



### Scope of the Underlying Dispute

3           The underlying dispute concerns the indirect merger of CenturyTel's and Embarq's Washington regulated operating subsidiaries ("Merger"). In Washington, CenturyTel provides local telephone service through its subsidiaries CenturyTel of Washington, Inc., CenturyTel of Inter Island, Inc., and CenturyTel of Cowiche, Inc. (collectively "CenturyTel ILECs"). CenturyTel provides long distance service in Washington through its subsidiary CenturyTel Long Distance, LLC. CenturyTel has two other non-ILEC operating entities registered in Washington: CenturyTel Solutions, Inc., and CenturyTel Fiber Company II, d/b/a LightCore, a CenturyTel Company LLC. Embarq provides local and long distance service through its operating subsidiaries, United Telephone Company of the Northwest d/b/a Embarq ("United") and Embarq Communications, Inc.

4           During the course of the proceeding, CenturyTel and Embarq filed pleadings and testimony contending that the Washington Utilities and Transportation Commission ("Commission") should approve the Merger without conditions because it causes no harm to the public interest and in fact benefits customers, and therefore, approval of the Merger without conditions is consistent with the public interest. *See e.g.*, Application and Direct and Rebuttal Testimony of G. Clay Bailey, Barbara C. Young, and Mark A. Gast.

5           Staff and Public Counsel filed testimony arguing that the Merger is not consistent with the public interest and that conditions should accompany any approval of the Joint Application. The conditions included prohibitions on the ability to recover merger transaction or branding costs from ratepayers, service quality reporting and guarantees, continuation for United and extension to CenturyTel ILECs of certain conditions from the order approving the parties' settlement in WUTC Docket No. UT-051291 ("Separation Order"),<sup>1</sup> several conditions related to the continued financial health of the CenturyTel ILECs and United, affiliated interest transaction reporting, a requirement to file an earnings review, and broadband improvement obligations. *See, e.g.*, Testimony of Staff witnesses Betty Erdahl and William Weinman, and Public Counsel witness Trevor Roycroft.

6           As discussed below, the Parties have reached an agreement that resolves (or renders moot) all of the issues in this proceeding. The Agreement does not adopt all of the conditions proposed by the Staff and Public Counsel, but the Parties have agreed to a set of conditions in the spirit of compromise and to facilitate a prompt resolution of this proceeding consistent with the public interest. The Agreement represents a fair and reasonable resolution of all issues in this docket, and accordingly, the Parties seek Commission approval of the Agreement without material change.

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<sup>1</sup> *In the Matter of the Request of Sprint Nextel Corporation for an Order Declining to Assert Jurisdiction Over or, in the Alternative, Application for Approval of the Transfer of Control of United and Sprint Long Distance, Inc. from Sprint Nextel Corporation to LTD Holding Company*, WUTC Docket No. UT-051291, Order 06, Approving and Adopting Settlement Agreement (March 14, 2006).

## Overview of the Proposed Settlement Agreement

### A. Substance of the Agreement

7 Pursuant to the Agreement, the Commission would approve the indirect merger of CenturyTel's and Embarq's local operating companies as being in the public interest subject to conditions related to the following issue areas raised by Public Counsel and Staff: (1) continuation of conditions approved in the Separation Order, (2) financial fitness of the merged company, (3) service guarantee, (4) merger synergies, (5) recovery of merger, branding and transaction costs, (6) customer notice, (7) transfer of long distance customers, (8) broadband improvement, (9) affiliated interest transactions, (10) one-time Lifeline notification, (11) milestone reporting, and (12) future treatment of synergy benefits. Please refer to Section E of the Agreement for the specific terms.

### B. Procedure

8 The Parties understand that the Commission has discretion, consistent with applicable law, to establish the appropriate procedures for determining whether the Commission will approve the Agreement. The Commission has proposed, and the Parties have agreed, to conduct a hearing on the Agreement pursuant to WAC 480-07-740(1).

## Statement of Parties' Views

9           This Narrative, as required by WAC 480-07-740(2)(a), includes a “statement of parties’ views about why the proposal satisfies both their interests and the public interest.” The Parties have contributed the following separate statements of their independent views:

A.   Staff

10           Staff believes that the conditions CenturyTel and Embarq have agreed to under the Agreement will ensure that the Merger results in no harm to the Washington customers of the CenturyTel and Embarq local exchange companies, and that the Agreement is therefore consistent with the public interest. Staff’s conclusion is based on its review of company responses to a substantial volume of data requests propounded by Public Counsel, the International Brotherhood of Electrical Workers, and Staff; the pre-filed testimony of the Parties; and the Application.

11           Staff’s general concerns with the proposed Merger, as stated in the pre-filed testimony of Mr. Weinman and Ms. Erdahl, related to *potential* negative effects on the financial health and service quality of the CenturyTel and Embarq local exchange companies in Washington.

12           Overall, Staff concluded that the Merger will offset the balance sheet weaknesses of the Joint Applicants relating to goodwill and debt/equity ratio, resulting in a healthier combined company. Nonetheless, Staff was concerned that, absent protective conditions, there could be a risk of management distraction during the integration of

the two companies (or the potential for the local operating companies to be used as sources of cash to finance initial integration costs instead of the Washington companies' networks).

13 Staff initially recommended that the Commission should not approve the transaction without measures to protect the financial health of United and the CenturyTel ILECs, and the quality of the regulated telecommunications services provided by those entities. The Agreement addresses each of the conditions proposed by Staff and also includes additional commitments on the part of the companies that provide assurance that the Merger will not harm the public interest.

14 **Service Quality:** CenturyTel and Embarq historically have exhibited good service quality. The Agreement continues that tradition and requires the Merged Company ILECs to provide a service guarantee for twelve months immediately after the integration of the billing systems. The companies also commit to provide reports to Staff when various customer-affecting systems are changed, so that Staff can monitor for customer service problems that might result from the transition.

15 **Financial Health:** The Agreement includes the restrictions against pledging assets of the Merged Company ILECs to secure borrowing undertaken by the parent and against rate case advocacy for a higher cost of capital as compared with what the cost of capital would have been absent the Merger.

16           In addition the companies commit to file for an Alternate Form of Regulation (AFOR), with applicable earnings review, no later than five years after closing the Merger. In combination with that, the companies also commit not to file for a rate increase for tariffed residential (R1) service (“Stay Out”) within the first year after closing. Both of these conditions ensure that any synergy savings that are realized will be considered in an earnings review within a timeframe in which they are likely to be fully realized.

17           The third financial health related aspect of the Agreement is the restriction on the companies’ recovery of Merger costs in rates and a special accounting for those costs to enable Staff to verify their future exclusion.

18           **Other Conditions:** The other conditions in the Agreement are also consistent with the public interest by: (1) bringing digital subscriber line (DSL) broadband capability to 2,200 customers that are presently unserved, (2) providing the assurance of a customer notice, with Staff and Public Counsel input, to inform customers of any forthcoming name change, (3) enabling the company to waive charges for customers choosing to switch to a third party carrier if their interexchange (long distance) carrier is changed as a result of the Merger, and (4) facilitating the desired communication process with Lifeline and tribal agencies of the name change so that confusion is minimized for WTAP beneficiaries.

C. Public Counsel

19 Public Counsel believes that the Agreement provides a reasonable resolution of the issues raised in Public Counsel's direct testimony. The Agreement addresses, either generally or specifically, the majority of key issue areas raised by Public Counsel.

20 Notably, the Agreement includes provisions that: (1) continue to apply to United the conditions of the Separation Order; (2) impose finance conditions on the combined Company that are similar to the Separation Order finance conditions; (3) require customer notice of any future name change; (4) provide reasonable customer notice of any changes in long-distance providers resulting from the Merger and protect consumers from incurring any PIC charges associated with a change in long-distance provider following that notice; (5) provide benefits associated with synergy sharing in the form of a conditioned one-year-minimum "stay-out" for requests to raise residential rates; (6) prevent the recovery of merger related costs in rates; (7) contain a plan to expand broadband service to a significant portion of UTNW residential lines that are currently not DSL-capable; (8) provide "milestone reporting" that will enhance the Staff and Public Counsel's ability to monitor service quality during systems integration; (9) provide a LifeLine notification program associated with any future name change; and, (10) contain affiliated interest reporting commitments.

21 In addition to adopting these important conditions, the Agreement permits any party to address merger synergies in future rate proceedings. Staff and Public Counsel



also retain the right to request that an earnings review be undertaken as part of any AFOR proceeding (which the Agreement commits the companies to seek within a five-year period).

22 To supplement the information contained in the application materials, which the Public Counsel and the Administrative Law Judge in this case have suggested is limited, Public Counsel conducted substantial discovery, issuing over 150 data requests upon the Joint Applicants. Based on its review Public Counsel believes that this set of significant merger conditions adequately addresses the risks or potential harms that could otherwise result from the Merger. Public Counsel therefore recommends that the Commission approve the Agreement, as submitted, as being in the public interest.

B. Joint Applicants

23 The Agreement satisfies Joint Applicants' interests because it resolves the issues raised by Public Counsel and Staff in this docket without further delay, avoids a decision (and perhaps protracted litigation) over the more contentious issues, allows for timely approval of the Merger, and thereby brings benefits to the companies' Washington customers. As a result, the Agreement is in the public interest. Even without conditions, however, the proposed Merger does no harm to and produces significant benefits for Joint Applicants' Washington customers, as established in the Joint Applicants' testimony. The conditions in the Agreement address Staff's and Public Counsel's concerns with the proposed transaction, thus removing all sources of

doubt that the transaction is in the public interest. Therefore, the Joint Applicants believe that expeditious approval of the Agreement, including the conditions contained therein, serves their interests and the public interest.

**Legal Points that Bear on the Agreement**

24           The Parties agree that the transaction described in CenturyTel and Embarq’s Joint Application of November 24, 2008, should be authorized pursuant to Chapter 80.12 RCW and Chapter 480-143 WAC, as an “indirect merger,” at the parent company level, of the Washington public service company subsidiaries of CenturyTel and Embarq, listed in paragraph 3, above.

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**Conclusion**

25 The Parties respectfully request that the Commission approve the Agreement.

DATED this 22<sup>nd</sup> day of April, 2009

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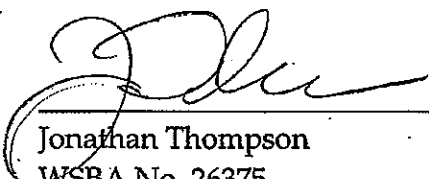
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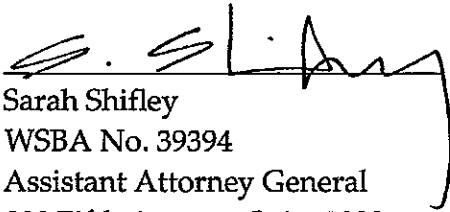
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