, however, the debt to EBITDA ratio exceeds 4.5x, the Joint Applicants should be required to file quarterly detailed reports on how it will reduce its debt to EBITDA ratio and other financial concerns that may exist. The Consumer Advocate also recommends that restricting HTI's ability to grant dividends should be modified to allow HTI the flexibility to grant dividends assuming that the debt to EBITDA does not exceed 4.0x. If that ratio is exceeded, Joint Applicants should be required to provide a discussion and detailed justification for the need to issue dividends in the semi-annual reports that should be filed but the ability to issue dividends would not be restricted unless otherwise ordered by the Commission.

2. Willingness.

By the application, the Consumer Advocate believes that it is reasonable to conclude that both HTI and CB are willing to offer, or continue to offer, affordable, reliable, and quality telecommunications services in the state of Hawaii.

3. Ability.

In the evaluation of ability of any applicant seeking to offer regulated utility services in Hawaii, the Consumer Advocate generally evaluates the applicant's managerial, financial and technical ability to provide the proposed service or services. The Consumer Advocate believes that, based on the HTI's history as well as available information on CB's and its management, the Commission should find that the requisite managerial ability exists. As for financial ability, the discussion above offers the Consumer Advocate's assessment and recommendation.

The Consumer Advocate believes that there are various factors that can and should be reviewed as it relates to technical ability. First, given the assertions and understanding that the current equipment and infrastructure will continue to be used as well as the current employees will continue to be retained, the Consumer Advocate believes that these are factors that generally support a finding that the technical ability will continue to be present.

As noted earlier, however, the Consumer Advocate believes another measurement of technical ability, especially where historical information exists, should consider the service quality, reliability, and/or resiliency. All of these general metrics are important to note as it relates to any regulated service and even more so for telecommunications services where quality services must be available for Hawaii's economy and those services must be resilient to facilitate Hawaii's ability to withstand catastrophic events or be available during times of urgent need. With regard to system reliability and resilience, the Commission currently requires HTI to file a monthly service quality report. In that report, HTI records its performance on 17 measures of service quality. There are objective metrics for 12 of the 17 measures. HTI meets or exceeds the metrics for some of the measures and fails to meet the objectives for other measures.[43] As part of its review, the Consumer Advocate also sought to review what metrics CB uses, such as in CA-IR-31, where the Consumer Advocate sought to determine whether, as part of developing best practices, there might be an opportunity to adopt other metrics that should be used to evaluate HTI's performance. After its review of the existing service metrics, benchmarks, and other relevant factors, the Consumer Advocate contends that these should be re-examined.

First, the Consumer Advocate believes that some of the existing standards should be eliminated from the report. There are certain service metrics that are no longer relevant as the evolution of technology has made them obsolescent. The Consumer Advocate also believes that Joint Applicants should provide a definite plan to improve its service quality metrics as there are a number of reported metrics that does not reflect acceptable results. The Consumer Advocate contends that HTI, and CB if the transaction is approved, should strive to improve on these metrics since if customers are dissatisfied, there are alternatives to the any of the services that they seek to offer in Hawaii. By improving the quality and affordability of its services, HTI will be in a better position to attract and retain customers. The Consumer Advocate also recommends that HTI should propose for inclusion in this report applicable metrics to better evaluate the

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43 As part of its review, the Consumer Advocate sought to determine what existing plans that HTI might have to improve its service quality. In response to CA-IR-32a., which requested the identification of each measure that has been implemented and the efficacy of the measure, Joint Applicants referred to the quarterly status report, which does not adequately address the identification and efficacy of measures implemented.

system resilience in order to properly assess whether HTI's infrastructure will be able to help Hawaii, especially in times of critical need.

Thus, to ensure that the Joint Applicants maintain and enhance system reliability and resilience, the Consumer Advocate recommends that Joint Applicants should file a detailed plan on how it will improve key service reliability metrics such as [redacted] and appropriate benchmarks should be established for other metrics, such as [redacted]. This plan should represent a realizable and reasonable action plan that will improve the customer service as well as allow the Commission and Consumer Advocate to evaluate Joint Applicants' efforts to ensure that customer service is improved. This plan should also provide sufficient detail so that the Commission and Consumer Advocate can evaluate HTI's efforts to ensure that services on the neighbor islands or in rural areas compare favorably to the services provided on Oahu. The Consumer Advocate does not recommend placing a date certain by which these improvements in service quality metrics should be achieved as the Consumer Advocate believes that the Joint Applicants should be allowed some flexibility in developing a reasonable plan, in conjunction with existing CAPEX plans to roll out additional infrastructure to improve its infrastructure to remain competitive. An overly prescriptive service quality improvement plan may be counter-productive to the overall financial health of HTI. Thus, the Consumer Advocate recommends that the Commission require Joint Applicants to file a service quality improvement plan, that also includes suggested revisions to the service measurement report to update as well as to include service resilient metrics and standards within nine months of the close of the transaction.

If, however, Joint Applicants do not demonstrate adequate compliance with the plan or do not provide a reasonable plan, the Consumer Advocate recommends that the Commission require the creation of an escrow account that Joint Applicants will be required to put sufficient funds to realize completion of the service quality improvement plans. Funds for this escrow account could come from [redacted]

This type of regulatory conditions is not unprecedented.[44]

II. PUBLIC INTEREST CONSIDERATIONS

As discussed earlier, another key factor in evaluation whether a proposed merger or acquisition is reasonable is an assessment of whether the transaction is in the public interest and the Commission's Appendix A has made clear certain factors that should be addressed when evaluating whether a proposed merger/acquisition is in the public interest. The Commission has identified six key areas and the Consumer Advocate will discuss benefits to ratepayers, the impact on competition, the mitigation of risks, corporate governance, and the transformation of the company.

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44 See, e.g., The California Public Utilities Commission Decision Granting Application Subject to Conditions and Approval of Related Settlements, filed on December 3, 2015, in Application 15-03-005.

1. Customer Benefits.

The Commission states that "the application should provide benefits to customers in the short- and long-term that are substantial and certain enough to be meaningful.[45] The Joint Applicants claim that they meet this condition "by providing them [customers] with greater product service offerings, greater competition for broadband Internet access, voice and video service, and enhanced system reliability and resilience with expanded fiber deployment throughout the state."[46] Cincinnati Bell claims that it is committed to building the HTI's next-gen fiber network statewide.[47]

To evaluate these claims, it is first necessary to examine the current statewide fiber network and then compare that network to the Joint Applicants' commitments to improve the network. Attachment 1 reports that HTI provides service at a maximum rate of 1000 Mbps to 224,705 households. These are the households served by the FTTP next-gen network, leaving 257,469 households off that network. Attachment 4 reports the same data on a county basis. The FTTP network serves 66.5% of households in Honolulu County and it serves only 4.8 to 7.8 of households in the other counties. Attachment 9 to 12 depict the fiber network on a county basis.[48]

The Joint Applicants have committed to the Cable Television Division ("CATV") that they will invest $20 million in the fiber network and expand the network to serve an

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45 Order No. 33795, Docket No. 2015-0022, Appendix A, at 2 – 17.

46 Joint Application, page 36.

47 Id., page 2.

48 See website: https://broadbandmap.fcc.gov.

additional 15,000 households over 4 years.[49] These commitments are in addition to HTI's Connect America Fund Phase II ("CAF II") commitment to expand the network to serve approximately an additional 11,000 households. Adding 15,000 households over 4 years is the equivalent of adding 3,750 per year. Given that HTI has 257,469 non-fiber households, adding households at that rate means HTI will take 69 years to complete its fiber buildout. The Consumer Advocate believes that rate of buildout raises questions about reasonable expectations of HTI's commitment to provide Hawaii's consumer with state of the art telecommunications services. The Consumer Advocate notes, however, the response to CA-IR-26 states that the 15,000 additional homes, "[a]s stated, . . . is most likely a floor." The Consumer Advocate encourages Joint Applicants to aggressively seek cost-effective CAPEX that can help improve HTI's ability to provide ubiquitous affordable state-of-the-art telecommunications services in Hawaii.

Putting aside those questions about how long the build out might take for now, however, as mentioned earlier, due to only [redacted] pro forma results being provided, the Consumer Advocate believes that a commitment to improve service quality would be observable benefit to existing customers and Hawaii that would be supportive of finding that there are significant net benefits. Thus, as mentioned earlier, the Commission should adopt the Consumer Advocate's recommended service quality and resiliency actions so that Hawaii might realize those benefits.

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49 In the Matter of the Joint Application of Cincinnati Bell Inc., Hawaiian Telcom Holdco, Inc, and Hawaiian Telecom Services Company, Inc. for Approval of the Transfer of Control of Hawaiian Telcom Service Company, Inc.'s Cable Television Franchise for the Island of O'ahu from Hawaiian Telcom Holdco, Inc. to Cincinnati Bell Inc., and related matters, Cable Television Division, Decision and Order No. 370, dated December 8, 2017, page 15.

The Consumer Advocate also recognizes that a commitment to increase the CAPEX in Hawaii $20 million more than what would have been made is supportive of finding significant net benefits due to the proposed transaction. However, as discussed earlier, since only [redacted] financial information was provided, the Consumer Advocate was unable to clearly establish what the benchmark to use to confirm that the proposed transaction will result in an additional $20 million being invested. The Consumer Advocate is concerned that, without sufficient means to note the benchmark and to evaluate the additional CAPEX, the Commission might rely on an assertion that $20 million **more** will be spent but there will be no way to verify that additional monies were spent. Thus, the Consumer Advocate recommends that the Commission require the Joint Applicants to file within three months of closing relevant documents and metrics that will allow the Commission to confirm that, four years after closing, the Joint Applicants have invested $20 million more in Hawaii. The Consumer Advocate also recommends that the documents make clear where the money has been spent to ensure that the neighbor islands receive some benefit of this additional investment. Available data, such as graphically depicted in the county maps show a clear disparity in the availability of fiber infrastructure on the neighbor islands and efforts should be made to ensure that the entire state, not just Honolulu county has the benefit of improved telecommunications infrastructure.

2. Competition.

The Commission's principle states: "Applicants must demonstrate that their proposal will promote robust competition in Hawaii's energy markets."[50] In this proceeding, the principle related to competition certainly applies to telecommunications markets. On a retail basis, HTI already faces competition from various services, such as those offered by Charter cable as well as other sources, such as mobile telephone services. In addition, the Consumer Advocate recognizes that the Hawaii legislature has recognized that retail telecommunications services are fully competitive.[51]

To enhance HTI's competitive position for retail services, it is necessary to buildout the fiber next-gen network. As noted above, it appears that the Joint Applicants are committed to moving slowly to expand that network. It would be helpful if the Joint Applicants would enhance their current commitment to expand the next-gen network.

On a wholesale level, HTI provides the fiber that will connect the facilities of the wireless carriers and allow those carriers to compete. The Consumer Advocate is not aware of any recent concerns that HTI's actions are stifling competition. As noted above, the HTI fiber deployment may not be capable of providing fiber services required by 5G wireless networks. The Division recommends that the Joint Applicants review their current plans and report to the Commission regarding their ability to meet the demands of 5G wireless carriers for fiber service.

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50 Order No. 33795, Docket No. 2015-0022, Appendix A, page 13 of 17.

51 See HRS § 269-16.85.

3. Risk Mitigation

The Commission's principle states: "Proposed ring fencing measures should protect the HECO Companies' customers from the impact of possible bankruptcy or other major problems that may occur in the future with respect to other members of an applicant's corporate family."[52] The Joint Applicants want the Commission to waive this requirement. They wish to permanently retire the existing Holdco debt and they wish to secure the debt of the parent company with the assets of Hawaiian subsidiary.[53] The Joint Applicants believe that ring fencing is inappropriate in the telecommunications market. They assert that integrating the finances of all of the companies will result in more capital investment.

Based on its assessment, the Consumer Advocate is not aware of any current or reasonably expected factors or events associated with CB or existing CB affiliates that would increase risk to HTI or Hawaii. With the understanding that much of CB's (and assuming that HTI's focus will be the same if the transaction is approved) focus is investing in additional fiber infrastructure as opposed to riskier investments,[54] such as non-core function acquisitions, the proposed transaction should not result in increased risk for HTI or risk exposure for Hawaii consumers. Thus, the Consumer Advocate does not believe that ring fencing measures are necessary at this time. If however, future events or factors arise, the Consumer Advocate urges Joint Applicants to provide timely

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52 Order No. 33795, Docket No. 2015-0022, Appendix A, page 4 of 17.

53 Joint Application, page 10 and 12.

54 Response to CA-IR-22.

information to the Commission and Consumer Advocate to evaluate the potential exposure that HTI and Hawaii might have.

4. Corporate Governance.

The Commission's principle states: "Applicants should provide documentation of the proposed corporate structure and clearly demonstrate how the proposed structure will ensure a meaningful, representative role for local governance and Hawaii stakeholders."[55] Based on the record, it appears that, while day-to-day management decisions will be delegated to Hawaii managers, all major governance decisions will be made at the parent company level. Without adequate representation, it would be difficult for Hawaiian stakeholders to participate in future governance decisions. With the understanding that two director seats on the board will be filled by Hawaii **residents**,[56]

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55 Order No. 33795, Docket No. 2015-0022, Appendix A, page 14 of 17.

56 Joint Applicants' commitment to have two director seats filled with Hawaii residents is offered in various places, such as on page 9 of the application. It is important to ensure that these seats are filled by Hawaii residents with longtime ties to Hawaii as opposed to filling the seats with individuals with Hawaii ties, people who might have recently moved to Hawaii, or people with residences in Hawaii (but don't really live in Hawaii).

5. Company Transformation.

The Commission's principle states: "Applicants should provide specific commitments that reflect the critical importance of transforming the HECO into a customer focused, cost efficient, and performance driven electric utility."[57] With respect to this proceeding, the Consumer Advocate notes that this principle could be generally applied where it directs the Joint Applicants to become a customer focused, cost efficient and performance driven telecommunications utility. Given the existing circumstances, the Consumer Advocate believes that market forces provide pressures to be cost efficient and performance driven. The Consumer Advocate notes that Joint Applicants contend that, due to certain factors, the ability to reduce costs as a result of the proposed transaction may be somewhat limited, but that opportunities still exist for improvement. Thus, the Joint Applicants will try to generate scale economies and synergies and adopt best of market strategies to cost effectively provide services. As noted earlier, however, the Consumer Advocate contends that the Joint Applicants must become more customer focused in order grow in their current market environment. The Consumer Advocate is aware of anecdotes of customers who are seeking other options due to frustrations with HTI. Thus, the Consumer Advocate believes that the earlier recommendations related to improving service quality and resiliency will help to re-focus on customer satisfaction.

III. RECOMMENDATION.

Based upon the above, the Consumer Advocate hereby states that, assuming that the Commission adopts the above recommended conditions, it supports the proposed

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[57] Order No. 33795, Docket No. 2015-0022, Appendix A, page 15 of 17.

transaction and that the Commission should find that Joint Applicants are fit, willing, and able to provide, or continue providing, telecommunications services in Hawaii and that the proposed transaction, with the adopted conditions will support a finding of public interest.

DATED: Honolulu, Hawaii, March 7, 2018.

Respectfully submitted,

By Dean Nish
DEAN NISHINA
Executive Director

DIVISION OF CONSUMER ADVOCACY

Table 1: Hawaiian Telcom State-Wide Broadband Availability By Maximum Advertised Download Speed			
Max Advertised Download Speed	**Number of Census Blocks**	**Number of Housing Units**	**Percentage of Housing Units**
0	0	0	0.0%
greater than 0 and less than 4	25	92	0.0%
4 or greater and less than 10	3,021	66,652	13.8%
10 mbps	29	136	0.0%
greater than 10 and less than 25	2,528	149,740	31.1%
25 mbps	640	40,849	8.5%
greater than 25 and less than 50	0	0	0.0%
equal to or greater than 50	3,006	224,705	46.6%
Totals	**9,249**	**482,174**	**100.0%**

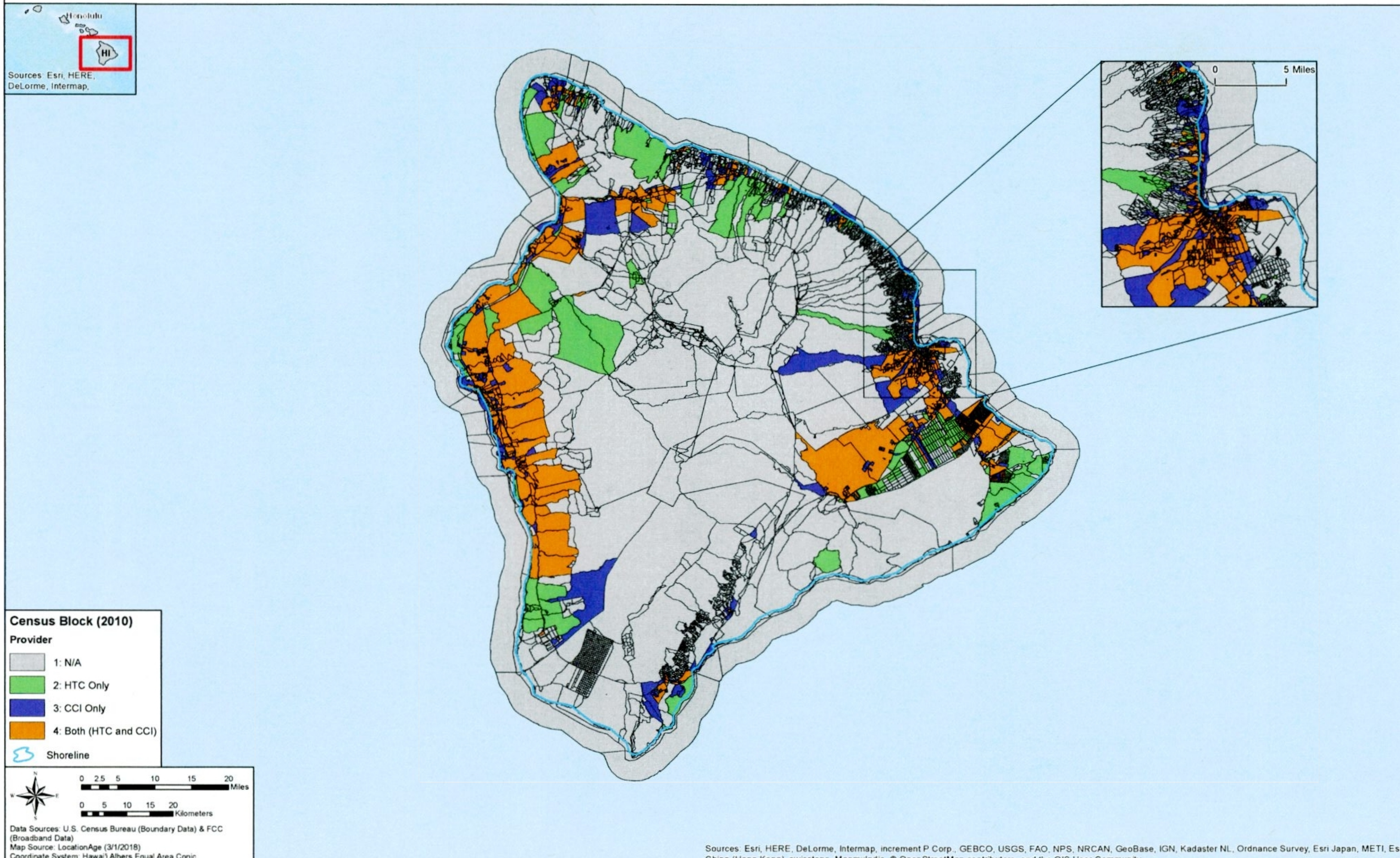
Table 2: Comparison of Hawaiian Telcom and Charter Comm Maximum Advertised Download Speeds In Census Blocks where Hawaiian Telcom and Charter Comm Provide Service								
	Hawaiian Telcom					Charter Comm		
Max Advertised Download Speed	Number of Census Blocks	Number of Housing Units	Percent of Housing Units	Population Count	Percent of Pop. Served by Company	Number of Census Blocks with 50 mbps or Greater Service	Number of Housing Units with 50 mbps or Greater Service	Population with 50 mbps or Greater Service
0	0	0	0.0%	0	0.0%	0	0	0
greater than 0 and less than 4	16	60	0.0%	178	0.0%	16	60	178
4 or greater and less than 10	2,390	56,931	12.1%	152,189	12.4%	2,390	56,931	152,189
10 mbps	0	0	0.0%	0	0.0%	0	0	0
greater than 10 and less than 25	2,452	148,312	31.5%	348,454	28.3%	2,452	148,312	348,454
25 mbps	636	40,793	8.7%	121,606	9.9%	636	40,793	121,606
greater than 25 and less than 50	0	0	0.0%	0	0.0%	0	0	0
equal to or greater than 50	2,957	224,085	47.7%	609,670	49.5%	2,957	224,085	609,670
Totals	**8,451**	**470,181**	**100.0%**	**1,232,097**	**100.0%**	**8,451**	**470,181**	**1,232,097**

Table 3: Hawaiian Telcom Broadband Availability by Maximum Advertised Download Speed				
In Census Blocks where Charter Comm Does Not Provide Service				
Max Advertised Download Speed	**Number of Census Blocks**	**Number of Housing Units**	**Percent of Housing Units**	**Population**
0	0	0	0.00%	0
greater than 0 and less than 4	9	32	0.27%	77
4 or greater and less than 10	631	9721	81.06%	20134
10 mbps	29	136	1.13%	316
greater than 10 and less than 25	76	1428	11.91%	2585
25 mbps	4	56	0.47%	250
greater than 25 and less than 50	0	0	0.00%	0
equal to or greater than 50	49	620	5.17%	1902
Totals	**798**	**11,993**	100.00%	**25,264**

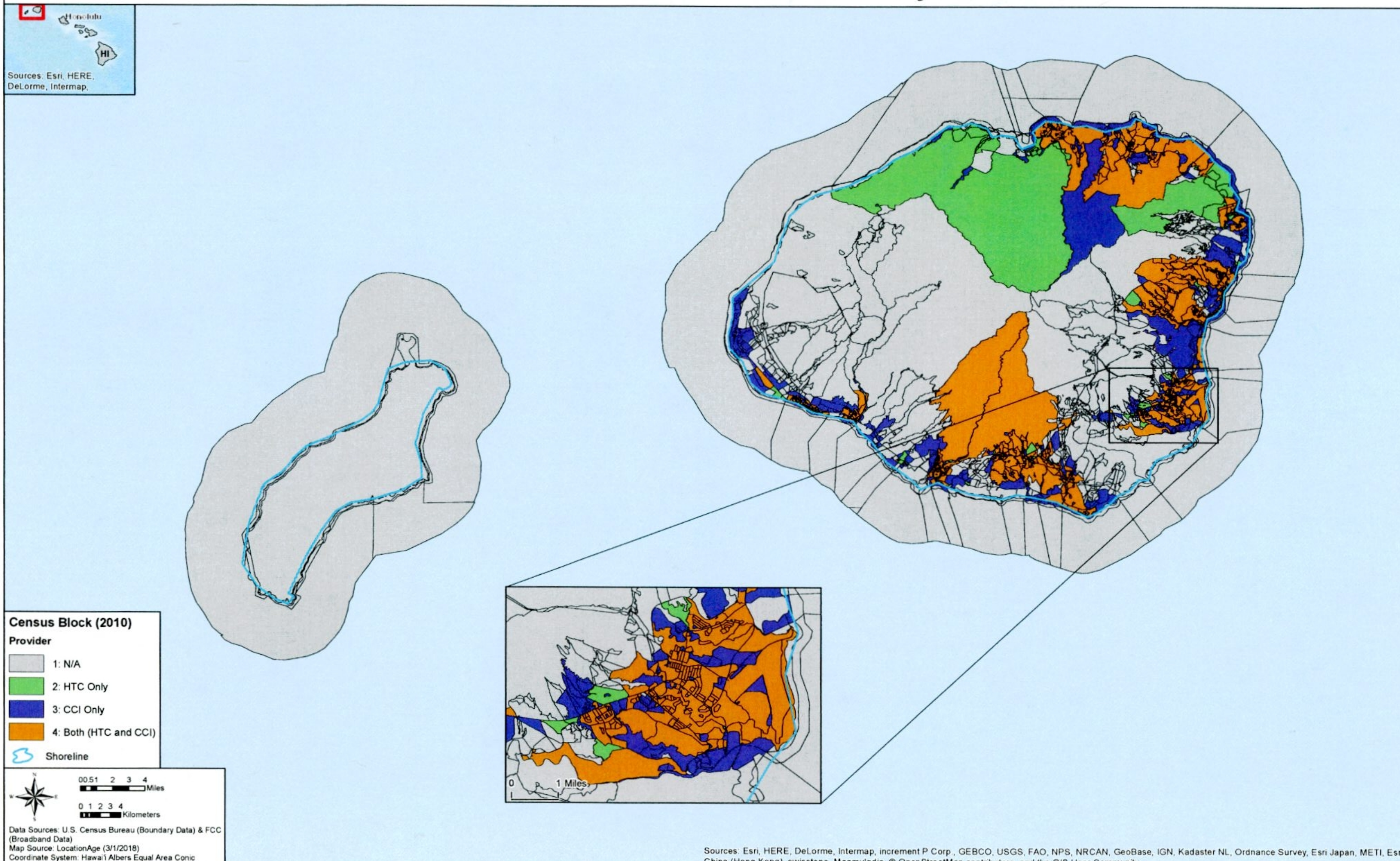
Table 4: County Download Speeds and Housing Counts

	CntyCode	15001	15003	15007	15009	
	County	Hawaii	Honolulu	Kauai	Maui	Totals
	Block Count Totals	2,130	5,014	910	1,195	9,249
Max Advertised Download Speed	Housing Unit Count Totals	67,154	322,810	27,905	64,305	482,174
0	Block Count	0	0	0	0	-
	Housing Unit Count	0	0	0	0	-
greater than 0 and less than 4	Block Count	8	13	1	3	25
	Housing Unit Count	28	45	0	19	92
4 or greater and less than 10	Block Count	1,364	704	480	473	3,021
	Housing Unit Count	29,717	14,769	8,602	13,564	66,652
10 mbps	Block Count	29		0	0	29
	Housing Unit Count	136	0	0	0	136
greater than 10 and less than 25	Block Count	638	808	406	676	2,528
	Housing Unit Count	34,031	52,445	17,532	45,732	149,740
25 mbps	Block Count	0	640	0	0	640
	Housing Unit Count	0	40,849	0	0	40,849
greater than 25 and less than 50	Block Count	0	0	0	0	-
	Housing Unit Count	0	0	0	0	-
equal to or greater than 50	Block Count	91	2,849	23	43	3,006
	Housing Unit Count	3,242	214,702	1,771	4,990	224,705
	Percent of Housing Units with 50 mbps or Greater	4.8%	66.5%	6.3%	7.8%	46.6%

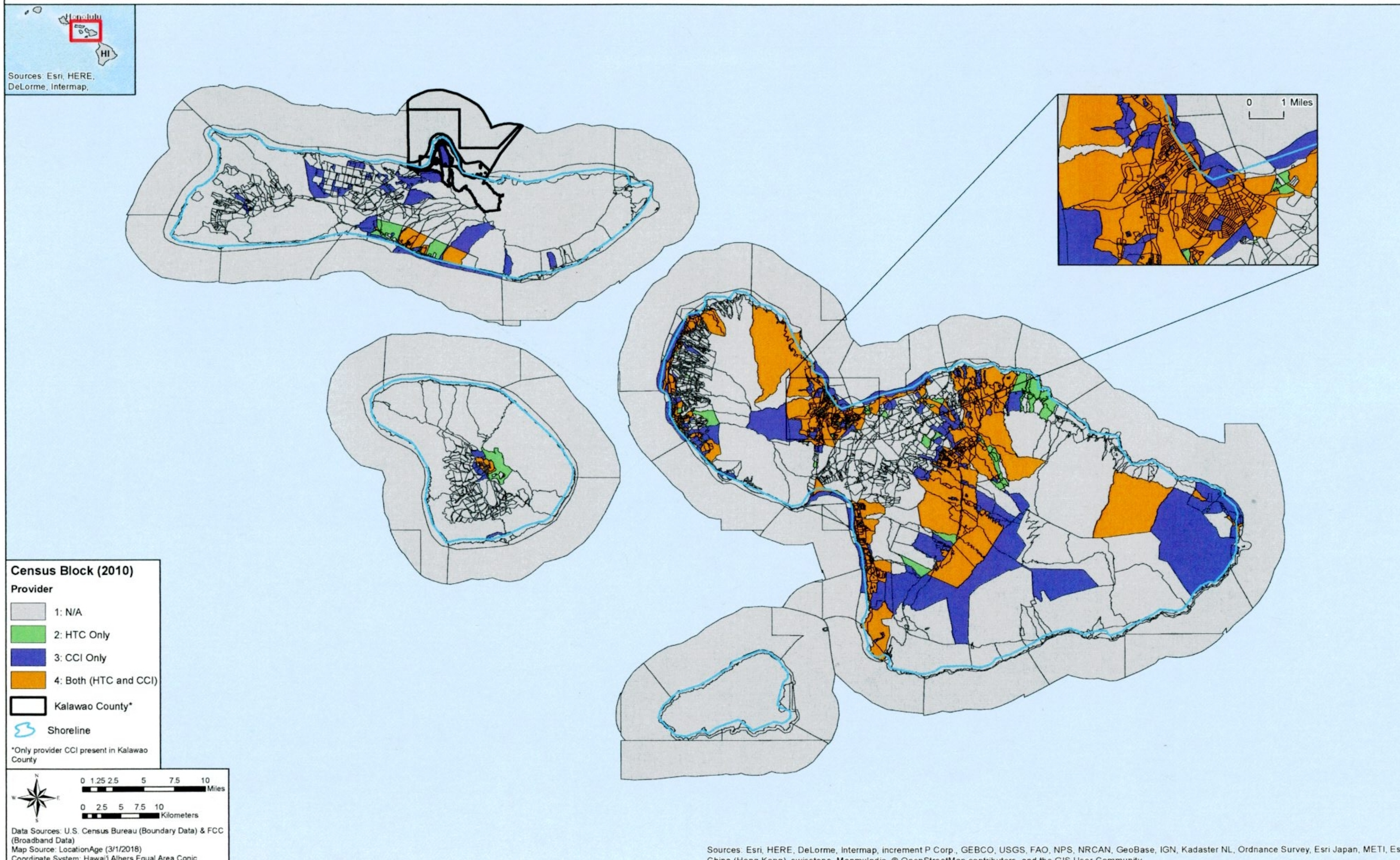
Hawai'i Fixed Broadband Providers - Hawai'i County HTC and CCI



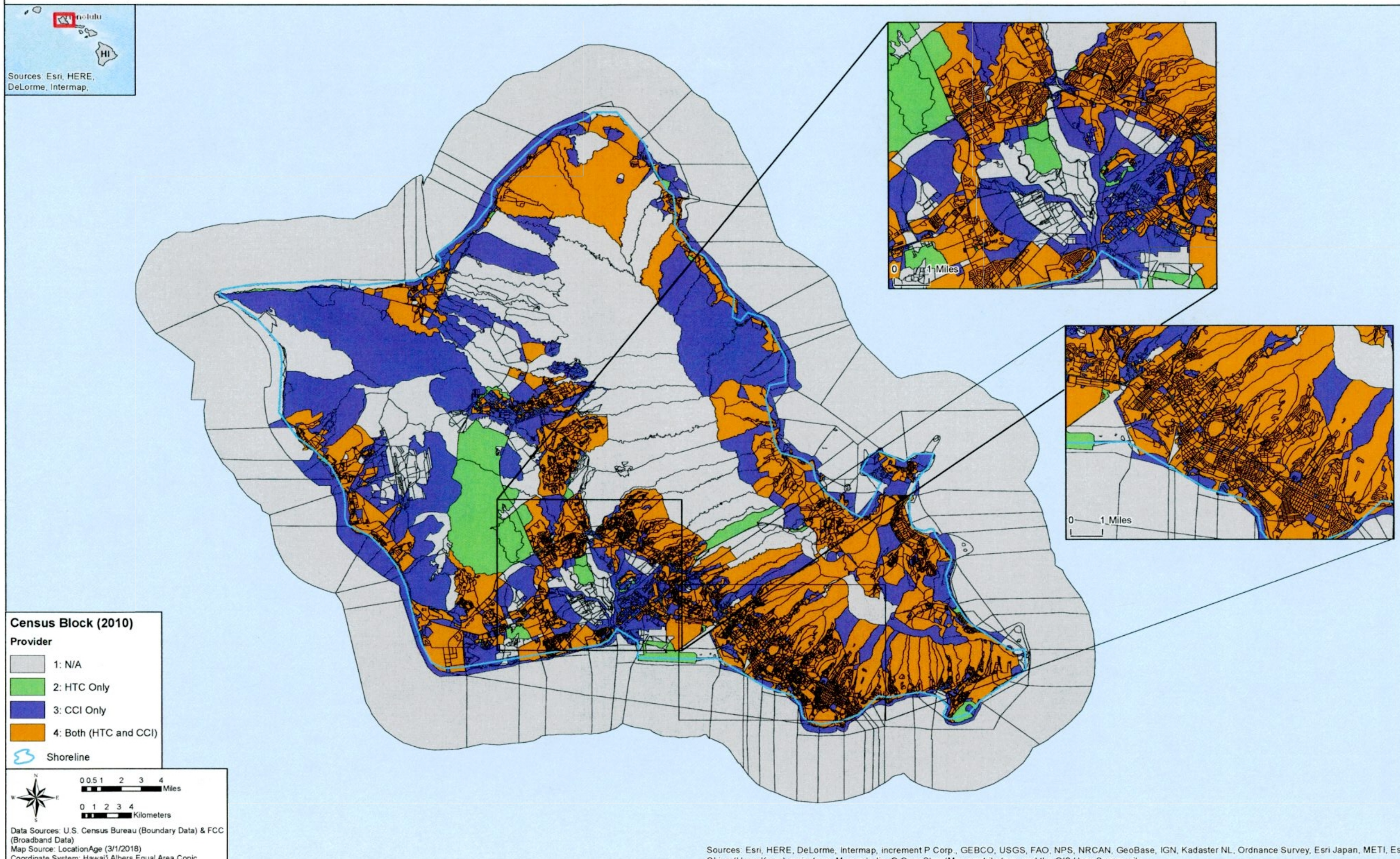
Hawai'i Fixed Broadband Providers - Kaua'i County HTC and CCI

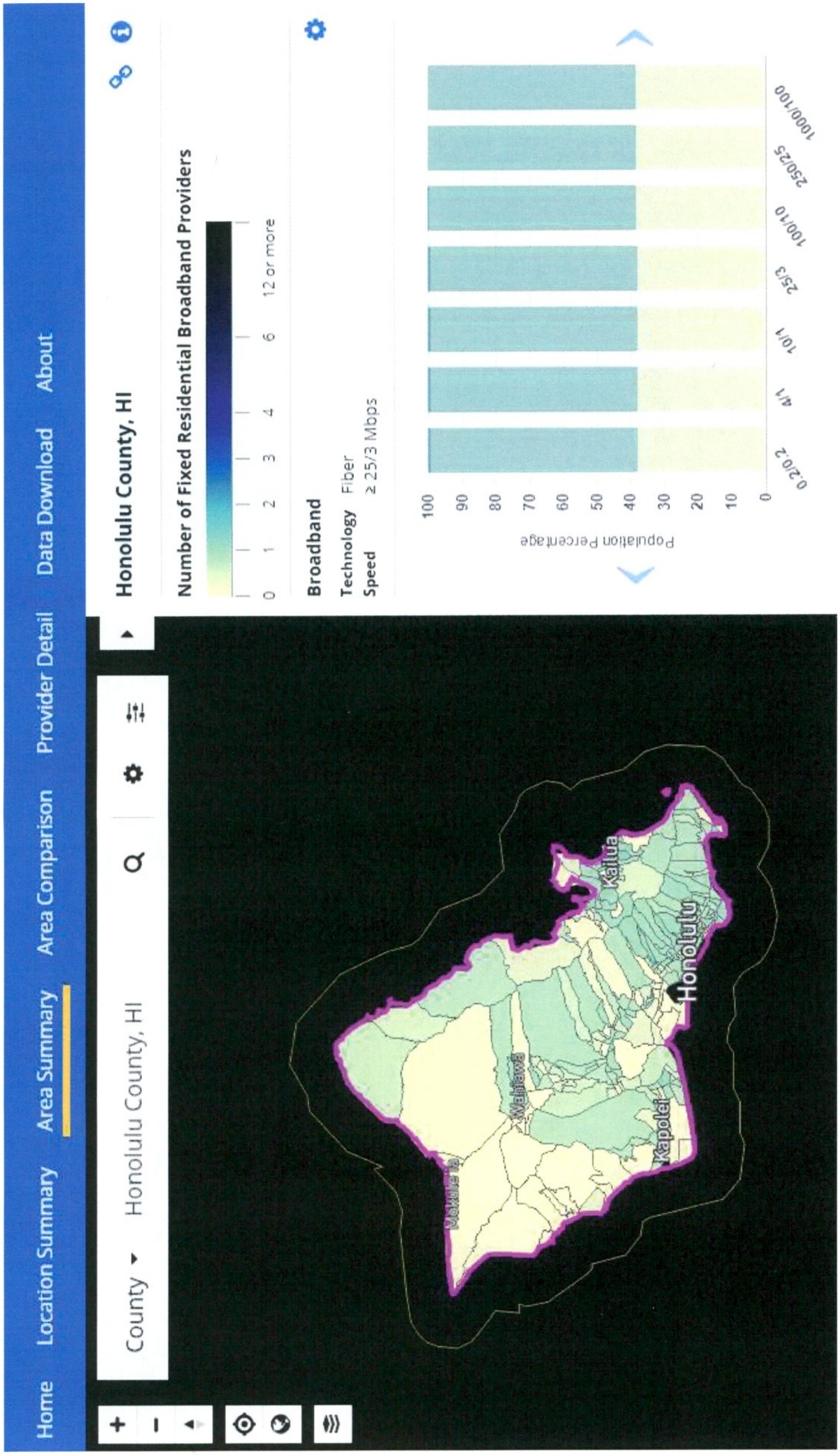


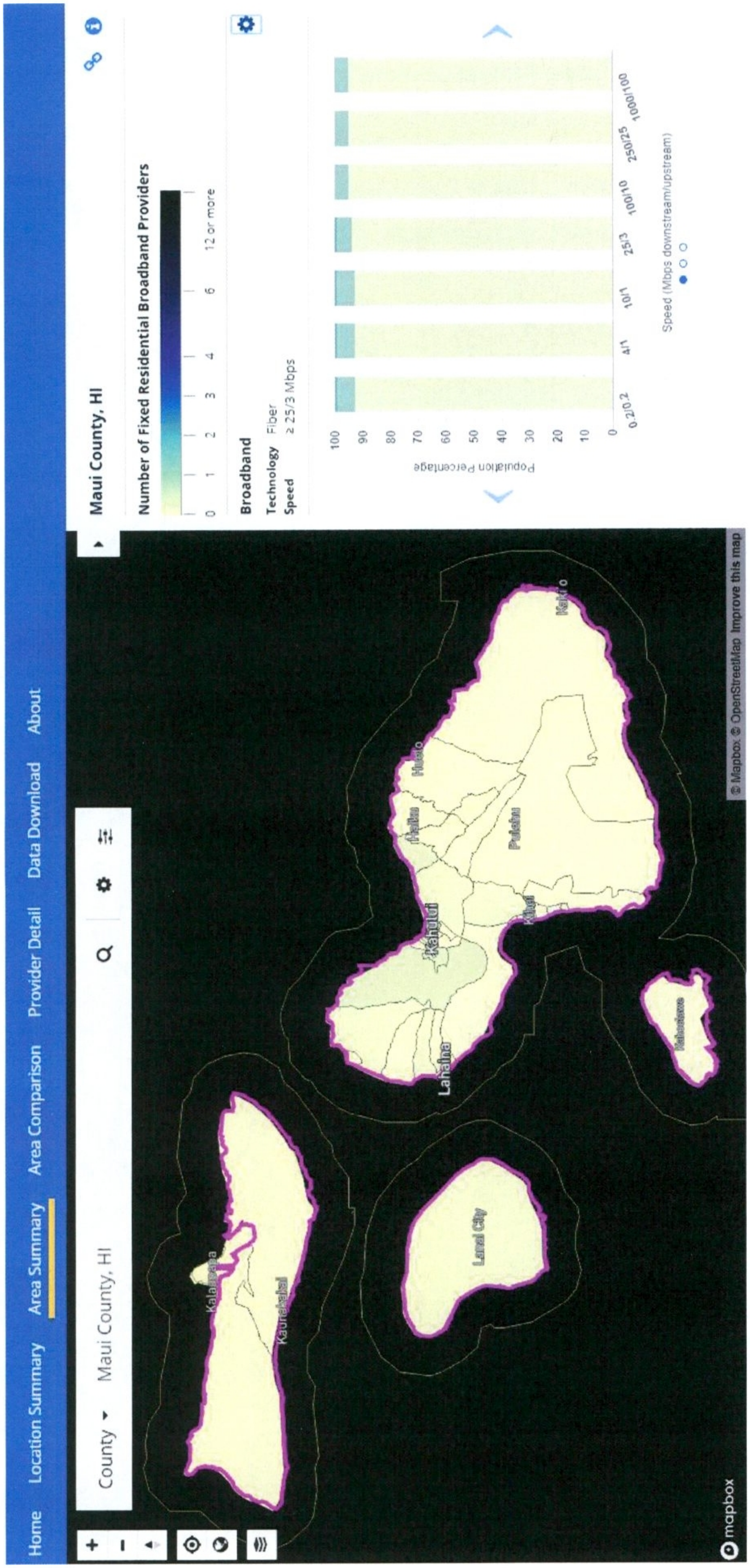
Hawai'i Fixed Broadband Providers - Maui and Kalawao Counties HTC and CCI



Hawai'i Fixed Broadband Providers - Oahu County HTC and CCI

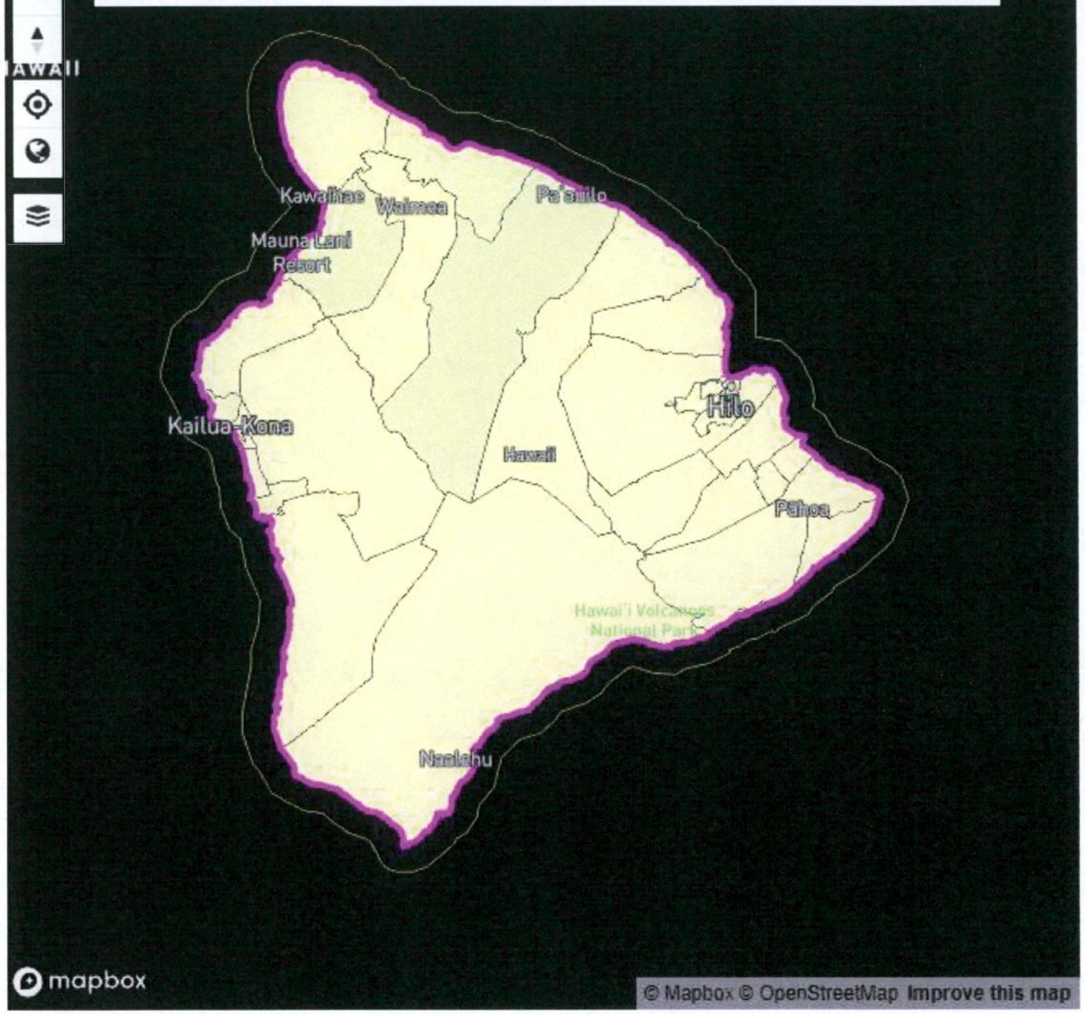



Home
Location Summary
Area Summary
Area Comparison
Provider Detail
Data Download
About
County
Honolulu County, HI
Honolulu County, HI
Number of Fixed Residential Broadband Providers
0
1
2
3
4
6
12 or more
Broadband
Technology Fiber
Speed ≥ 25/3 Mbps
Population Percentage
100
90
80
70
60
50
40
30
20
10
0
0.2/0.2
4/1
10/1
25/3
100/10
250/25
1000/100
Kailua
Honolulu
Wahiawā
Kapolei


Home
Location Summary
Area Summary
Area Comparison
Provider Detail
Data Download
About
County
Maui County, HI
Maui County, HI
Number of Fixed Residential Broadband Providers
0
1
2
3
4
6
12 or more
Broadband
Technology Fiber
Speed ≥ 25/3 Mbps
Population Percentage
100
90
80
70
60
50
40
30
20
10
0
0.2/0.2
4/1
10/1
25/3
100/10
250/25
1000/100
Speed (Mbps downstream/upstream)
Kalaupapa
Kaunakakai
Lanai City
Lahaina
Kahului
Kihei
Pukalani
mapbox
© Mapbox © OpenStreetMap Improve this map

Home | Location Summary | Area Summary | Area Comparison | Provider Detail | Data Download | About

County ▾ Hawaii County, HI



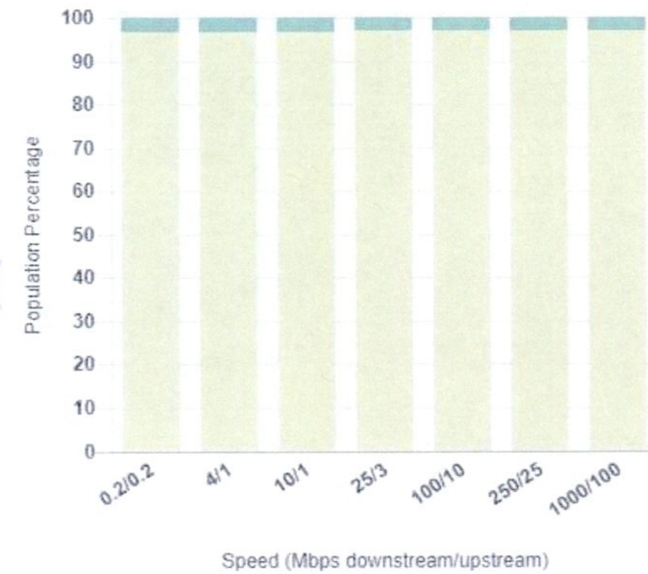
Hawaii County, HI

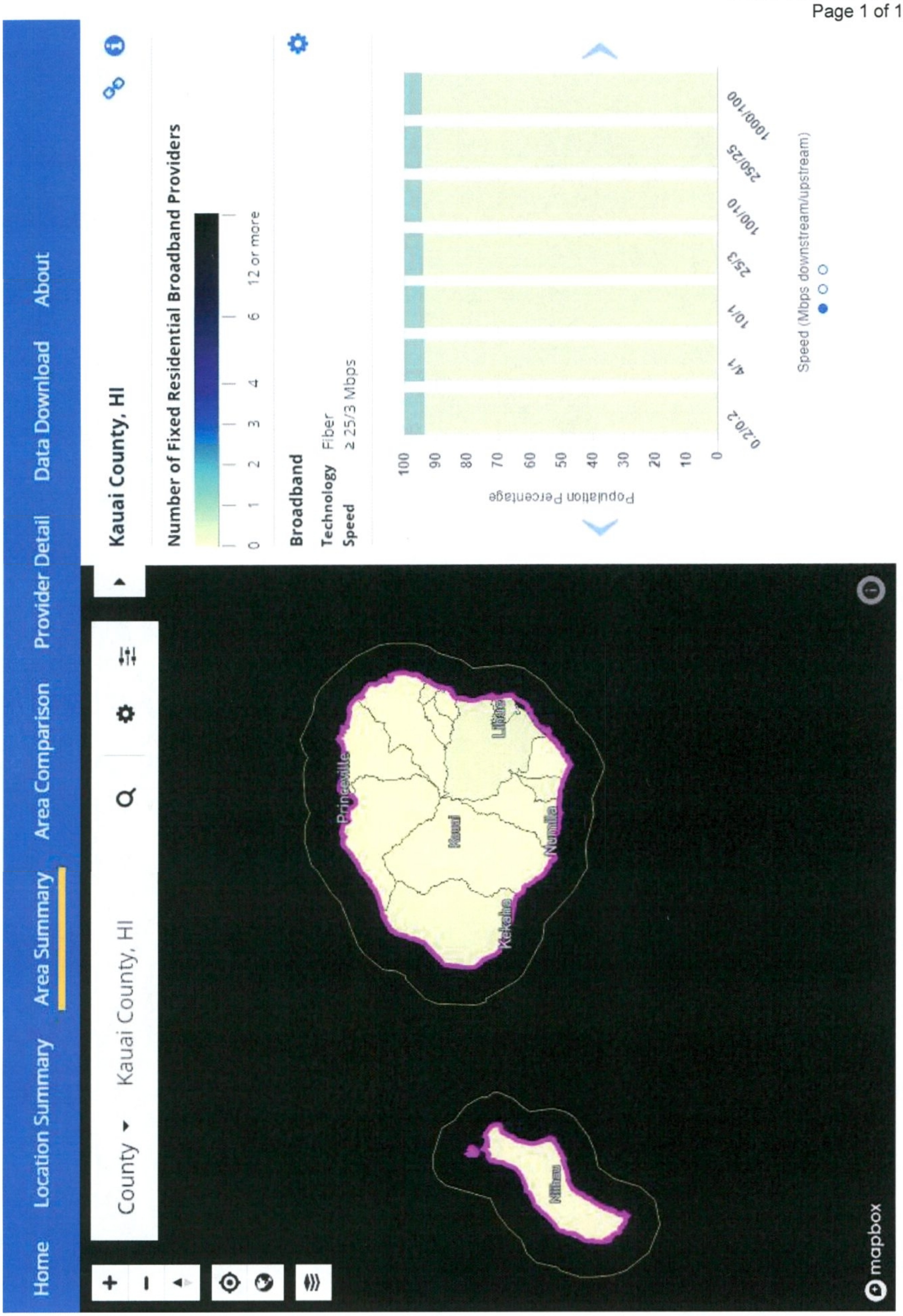
Number of Fixed Residential Broadband Providers

0 1 2 3 4 6 12 or more

Broadband

Technology Fiber
Speed ≥ 25/3 Mbps




Home
Location Summary
Area Summary
Area Comparison
Provider Detail
Data Download
About
County
Kauai County, HI
Princeville
Lihue
Kauai
Numila
Kekaha
Niihau
mapbox
Kauai County, HI
Number of Fixed Residential Broadband Providers
0
1
2
3
4
6
12 or more
Broadband
Technology Fiber
Speed ≥ 25/3 Mbps
Population Percentage
100
90
80
70
60
50
40
30
20
10
0
0.2/0.2
4/1
10/1
25/3
100/10
250/25
1000/100
Speed (Mbps downstream/upstream)

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing **DIVISION OF CONSUMER ADVOCACY'S STATEMENT OF POSITION** was duly served upon the following parties, by personal service, hand delivery, and/or U.S. mail, postage prepaid, and properly addressed pursuant to HAR § 6-61-21(d).

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DATED: Honolulu, Hawaii, March 7, 2018.

JMatsumoto