

**BEFORE THE WASHINGTON STATE
UTILITIES AND TRANSPORTATION COMMISSION**

In the Matter of the)	
)	
Request of Sprint Nextel Corporation)	DOCKET UT-051291
for an Order Declining to Assert)	
Jurisdiction Over or, in the Alternative,)	
Application of Sprint Nextel)	ORDER 06
Corporation for Approval of the)	
Transfer of Control of United)	
Telephone Company of the Northwest)	APPROVING AND ADOPTING
and Sprint Long Distance, Inc. From)	SETTLEMENT AGREEMENT
Sprint Nextel Corporation to LTD)	
Holding Company.)	
.....)	

Synopsis: The Commission approves Sprint Nextel Corporation’s proposed transfer of control of United Telephone Company of the Northwest (United) and Sprint Long Distance, Inc. (SLDI), from Sprint Nextel Corporation to LTD Holding Company, a/k/a Embarq, on conditions specified in a Settlement Agreement supported by all parties to this proceeding. The settlement conditions protect against harm to the public interest that might otherwise result from the proposed spin-off of United and SLDI, and provide benefits to United’s customers in Washington.

1 PROCEEDINGS: On August 26, 2005, Sprint Nextel Corporation (Sprint) requested the Commission to either decline to assert jurisdiction over, or grant Sprint’s application for approval of its proposed transfer of control of United Telephone Company of the Northwest (United) and Sprint Long Distance, Inc. (SLDI), from Sprint to LTD Holding Company, now known as Embarq.¹ The

¹ United will do business as Embarq following the corporate reorganization.

proposed transfer of control would separate Sprint's existing wireline local service operation into an independent, stand-alone company. The Commission took jurisdiction under chapter 80.12 RCW and set the application for hearing.

2 Sprint, Public Counsel and Commission Staff filed a Settlement Agreement on March 2, 2006, and ask the Commission adopt it as a full resolution of the issues in this proceeding. The parties recommend that the Commission approve the proposed transfer of control, subject to the conditions stated in the Settlement Agreement.

3 **PARTY REPRESENTATIVES:** Tre Hendricks, III, attorney, Sprint Corporation, Hood River, Oregon, and Gregory J. Kopta, Davis Wright Tremaine L.L.P., Seattle, Washington, represent Sprint Nextel. Simon J. ffitch and Judy Krebs, Assistant Attorneys General, Seattle, Washington, represent the Public Counsel Section of the Washington Office of Attorney General. Gregory J. Trautman, Assistant Attorney General, Olympia, Washington, represents the Commission's regulatory staff ("Commission Staff or Staff").²

4 **COMMISSION DETERMINATIONS:** The Commission finds that Sprint's proposed transfer of control of United and SLDI to LTD Holding Company (LTD) under the conditions stated in the parties' Settlement Agreement is consistent with the public interest. *WAC 480-143-170*. Accordingly, the Commission concludes that it should adopt the proposed Settlement Agreement as a full resolution of the issues in this proceeding and approve the proposed transfer of control under chapter 80.12 RCW.

² In formal proceedings, such as this case, the Commission's regulatory staff functions as an independent party with the same rights, privileges, and responsibilities as any other party to the proceeding. There is an "*ex parte* wall" separating the Commissioners, the presiding Administrative Law Judge, and the Commissioners' policy and accounting advisors from all parties, including Staff. *RCW 34.05.455*.

MEMORANDUM

I. Background and Procedural History

- 5 On August 26, 2005, Sprint filed an application requesting that the Commission decline to assert jurisdiction over the proposed separation of Sprint's local telephone division operations into a new holding company or, alternatively, to approve the separation. The proposed separation would transfer control of the corporate entities currently known as United and SLDI to LTD Holding Company, a new parent company.
- 6 The Commission conducted a first prehearing conference before Administrative Law Judge Dennis J. Moss on October 7, 2006, and entered Order No. 01, its prehearing conference order, on October 12, 2006. In Order No. 01, the Commission established a schedule, including dates for parties to prefile testimony and exhibits, and hearing dates.
- 7 Public Counsel filed a Petition for Interlocutory Review of Order No. 01 Regarding the Hearing Dates on October 21, 2005. The Commission denied Public Counsel's Petition on November 9, 2005.
- 8 Staff and Public Counsel filed testimony on November 30, 2005, contesting Sprint's application and recommending that the Commission either refuse to approve the proposed separation or impose several conditions on any such approval. These conditions included distribution to ratepayers of Washington's share of the gain from the 2003 sale of Sprint's directory publishing affiliate, prohibition on United's ability to recover transition and transaction costs from its ratepayers, requirements concerning service quality reporting and remedies, several conditions related to the continued financial health of the local exchange telephone entity (*i.e.*, "ring-fencing" provisions), and restrictions on affiliated interest agreements.
- 9 On December 8, 2005, Public Counsel filed its Renewed Motion for Continuance and Motion for Leave to File Cross-Rebuttal. Public Counsel argued that it should

have an opportunity to file cross-rebuttal testimony on the issue of rate rebalancing that was part of Staff's response case. On December 13, 2005, the Commission granted, in part, Public Counsel's Motion for Continuance, but denied Public Counsel's Motion for Leave to File Cross-Rebuttal.

- 10 Public Counsel, citing WAC 480-07-375, filed a "Motion for Reconsideration" of the Commission's denial of its Motion for Leave to File Cross-Rebuttal on December 16, 2005. The Commission treated Public Counsel's motion as a petition for review of interlocutory order as provided under WAC 480-07-810. The Commission again denied Public Counsel's Motion for Leave to File Cross-Rebuttal in Order No. 05, entered on December 23, 2005.
- 11 The Commission also required in Order No. 05 that the parties to file prehearing briefs on January 25, 2006, presenting their arguments concerning whether rate rebalancing and directory publishing issues were properly before the Commission in this proceeding. The Commission conducted a prehearing conference on January 30, 2006. By oral order, the Commission determined that rate rebalancing would not be considered in this proceeding.
- 12 The Commission ordered that issues related to Sprint's 2003 sale of its directory publishing business would be considered and authorized the parties to file supplemental testimony on February 6 and 13, 2006. Evidentiary hearings were scheduled for February 27 through March 1, 2006.
- 13 The parties informed the Commission on February 22, 2006, that they had achieved a settlement in principle. The Commission suspended the procedural schedule. The parties filed their "all-party," "unanimous" Settlement Agreement on March 2, 2006, supplemented by a joint narrative in support, as required under WAC 480-07-740(2)(a).

- 14 Commission Chairman Mark H. Sidran, Commissioners Patrick J. Oshie and Philip B. Jones, and Administrative Law Judge Moss heard testimony in support of the proposed settlement on March 6, 2006.³

II. Settlement Agreement

- 15 The parties ask the Commission to approve the separation of Sprint's local telephone division operations, including United and SLDI, into a new company as being in the public interest subject to conditions contained in eight issue areas: (1) directory sale, (2) recovery of separation, branding and transition costs, (3) service guarantee, (4) service quality, (5) customer notice, (6) finance conditions, (7) affiliated interest agreements, and (8) broadband reporting. The witnesses who appeared at the settlement hearing identified the conditions related to the gain on the sale of directory publishing in 2003 and the finance, or ring-fencing conditions as being particularly significant.
- 16 The parties agree that \$9,789,750 of the gain Sprint realized from the sale of its directory publishing business in 2003 will be attributed to ratepayers for purposes of settlement. The parties agree to a ten year amortization of the gain, beginning January 1, 2008, or at the effective date of new rates, if sooner. The annual amortization amount will be \$1.451 million. This amount will be substituted for the revenue imputation currently embedded in rates. Sprint also agrees to issue a one-time bill credit of \$400,000 to United's retail customers on a per account basis within 60 days after the separation.
- 17 The parties agree to several ring-fencing provisions which will be effective for no less than four years or until such time as United is classified as a competitive communications company in Washington under RCW 80.36.320. The provisions include limitations on dividends under two specified conditions:

³ Following the hearing, the parties memorialized three corrections to the Settlement Agreement filed on March 2, 2006. The parties filed revised substitute page 6 on March 8, 2006, and revised page 3 on March 10, 2006. The final version of the Settlement Agreement is attached to this order as an Appendix.

- LTD's common equity ratio is less than 50% relative to the book value of its net debt.⁴
- Neither LTD nor United (if rated separately) is assigned an investment grade corporate credit rating by two of more of the major credit rating agencies (*i.e.*, Moody's, S&P, and Fitch).

18 Sprint also agrees that neither LTD Holdings nor United will pledge United's assets to secure any borrowing by LTD or its affiliates and subsidiaries other than United.

19 The remaining conditions include agreements that:

- United will not seek to recover in rates costs arising from the reorganization.
- United will offer a service guarantee in its tariff in the form of a \$15 credit to residential customers or \$25 to business customers for missed repair or installation commitments, if missed for reasons within the company's control. This is similar to a tariff provision applying to United's operations in Nevada.
- United will continue to comply with applicable Commission-approved service quality requirements.
- United will provide individual customer notice of the separation, name change, and any change to the bill format.
- If customers choose a long distance carrier other than SLDI within 90 days after the receiving notice of the change, they will not be charged a Primary Interexchange Carrier (PIC) charge.
- United will not contest the "affiliated interest" status of any contracts negotiated with Sprint prior to the separation and will provide relevant cost data about those transactions in any proceeding in which revenue or expenses relating to such contracts are in issue.

⁴ Common equity and net debt are defined in the Settlement Agreement.

- United will provide information to Staff or Public Counsel, on request, concerning broadband services deployment.

III. Discussion and Decision

- 20 The parties identified in their testimonies a number of concerns regarding the proposed transaction, which they propose to resolve by their settlement. The Settlement Agreement sets forth conditions intended to mitigate the potential negative consequences of the separation identified through the testimony by witnesses for Public Counsel and Staff. The possibility of parent company financial distress adversely affecting the local exchange carrier was the most significant concern identified by Commission Staff in its review of the proposed transaction. Public Counsel also identified this as among its more significant issues.
- 21 Section E.6. of the Settlement Agreement implements corporate finance commitments to protect the financial health of the local exchange carrier should the parent company or its affiliates experience financial distress. These commitments include financing restrictions, dividend restrictions, monitoring and reporting requirements that will continue for four years following the spin-off. Company actions and reports under these commitments are triggered either by ratings agencies' evaluations that lower corporate credit ratings for United or its new parent to less than investment grade or by internal company financial analysis that shows the average market value of LTD's common equity is less than 50 percent of the book value of LTD's debt. Based on the parties' joint narrative statement, and other evidence, we find that Section E.6. of the Settlement Agreement adequately addresses these potential impacts to United.
- 22 The settlement also recognizes the value to United of Sprint's sale of its directory publishing business in 2003. Section E.1. of the Settlement Agreement establishes an agreed amount of gain to be attributed to ratepayers and a basis for treating the gain in future rate proceedings. Section E.1. provides for an annual revenue credit of \$1.451 million per year for 10 years to replace the current directory revenue

imputation. In addition, a customer bill credit totaling \$400,000 will be distributed to retail customers on a per account basis within 60 days after the spin-off is finalized.

23 Section E.2. of the Settlement Agreement prevents the company from recovering in current or future rates the costs of separation, rebranding and transition. It thus addresses Commission Staff's concern that the transaction might impose additional costs on United's ratepayers.

24 We find that section E.1. of the Settlement Agreement establishes a reasonable basis for treating the gain from Sprint's sale of its directory publishing business in future rate proceedings and provides immediate benefits to current customers. We find that the provisions in section E.2. also protect ratepayers from transaction-related costs that they should not bear.

25 Sections E.3. and E.4. of the Settlement Agreement concern the reorganized local exchange company's obligation to continue providing high-quality service to its customers. All parties recognize that United has established a good record over recent years in terms of service quality. The service guarantees established in section E.3. give the company a financial incentive to continue to provide good installation and repair service and will compensate customers when service is inadequate. Section E.4. serves to focus the company's attention on its existing service quality obligations established by statute and rule. We find these provisions both preserve and enhance United's commitment to provide good service to its customers.

26 In summary, the proposed settlement is consistent with the public interest because it includes a set of commitments that emphasize important public service obligations and protect the local service company's customers from potential harm. The Settlement Agreement includes well-crafted safeguards intended to protect United's customers from any financial distress experienced by other

companies within the new holding company structure. The settlement protects the Commission's ability to regulate in the public interest and set rates that are fair, just, reasonable and sufficient by establishing facts, accounting and rate treatment with respect to Sprint's sale of its directory publishing business in 2003, and costs associated with, or arising from the proposed spin-off. The Settlement Agreement also includes commitments to maintain a high level of service quality.

- 27 We find that the proposed transaction, conditioned by the commitments made in the Settlement Agreement, is consistent with the public interest. We find that the requirements under chapter 80.12 RCW and chapter 480-143 WAC governing transfers of property are satisfied. Accordingly, we conclude that we should approve Sprint's application for transfer of control, as modified by the terms of the Settlement Agreement, which is appended to and made a part of this order.

FINDINGS OF FACT

- 28 Having discussed above all matters material to our decision, and having stated general findings, the Commission now makes the following summary findings of fact. Those portions of the preceding discussion that include findings pertaining to the Commission's ultimate decisions are incorporated by this reference.
- 29 (1) The Washington Utilities and Transportation Commission is an agency of the State of Washington, vested by statute with authority to regulate rates, rules, regulations, practices, accounts of, and transfers of property by public service companies, including telecommunications companies.
- 30 (2) Sprint is a "public service company" and a "telecommunications company" as those terms are defined in RCW 80.04.010 and as those terms otherwise are used in Title 80 RCW. Sprint is engaged in Washington State in the business of supplying utility services and commodities to the public for compensation.

- 31 (3) On August 26, 2005, Sprint filed an application requesting that the Commission decline to assert jurisdiction over the proposed separation of Sprint's local telephone division operations into a new holding company or, alternatively, to approve the separation. The proposed separation would transfer control of the corporate entities currently known as United and SLDI to LTD, a new parent holding company.
- 32 (4) On March 2, 2006, Sprint, Commission Staff and Public Counsel filed a Settlement Agreement and requested the Commission to adopt its terms as conditions for approval of the proposed transaction and as a full resolution of the issues pending in this proceeding.
- 33 (5) The terms of the parties' Settlement Agreement are as set forth in the Appendix to this order which is incorporated into the body of this order by reference, as if set forth in full.

CONCLUSIONS OF LAW

- 34 Having discussed above in detail all matters material to our decision, and having stated general findings and conclusions, the Commission now makes the following summary conclusions of law. Those portions of the preceding detailed discussion that state conclusions pertaining to the Commission's ultimate decisions are incorporated by this reference.
- 35 (1) The Washington Utilities and Transportation Commission has jurisdiction over the subject matter of, and parties to these proceedings. *Title 80 RCW.*
- 36 (2) Chapter 80.12 RCW requires public service companies to secure Commission approval before they can lawfully dispose of the whole or any part of their franchises, properties or facilities that are necessary or useful in the performance of their duties to the public. *RCW 80.12.020.* Any disposition made without Commission authority is void. *RCW 80.12.030.*

- 37 (3) The Settlement Agreement filed in this proceeding, considered in the light of the record, including supportive testimony from all parties, fairly resolves the issues and should be approved and adopted as the Commission's determination of the issues. The proposed transaction, subject to the requirements stated in the Settlement Agreement, is consistent with the public interest. *WAC 480-143-170*. Accordingly, Sprint's application for approval of the transfer of United and SLDI to LTD subject to the terms included in the Settlement Agreement should be granted.
- 38 (4) United, whether doing business under that name or another, should be required to file within 30 days after its transfer to LTD a petition for an accounting order to establish its authority to establish such deferral, side-bar, or other account(s) as necessary to make effective the terms of Section E.1. of the Settlement Agreement.
- 39 (5) The Commission should retain jurisdiction over the subject matter and the parties to effectuate the terms of this order.

ORDER

THE COMMISSION ORDERS THAT:

- 40 (1) The parties' request for leave to file revised pages to their Settlement Agreement as filed in this proceeding on March 2, 2006, is granted.
- 41 (2) The Settlement Agreement attached as an Appendix to this order is approved and adopted in full resolution of the issues pending in this proceeding.
- 42 (3) Sprint's Application for Approval of the Transfer of Control of United Telephone Company of the Northwest and Sprint Long Distance, Inc., from Sprint Nextel Corporation to LTD Holding Company, filed on August 26,

2005, as modified by the terms of the Settlement Agreement, is consistent with the public interest and is approved.

- 43 (4) United, whether doing business under that name or another, is required to file a petition for an accounting order within 30 days after its separation from Sprint to establish its authority to maintain deferral, side-bar, or such other account(s) as necessary to make effective the terms of Section E.1. of the Settlement Agreement. The filing is to be made as a “subsequent filing” under WAC 480-07-880 and -885.
- 44 (5) The Commission retains jurisdiction to effectuate the terms of this Order.

DATED at Olympia, Washington, and effective March 13, 2006.

WASHINGTON STATE UTILITIES AND TRANSPORTATION COMMISSION

MARK H. SIDRAN, Chairman

PATRICK J. OSHIE, Commissioner

PHILIP B. JONES, Commissioner

NOTICE TO PARTIES: This is a final order of the Commission. In addition to judicial review, administrative relief may be available through a petition for reconsideration, filed within 10 days of the service of this order pursuant to RCW 34.05.470 and WAC 480-07-850, or a petition for rehearing pursuant to RCW 80.04.200 or RCW 81.04.200 and WAC 480-07-870.

APPENDIX