

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

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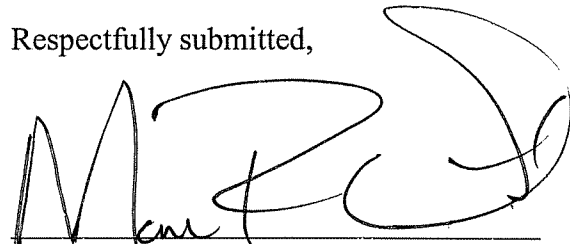
APPLICATION FOR APPROVAL OF THE )  
TRANSFER OF CONTROL OF ALLTEL ) CASE NO.  
KENTUCKY, INC. AND KENTUCKY ) 2005-00534  
ALLTEL, INC. )

PUBLIC SERVICE  
COMMISSION

APPLICANTS' RESPONSES TO INITIAL DATA REQUEST OF  
COMMISSION STAFF TO APPLICANTS

Pursuant to Administrative Regulation 807 KAR 5:001, Alltel Kentucky, Inc., Kentucky Alltel, Inc., Alltel Communications, Inc., Alltel Holding Corp., Valor Communications Group, and Alltel Holding Corporate Services, Inc. (collectively, "Applicants") file the following Responses to the Commission Staff Initial Data Requests:

Respectfully submitted,



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**CERTIFICATE OF SERVICE**

I hereby certify that a true and accurate copy of the foregoing was served via overnight delivery or as noted below upon the following:

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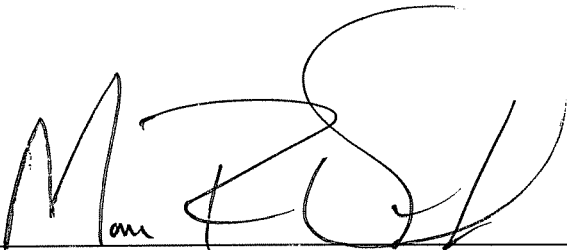
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on this the 13<sup>th</sup> day of March, 2006.

  
\_\_\_\_\_  
Mark R. Overstreet

1. Refer to Gardner Testimony page 3, line 14. Explain how a significantly larger wireline company, as compared to other rural local exchange companies, is a benefit to Kentucky ratepayers.

**Response: See answer to question 2 related to the benefits of economies of scale and scope of the Merged Wireline Business.**

**Response provided by Brent Whittington.**

2. Refer to Gardner Testimony page 3, lines 15-17.
  - a. Explain how increased scale is a benefit to Kentucky ratepayers.
  - b. Explain how increased scope is a benefit to Kentucky ratepayers.

**Response to (a) and (b): The Merged Wireline Business will be the largest rural telephone holding company in the United States. It will provide service to approximately 3.4 million wireline customers in 16 states. Its annual revenues are expected to be approximately \$3.4 billion and it should generate approximately \$1.7 billion of annual operating income before depreciation and amortization. This company's size will provide the Merged Wireline Business with increased buying power which translates into lower costs of equipment, network, materials and supplies. After centralized support staffing is complete, the Merged Wireline Business will be able to accomplish additional growth in access lines and related wireline services at lower costs per unit and, therefore, expects potential reductions in per access line allocations and related costs per unit for deployment of advanced services.**

**Response provided by Brent Whittington.**

- c. Provide a discussion of the support services that are currently provided to regulated entities by Alltel Corporation.

**Response: Alltel Corporation currently provides the following services: marketing, customer service, network planning, finance, HR management, legal, and information services.**

**Response provided by Jeffery Gardner.**

d. Provide a discussion of how the level of support services that are currently provided to regulated entities is going to be improved. Also, provide a chart that documents how the support service levels are currently tracked (benchmarks) and the improvement goals for each category that will be achieved after the merger.

**Response: A corporate team solely dedicated to the support of its wireline operations will improve the Merged Wireline Business's level of centralized services to its wireline subsidiaries. The singularly focused corporate support team will be able to respond more quickly and will not find it necessary to consider the ramifications of its actions and decisions on wireless services or deployment of wireless services. The wireline business will not have to justify its capital and other needs in comparison to that of wireless counterparts.**

**Response provided by Jeffery Gardner.**

3. Refer to Gardner Testimony page 6.

a. Provide a description of how the regulated entities will finance necessary and large capital improvements in their outside plant and infrastructure.

**Response: The regulated entities will receive advances from the new holding company to finance their capital investments. This is the current process, and no changes will occur as a result of the transactions other than singular focus without competition for capital by wireless.**

**Response provided by Brent Whittington.**

b. Provide a discussion of how capital will be budgeted and allocated to the various subsidiaries by the New Holding Company.

**Response: Capital expenditures will be budgeted and allocated as it is today, with no changes in the capital budget process or allocation methodologies as a result of the transactions.**

**Response provided by Brent Whittington.**

c. Do the regulated entities in Kentucky anticipate maintaining at least the same levels of O&M expenditures and capital investment in Kentucky as before the spin-off and merger? Explain.

**Response: Yes.**

**Response provided by Brent Whittington.**

4. Refer to Gardner Testimony pages 6 and 9-10. Provide the current dividend policy and rate regarding the remission from regulated entities in Kentucky to the current parent corporation. Does the New Holding Company anticipate any changes to the current dividend payment policy (the remission rate) regarding the regulated entities to the new parent? Explain and quantify any differences.

**Response: A subsidiary pays a dividend monthly to its parent company only if two criteria are met: (1) subsidiary has a net income, and (2) subsidiary's debt-to-equity ratio is 0.65 or below. If both criteria are met, then the dividend from the subsidiary to parent is equal to 90% of subsidiary's net income. This dividend policy will not change due to the transactions.**

**Response provided by Brent Whittington.**

5. Refer to Gardner Testimony page 9. Provide the exact citation in Exhibit 1 that documents that the expected New Holding Company will produce annual operating income before depreciation and amortization of \$1.7 billion.

**Response: Refer to the Unaudited Pro Forma Combined Condensed Statements of Income for Valor Communications Group Inc. from the column labeled “Combined” and add Operating Income (\$1,091.4 million) and Depreciation and Amortization (\$577.6 million). The resulting amount of \$1,669 million is the estimated 2005 annual operating income before depreciation and amortization of the New Holding Company.**

**Response provided by Brent Whittington.**



6. Refer to Gardner Testimony page 10.

a. Provide the calculations for the debt equity ratios of the current parent and the debt equity ratios anticipated for the New Holding Company after the merger.

**Response: Attached hereto are the debt to enterprise values.**

**Response provided by Brent Whittington.**

b. Explain why distributing a greater percentage of free cash flow back to the parent than do similarly situated ILECs is beneficial for Kentucky ratepayers.

**Response: This question is inappropriate as Applicants have not made such a statement. The question appears to confuse the dividend the new holding company will pay to its shareholders with the dividends the wholly-owned subsidiaries pay to their shareholder (i.e., their holding company). The percentage of cash that the operating companies (such as Alltel Kentucky and Kentucky Alltel) distribute to their parent company will not change as a result of the transactions. The parent company will distribute a greater percentage of its cash flow back to its shareholders to make the stock attractive to investors and ensure the Merged Wireline Business can obtain the capital it needs in the future.**

**Response provided by Brent Whittington.**

**Alltel Holding Corporate Services**

Calculation of Debt to Enterprise Value

KY PSC Initial Data Request, question 6.a.

<b>CURRENT PARENT (Alltel Corporation)</b>	
DEBT	\$      £
ENTERPRISE VALUE (EV):	
Equity:	
Common stock outstanding, 12/31/05	
Closing stock price, 12/30/05	\$
Total Equity ( b x c )	\$
Debt:	\$
TOTAL ENTERPRISE VALUE ( a + d )	\$
DEBT / EV RATIO ( a / e )	

<b>NEW HOLDING COMPANY</b>	
DEBT	\$
ENTERPRISE VALUE (EV):	
Equity:	
Common stock outstanding, 12/31/05	
Closing stock price, 12/30/05	\$
Total Equity ( b x c )	\$
Debt:	\$
TOTAL ENTERPRISE VALUE ( a + d )	\$
DEBT / EV RATIO ( a / e )	

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7. Refer to Gardner Testimony page 10, lines 8-12. Does the statement mean that the company is so highly leveraged that it must issue new stock to fund future capital needs as opposed to issuing debt? Explain.

**Response: No, it does not. Additional capital expenditures will be funded through operating cash flow.**

**Response provided by Brent Whittington.**

8. Refer to Gardner Testimony page 11. Provide a copy of the solvency opinion from Duff & Phelps, LLC.

**Response: A copy of the draft solvency opinion will be available later this week and provided immediately thereafter. It is labeled draft because the final opinion will not be required by Alltel until a future board meeting immediately prior to close of the transactions at which time the Alltel Board will approve the dividends and distributions required to consummate the transactions. The draft opinion, however, provides definitive conclusions regarding solvency and is the result of a completed analysis by Duff and Phelps, subject only to being brought forward for passage of time to the date of the next Alltel Board meeting and then made final.**

**Response provided by Brent Whittington.**

9. Refer to Gardner Testimony page 13.

a. Identify the companies which are being used as comparable companies to the New Holding Company.

**Response: Century Tel (CTL), Citizens (CZN), Iowa Telecommunications (IWA), Fairpoint Communications (FRP), Consolidated (CNSL) and Commonwealth (CTCO).**

**Response provided by Jeffery Gardner.**

b. Provide a chart which compares the companies by name referred to in the testimony to the anticipated financial measures of the New Holding Company.

**Response: A chart comparing the capital structure of the Merged Wireline Business to the companies mentions in Part (a) of the questions was included in Mr. Gardner's testimony as Exhibits 2 and 3.**

**Response provided by Jeffery Gardner.**

10. Refer to Exhibit 1 of Gardner Testimony. Provide the analogous balance sheets and income statements for Alltel Corporation and for the wireless business as that provided for Alltel Holdings, Valor, and the new combined company as in Exhibit 1.

**Response: Alltel Corporation analogous balance sheets and income statements for year ended December 31, 2005 do not exist. There are no analogous balance sheets or income statements for the wireless business.**

**Response provided by Brent Whittington.**

11. Provide a detailed explanation of the methodology for assigning the existing debt of Alltel Corporation to the new wireless and wireline entities before the merger with Valor Communications Group.

**Response: Alltel Corporation debt is not being assigned. The Merged Wireline Business will issue its own debt. As explained in the Amended and Restated Application and Mr. Gardner's testimony, the Merged Wireline Business will provide Alltel Corporation consideration for the existing Alltel wireline business, including the tax basis in such business.**

**Response provided by Brent Whittington.**

12. Of the total Alltel Corporation debt being assigned to Alltel Holding, provide a detailed discussion of the debt and a chart illustrating the assignment of debt between the incumbent local exchange carriers by state, competitive local exchange carriers, Internet, long distance, telecommunications information services, directory publishing, and product distribution operations for the year ended December 31, 2005.

**Response: Prior to the spin-off and merger with Valor, Alltel Holding Corp. will borrow approximately \$4.9 billion through a new senior secured credit agreement and the issuance of unsecured debt securities in a private placement or through a public offering and through the distribution to Alltel of \$1.538 billion of Alltel Holding Corp.'s debt securities. Proceeds from the debt issuance will be used to pay a special dividend to Alltel in an amount not to exceed Alltel's tax basis in Alltel Holding Corp. and for other purposes, including the repayment of certain debt obligations of Valor and Alltel Holding Corp. The Alltel Holding Corp. debt will not be assigned to the incumbent local exchange carriers by state, competitive local exchange carriers, Internet, long distance, telecommunications information services, directory publishing, or product distribution operations. Also see response to question 11.**

**Response provided by Brent Whittington.**



13. Provide a detailed, step-by-step explanation of what the spin-off of Alltel Holdings and the wireless business and then the merger of Alltel Holdings and Valor will mean to a small shareholder (1,000 shares) of Alltel Corporation stock, including any cash payments and dividends and the number of shares in all companies the shareholder will own after the spin-off and merger.

**Response: Each shareholder will maintain his or her existing shares of Alltel Corporation stock. In addition, he or she will receive approximately 1.04 shares of the new company for each Alltel share owned. Alltel expects to pay an annual dividend of \$.50 per share, and the new company will pay an annual dividend \$1.00 per share. The total combined annual dividends of the MWB and Alltel represent a slight increase from Alltel's annual dividends today.**

**Response provided by Brent Whittington.**

14. Refer to Exhibit 1 of Mr. Gardner's testimony. The new combined company appears to have taken on \$5.517 billion in debt and doubled the amount of goodwill carried on its books.

a. The new combined company is a debt-financed company. Provide a detailed explanation of how this company is financially stronger and more viable than Alltel Holdings prior to being spun off.

**Response: Relative to peers, the new company is very well capitalized. In addition, the wireline separation creates enhanced strategic, financial and operational opportunities for the new wireline company.**

**Response provided by Brent Whittington.**

b. Provide a detailed explanation of the exact benefits, quantifiable if possible, that Kentucky ratepayers can expect from the merger of Alltel Holdings and Valor.

**Response: The Merged Wireline Business will be the largest rural telephone holding company in the United States. It will provide service to approximately 3.4 million wireline customers in 16 states. Its annual revenues are expected to be approximately \$3.4 billion and it should generate approximately \$1.7 billion of annual operating income before depreciation and amortization. This company's size will provide the Merged Wireline Business with increased buying power which translates into lower costs of equipment, network, materials and supplies. After centralized support staffing is complete, the Merged Wireline Business will be able to accomplish additional growth in access lines and related wireline services at lower costs**

**per unit and, therefore, expects potential reductions in per access line allocations and related costs per unit for deployment of advanced services.**

**Response provided by Brent Whittington.**

15. Refer to Note (b) in Exhibit 1 of Mr. Gardner's testimony. Provide a detailed explanation of why a special dividend, estimated at \$2.4 billion, is being paid to Alltel in an amount not to exceed Alltel's tax basis in Alltel Holdings.

**Response: To accomplish the separation and compensate Alltel Corporation for the wireline business and appropriately capitalize the separate companies.**

**Response provided by Brent Whittington.**

16. Valor has a negative net worth, more debt than assets. Explain how the addition of Valor will bring value to the new company.

**Response:** See response to question 2(a) and 2(b). The additional scale and scope of the new company will allow it to have access to capital, allow it to lower its operating costs, and provide additional bargaining power when negotiating with vendors.

**Response provided by Brent Whittington.**

17. What is included in the category “other assets” on Valor’s balance sheet?

**Response:** As of December 31, 2005, Valor had approximately \$52.4 million in the “other assets” category, which was composed of the following items:

<b>Unamortized debt issuance costs</b>	<b>\$30.7 million</b>
<b>Rural Telephone Finance Corp equity certificates</b>	<b>\$ 7.7 million</b>
<b>Investments in cellular partnerships</b>	<b>\$ 7.4 million</b>
<b>Other assets</b>	<b><u>\$ 6.6 million</u></b>
<b>Total other assets</b>	<b>\$52.4 million</b>

**Response provided by Brent Whittington.**

18. Explain how Valor's unfunded pension liability will affect the new company's overall pension liability. Does Alltel have any unfunded pension liability?

**Response: As of December 31, 2005, neither Valor nor Alltel has an unfunded pension liability per ERISA guidelines.**

**Response provided by Brent Whittington.**

19. Give a brief history of Valor's operations, including the date it began, former names it may have operated under, acquisition history, and principle owners.

**RESPONSE:**

**History of Valor's Operations**

Valor is one of the largest providers of telecommunications services in rural communities in the southwestern United States. Formed in 2000, Valor operates telephone access lines in primarily rural areas of Texas, Oklahoma, New Mexico and Arkansas.

Headquartered in Irving, Texas, Valor operates as a rural local exchange carrier that has been operating in these markets for over 75 years. Valor offers a wide range of telecommunications services to residential, business and government customers, including local exchange telephone services, long distance, bundled services, DISH™ Network Satellite TV, high-speed DSL Internet, and access services.

Valor Communications Group, Inc., was formed in 2004, as the holding company for Valor's operations. In February 2005, Valor Communications Group announced its initial public offering, trading under the ticker symbol "VCG" on the New York Stock Exchange.

**Former Names**

dba Communications Inc.

VALOR Telecommunications Southwest, LLC

VALOR Telecommunications of New Mexico, LLC

VALOR Telecommunications of Oklahoma, LLC

VALOR Telecommunications of Texas, LP

**Acquisition History**

Valor acquired select telephone assets from GTE Southwest Corporation (GTE) in 2000, which is now part of Verizon. The company purchased all of the GTE access lines in Oklahoma and New Mexico and approximately 15 percent of GTE's access lines in Texas. A portion of the access lines acquired in Texas is physically located in Texarkana, Ark.

In January 2002, Valor acquired Kerrville Communications Corporation, the local telephone company serving Kerrville, Texas, which includes Kerrville Telephone Company, Advanced Tel-Com Systems Corporation, Kerrville Cellular Inc., and part ownership of Five Star Wireless.

**Principal Owners**



**Valor's formation was orchestrated by equity sponsors Welsh, Carson, Anderson & Stowe, Vestar Capital Partners, Citicorp Venture Capital, and a group of 12 Hispanic investors.**

**Valor Communications Group is a publicly traded company listed on the NYSE under the symbol "VCG."**

**Original equity partners, Welsh, Carson, Anderson & Stowe, and Vestar Capital Partners are major stockholders.**

**Response provided by Brent Whittington**

20. Is Valor being investigated currently by any state or federal regulatory body?

**Response: No.**

**Response provided by Michael Rhoda**

21. Has Valor had any investigations or judgments against it by any state or federal regulatory body in the past four years?

**Response: The Texas Public Utility Commission initiated an investigation against Valor following complaints from customers in Texarkana. After an investigation, the Staff of the Commission issued a report and recommended enforcement action against the Company for alleged violations of the Commission's rules. Prior to the initiation of an enforcement action, the Company and the Staff engaged in a series of negotiations. After a series of negotiations, the parties reached an agreement in principle, the key terms of which include: a refund of \$346,092 to touchtone customers (the refund was made in 2003); payment of an administrative penalty of \$350,000; and a commitment to make incremental infrastructure investments of \$1,945,000 in 2004 and \$500,000 in 2005. The agreement was executed by Valor and the Staff and filed with the Commission on April 7, 2004. The Texas Commission approved the Settlement Agreement on June 9, 2004. Valor is in compliance with the requirements set forth in the Settlement Agreement.**

**Response provided by Michael Rhoda.**