410

OPEN MEETING
ORIGINAL

MEMORANDUM

TO: THE COMMISSION

FROM: Utilities Division

DATE: October 15, 2004

RE: IN THE MATTER OF THE APPLICATION OF EVERCOM SYSTEMS, INC. IN CONNECTION WITH AN INDIRECT TRANSFER OF CONTROL AND THE PROVISION OF CERTAIN SECURE AND UNSECURED GUARANTEES (DOCKET NO. T-03479A-04-0549)

On July 29, 2004, Evercom Systems, Inc. ("ESI" and "Applicant"), pursuant to the Public Utility Holding Companies and Affiliated Interest Rules of the Arizona Administrative Code ("A.A.C.") R14-2-801 et seq. ("Affiliated Interest Rules") and Arizona Revised Statutes ("A.R.S.") §40-285, requested that the Commission: (a) expeditiously waive the application of the Affiliated Interests Rules concerning its indirect transfer of control and guarantees or (b) in the alternative, expeditiously approve those transactions under the Affiliated Interests Rules without a hearing. ESI further requests, pursuant to A.R.S. §40-285, that the Commission approve ESI's request to encumber its assets in Arizona pursuant to the secured guarantee described in its Application. On August 27, 2004, ESI filed an amendment to its initial Application to reflect certain changes in the facts that occurred since the time it filed its original Application.

ESI, the Applicant, was certificated to provide Customer Owned Pay Telephone ("COPT") services in Arizona in Decision No. 60924. On May 22, 1998, in Decision No. 60924, the Commission granted to Talton Invision, Inc. a Certificate of Convenience and Necessity authorizing it to provide COPT services throughout Arizona. On January 25, 1999, Talton Invision, Inc. changed it name to ESI.

In its Application, ESI states that it provides inmate telecommunications services in Arizona and forty-three other jurisdictions, offering local, intrastate, interstate and international calling services to inmates in more than 2000 correctional facilities nationwide.

ESI further stated that it is a privately held company incorporated under the laws of the State of Delaware and that its principal offices are located in Irving, Texas. It further stated that it is a wholly owned subsidiary of Evercom, Inc. ("EI"), a Delaware corporation which is in turn a wholly owned subsidiary of Evercom Holdings, Inc. ("EHI").

In its initial Application and the Amendment to its Application, ESI provided the following information relating to the indirect parent level transfer of control and encumbrance of its assets for which it requests Commission approval:

Proposed Merger Transaction

EHI entered into a merger agreement, dated July 10, 2004, with (a) TZ Holdings, Inc. ("TZ"), a State of Delaware corporation, and (b) New Mustang Acquisition, Inc. ("Mustang"), another State of Delaware corporation which is a wholly-owned subsidiary of TZ. Upon completion of the proposed transaction EHI will be a wholly-owned subsidiary of TZ. In its Amendment to its Application, ESI stated that TZ had changed its corporate name to Securus Technologies, Inc. ("STI").

ESI further stated that TZ (hereinafter called STI) is majority-owned by H.I.G.-TNetix, Inc., an affiliate of H.I.G. Capital, LLC ("HIG"), a Miami-based private equity firm, which has over $1 billion under management. ESI further stated that Investors in HIG-managed funds include leading financial institutions, insurance companies, pension funds and university endowments. According to ESI, STI has no other operational purpose other than to hold ownership interests in various enterprises in which HIG has invested.

ESI states that STI formed Mustang for the sole purpose of effecting the proposed merger and upon the merger's completion; Mustang will be merged out of existence. The merger will be accomplished through Mustang's merger into EHI. As part of the merger of EHI into Mustang, all of the current stock and stock options of EHI shall be converted or retired. The retirement will be accomplished through STI's purchase of EHI stock or options from the current shareholders; and the former EHI treasury stock will be retired. ESI further explained that simultaneous with the closing of the merger, certain former stockholders of EHI will acquire certain stock of STI in an aggregate amount so that the ratio of STI common stock owned by HIG (or its affiliates) to STI common stock owned by the former EHI stockholders is not greater than 65:35 immediately after giving effect to the merger.

Organization charts depicting all the affiliates and their relationships with the holding company relating to the proposed indirect transfer of control of ESI are shown in Attachment A, Attachment B, and Attachment C. The following describes the activities and transactions of each affiliate involved in the proposed transfer as represented by the various Attachments:

a) The current ownership structure of ESI and affiliates is shown on Attachment A;

b) Attachment B shows the pre-merger ownership structure. STI is the parent company of Mustang. EHI, the indirect parent of ESI, and its subsidiaries will merge into Mustang as stated in the initial Application; and

c) Attachment C, which indicates the post-merger subsidiaries structure, shows that Mustang will be replaced by EHI and its subsidiaries.

ESI further states that upon completion of the merger, the current existing, inter-corporate relationships between ESI, EI and EHI shall remain totally unchanged. ESI's immediate parent (and its parent's parent) will remain the same. However EHI will become a wholly-owned subsidiary of STI, which will be majority owned by H.I.G-TNetrix, Inc., an affiliate of HIG, the Miami-based private equity firm.

ESI states that it will remain a separately certificated entity providing the services it currently offers. The transaction will be transparent to the customer of ESI. ESI states that there will be no immediate changes in the terms and conditions of the services provided by ESI, pursuant to the applicable tariffs or price lists that ESI currently has on file as approved by the Commission. ESI will continue to market, brand and bill its services as it has done in the past. There are no current plans to change the management structure of ESI.

Based on the data requests sent to the Applicant, Staff obtained the following additional information:

- ESI currently has contracts with 10 confinement facilities in Arizona to provide telecommunications services to inmates (Based on ESI's 2003 Utility Annual Report for Customer Owned Pay Telephone Provider, ESI currently provides pay telephone service to 11 confinement locations in Arizona);

- The post-merger ownership of STI is as follows: H.I.G.-TNetix, Inc, will own 59 percent and other minority stockholders, including former stockholders of EHI, will own 41 percent. The largest single minority stockholder is Alexander Enterprise Holdings Corp., a private investment partnership based in Miami, Florida, will own about 10 percent of STI. Among the remaining stockholders, no individual stockholder will directly hold more than 5 percent of STI; and

- ESI's current value of depreciated assets used to provide telecommunications services in Arizona is approximately $100,000.

As part of its request for waiver of the Affiliated Interest rules, ESI states that it has a very modest presence in the State of Arizona. Approximately one percent of its assets are located in Arizona and its Arizona intrastate revenues are less than five percent of its total revenues in 2003.

Affiliated Interest Rules

ESI is a Class A utility that is subject to A.A.C. R14-2-801 et seq., the Affiliated Interests Rules. Staff reviewed the Applicant's 2003 annual report filed with the Commission to determine the applicability of ESI as a Class A investor owned utility. A telecommunications carrier that has Arizona jurisdictional revenues of more than $1 million is considered to be a Class A utility. ESI, an investor-owned utility, generated more than $1 million of Arizona revenue in 2003.

ESI believes that a waiver of the application of the Affiliated Interests Rules to the proposed transactions would be in the public interest since (a) it will continue to market, brand, and bill its services as it has been doing, (b) there will be no change to its rates, terms and conditions of service, (c) there are other COPT providers who seek to serve confinement facilities, usually through participation in competitive bids sought by facility administrators; (d) the grant of the waiver would not impair the authority of the Commission to assess and approve the contemplated secured guarantee of ESI's assets under A.R.S. §40-285; and (e) the grant of the waiver would not affect the Commission's jurisdiction over ESI as a public service corporation. If no waiver is granted, ESI asks for approval under the Affiliated Interest Rules.

The Applicant provided information addressing the Affiliated Interest Rule requirements, A.A.C. R14-2-803 (A) items 1 through 11. While Staff will not repeat all of ESI's responses, the most significant information contained in its responses is as follows:

- ESI states that the business purposes for establishing or reorganizing the holding company is to help STI to acquire indirect controlling interest in ESI and its affiliates;

- ESI states that the proposed method of financing the holding company and the resultant capital structure is that STI will finance the transaction through its issuance as borrower of: (a) up to $154 million in senior notes ("Senior Notes") and (b) up to an additional $40 million in senior subordinated notes ("Senior Subordinated Notes"). The proposed method of financing is discussed further in the next section;

- There will be no changes in the rates, terms and conditions of service provided by ESI as a result of the parent-level transfer of control. The cost of capital for ESI is expected to be comparable to current levels;

- ESI also states that the financial strength and other resources of STI and HIG will position ESI to have access to adequate capital for the current and expected future service needs of its customers. STI at this point has no specific plan for investment of specific amounts in ESI; and

- ESI also states that the contemplated transaction will eliminate all of ESI's issued debt. It will become guarantor of debt issued by STI. STI, which is investing substantial assets to acquire an indirect controlling interest in ESI, is committed to invest the sums necessary for ESI to maintain and enhance its level of services in the State of Arizona. The $30 million Credit Facility would be available for that purpose.

ARS § 40-285

As part of its Application, ESI stated that STI expects to finance the parent–level transaction through debt financing obtained by STI as issuer/borrower, with ESI and the other subsidiaries of STI providing both secured and unsecured guarantees of the debt issued by STI.

ESI points out that in Decision No. 66639, dated December 18, 2003, and Decision No. 66942, dated April 21. 2004, this Commission approved ESI's borrowing of up to $59.5 million through secured credit facilities from General Electric Capital Corporation and a number of other lenders. The debt was in the form of a $25.5 million revolving credit agreement and $34 million in term loans. The debt was secured by ESI's assets and stock. In addition, ESI's immediate parent, EI and certain other affiliates of ESI were guarantors of that debt. This financing package, according to ESI, repaid and replaced similarly-structured credit facilities of up to $72.5 million that the Commission had previously-approved in Decision No. 64741 dated April 17, 2002.

ESI states that the current $25.5 million revolving credit facility will be replaced with a comparable $30.0 million syndicated revolving credit facility incurred by STI guaranteed by ESI (among others) and again secured, in part, by ESI's assets and stock (the "Credit Facility"). The final maturity date of the Credit Facility will be July 31, 2009. In its Amendment to its Application, ESI states that the final maturity date of the Credit Facility has been amended to September 2009. ESI states that the proceeds of the Credit Facility will be used for ongoing working capital needs of STI and its subsidiaries, and for general corporate purposes, which would include the funding of ESI's ongoing operations in Arizona and 43 other jurisdictions, as was the prior revolving credit facility. ESI also states that the interest terms under this replacement facility are comparable to those most-recently approved by the Commission in Decision No. 66639 dated December 18, 2003, and Decision No. 66942 issued April 21, 2004.

ESI also states that it will be a secured guarantor of up to $154 million in senior notes to be issued by STI, in connection with STI's acquisition of all of the stock of EHI ("Senior Notes"). ESI also states that the Senior Notes will also be guaranteed, on a similar basis, by Evercom, EHI and the other affiliates of ESI, including other subsidiaries of STI. The guarantees of STI's Senior Notes will be secured by the assets (including any stock) owned by the guarantors, although the security interest of the holders of the Senior Notes in the collateral will be second in priority to the security interest granted to the lenders under the Credit Facility. Finally, STI will issue an additional $40 million in senior subordinated notes ("Senior Subordinated Notes"), for which ESI, Evercom, EHI and the other affiliates of ESI, including other subsidiaries of STI, will provide unsecured guarantees on a senior subordinated basis. The proceeds of these guaranteed debt obligations of STI will be used to repay the previously-approved ESI debt obligations in the amount of $40 million, pay the purchase price of the EHI stock in the amount of approximately $87 million, with the balance to be used for working capital in support of ESI's operations and STI's other inmate telecommunications operation through its other subsidiary, T-NETIX, Inc.

ESI seeks Commission approval of the secured guarantee since all of ESI's current debt obligations, approximately $40 million, will be repaid and the facilities terminated. ESI states that in addition ESI will provide secured guarantees with respect to debt, however similar guarantees are being provided by all of the other affiliates of ESI, including other subsidiaries of STI. ESI also states that the financial strength and other resources of STI and HIG will position ESI to have access to adequate capital for the current and expected future needs of its customers.

Discussion and Staff Recommendations

Under A.A.C. R14-2-804 (C) the Commission will review the transactions to determine if they would impair the financial status of the public utility, otherwise prevent it from attracting capital at fair and reasonable terms, or impair the ability of the public utility to provide safe, reasonable and adequate service.

A.R.S. §40-285 (A) requires Commission approval for any encumbrances of a public services corporation's assets that are necessary or useful in the performance of its duties to the public.

Staff recommends approval of the indirect merger at the parent level of ESI under A.A.C. R14-2-801 et seq. and guarantee by ESI of STI's notes and credit facility. Staff believes, based upon ESI's representations, that the transaction will not impair the financial status of the public utility, prevent it from attracting capital at fair and reasonable terms, or impair the ability of the public utility to provide safe, reasonable and adequate service. As ESI states, the financial strength and other resources of STI and HIG will position ESI to have access to adequate capital for the current and expected future needs of its customers. ESI further states that its cost of capital is expected to be comparable to current levels. Finally, the funds are to be used in part for working capital in support of ESI's operations.

Staff also recommends approval of the encumbrance of ESI's assets under A.R.S. §40-285 since this will enable ESI to eliminate all of its direct debt and have access to the financial resources of its parent company and is in the public interest.

Item 9 of A.A.C. R14-2-803 (A) requires ESI to file copies of all relevant documents and filings with the United States Securities and Exchange Commission and other federal and state agencies pertaining to the proposed transactions with the Commission. Staff believes the filing of copies of these documents should be a condition of approval. This information should be provided to the Commission within 90 days from the effective date of the Order of this matter.

for Ernest G. Johnson
Director
Utilities Division

EGJ:JFB:rdp/MAS

ORIGINATOR: John F. Bostwick

BEFORE THE ARIZONA CORPORATION COMMISSION

MARC SPITZER
Chairman
WILLIAM A. MUNDELL
Commissioner
JEFF HATCH-MILLER
Commissioner
MIKE GLEASON
Commissioner
KRISTIN K. MAYES
Commissioner

IN THE MATTER OF THE APPLICATION OF EVERCOM SYSTEMS, INC. IN CONNECTION WITH AN INDIRECT TRANSFER OF CONTROL AND THE PROVISION OF CERTAIN SECURE AND UNSECURED GUARANTEES	DOCKET NO. T-03479A-04-0549 DECISION NO. ________ <u>ORDER</u>

Open Meeting
October 26 and 27, 2004
Phoenix, Arizona

BY THE COMMISSION:

INTRODUCTION

On July 29, 2004, Evercom Systems, Inc. ("ESI" and "Applicant"), pursuant to the Public Utility Holding Companies and Affiliated Interest Rules of the Arizona Administrative Code ("A.A.C.") R14-2-801 et seq. ("Affiliated Interest Rules") and Arizona Revised Statutes ("A.R.S.") §40-285, requested that the Commission: (a) expeditiously waive the application of the Affiliated Interests Rules concerning its indirect transfer of control and guarantees or (b) in the alternative, expeditiously approve those transactions under the Affiliated Interests Rules without a hearing. ESI further requests, pursuant to A.R.S. §40-285, that the Commission approve ESI's request to encumber its assets in Arizona pursuant to the secured guarantee described in its Application. On August 27, 2004, ESI filed an amendment to its initial Application to reflect certain changes in the facts that occurred since the time it filed its original Application.

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FINDINGS OF FACT

1. ESI, the Applicant, was certificated to provide Customer Owned Pay Telephone ("COPT") services in Arizona in Decision No. 60924. On May 22, 1998, in Decision No. 60924, the Commission granted to Talton Invision, Inc. a Certificate of Convenience and Necessity authorizing it to provide COPT services throughout Arizona. On January 25, 1999, Talton Invision, Inc. changed it name to ESI.

2. In its Application, ESI states that it provides inmate telecommunications services in Arizona and forty-three other jurisdictions, offering local, intrastate, interstate and international calling services to inmates in more than 2000 correctional facilities nationwide.

3. ESI further stated that it is a privately held company incorporated under the laws of the State of Delaware and that its principal offices are located in Irving, Texas. It further stated that it is a wholly owned subsidiary of Evercom, Inc. ("EI"), a Delaware corporation which is in turn a wholly owned subsidiary of Evercom Holdings, Inc. ("EHI").

In its initial Application and the Amendment to its Application, ESI provided the following information relating to the indirect parent level transfer of control and encumbrance of its assets for which it requests Commission approval:

Proposed Merger Transaction

4. EHI entered into a merger agreement, dated July 10, 2004, with (a) TZ Holdings, Inc. ("TZ"), a State of Delaware corporation, and (b) New Mustang Acquisition, Inc. ("Mustang"), another State of Delaware corporation which is a wholly-owned subsidiary of TZ. Upon completion of the proposed transaction EHI will be a wholly-owned subsidiary of TZ. In its Amendment to its Application, ESI stated that TZ had changed its corporate name to Securus Technologies, Inc. ("STI").

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5. ESI further stated that TZ (hereinafter called STI) is majority-owned by H.I.G.-TNetix, Inc., an affiliate of H.I.G. Capital, LLC ("HIG"), a Miami-based private equity firm, which has over $1 billion under management. ESI further stated that Investors in HIG-managed funds include leading financial institutions, insurance companies, pension funds and university endowments. According to ESI, STI has no other operational purpose other than to hold ownership interests in various enterprises in which HIG has invested.

6. ESI states that STI formed Mustang for the sole purpose of effecting the proposed merger and upon the merger's completion; Mustang will be merged out of existence. The merger will be accomplished through Mustang's merger into EHI. As part of the merger of EHI into Mustang, all of the current stock and stock options of EHI shall be converted or retired. The retirement will be accomplished through STI's purchase of EHI stock or options from the current shareholders; and the former EHI treasury stock will be retired. ESI further explained that simultaneous with the closing of the merger, certain former stockholders of EHI will acquire certain stock of STI in an aggregate amount so that the ratio of STI common stock owned by HIG (or its affiliates) to STI common stock owned by the former EHI stockholders is not greater than 65:35 immediately after giving effect to the merger.

7. Organization charts depicting all the affiliates and their relationships with the holding company relating to the proposed indirect transfer of control of ESI are shown in Attachment A, Attachment B, and Attachment C. The following describes the activities and transactions of each affiliate involved in the proposed transfer as represented by the various Attachments:

a) The current ownership structure of ESI and affiliates is shown on Attachment A;

b) Attachment B shows the pre-merger ownership structure. STI is the parent company of Mustang. EHI, the indirect parent of ESI, and its subsidiaries will merge into Mustang as stated in the initial Application; and

c) Attachment C, which indicates the post-merger subsidiaries structure, shows that Mustang will be replaced by EHI and its subsidiaries.

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8. ESI further states that upon completion of the merger, the current existing, inter-corporate relationships between ESI, EI and EHI shall remain totally unchanged. ESI's immediate parent (and its parent's parent) will remain the same. However, EHI will become a wholly-owned subsidiary of STI, which will be majority owned by H.I.G-TNetrix, Inc., an affiliate of HIG, the Miami-based private equity firm.

9. ESI states that it will remain a separately certificated entity providing the services it currently offers. The transaction will be transparent to the customers of ESI. ESI states that there will be no immediate changes in the terms and conditions of the services provided by ESI, pursuant to the applicable tariffs or price lists that ESI currently has on file as approved by the Commission. ESI will continue to market, brand and bill its services as it has done in the past. There are no current plans to change the management structure of ESI.

10. Based on the data requests sent to the Applicant, Staff obtained the following additional information:

- ESI currently has contracts with 10 confinement facilities in Arizona to provide telecommunications services to inmates (Based on ESI's 2003 Utility Annual Report for Customer Owned Pay Telephone Provider, ESI currently provides pay telephone service to 11 confinement locations in Arizona);
- The post-merger ownership of STI is as follows: H.I.G.-TNetix, Inc, will own 59 percent and other minority stockholders, including former stockholders of EHI, will own 41 percent. The largest single minority stockholder is Alexander Enterprise Holdings Corp., a private investment partnership based in Miami, Florida, will own about 10 percent of STI. Among the remaining stockholders, no individual stockholder will directly hold more than 5 percent of STI; and
- ESI's current value of depreciated assets used to provide telecommunications services in Arizona is approximately $100,000.

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11. As part of its request for waiver of the Affiliated Interest rules, ESI states that it has a very modest presence in the State of Arizona. Approximately one percent of its assets are located in Arizona and its Arizona intrastate revenues are less than five percent of its total revenues in 2003.

Affiliated Interest Rules

12. ESI is a Class A utility that is subject to A.A.C. R14-2-801 et seq., the Affiliated Interests Rules. Staff reviewed the Applicant's 2003 annual report filed with the Commission to determine the applicability of ESI as a Class A investor owned utility. A telecommunications carrier that has Arizona jurisdictional revenues of more than $1 million is considered to be a Class A utility. ESI, an investor-owned utility, generated more than $1 million of Arizona revenue in 2003.

13. ESI believes that a waiver of the application of the Affiliated Interests Rules to the proposed transactions would be in the public interest since (a) it will continue to market, brand, and bill its services as it has been doing, (b) there will be no change to its rates, terms and conditions of service, (c) there are other COPT providers who seek to serve confinement facilities, usually through participation in competitive bids sought by facility administrators; (d) the grant of the waiver would not impair the authority of the Commission to assess and approve the contemplated secured guarantee of ESI's assets under A.R.S. §40-285; and (e) the grant of the waiver would not affect the Commission's jurisdiction over ESI as a public service corporation. If no waiver is granted, ESI asks for approval under the Affiliated Interest Rules.

14. The Applicant provided information addressing the Affiliated Interest Rule requirements, A.A.C. R14-2-803 (A) items 1 through 11. While Staff will not repeat all of ESI's responses, the most significant information contained in its responses is as follows:

- ESI states that the business purposes for establishing or reorganizing the holding company is to help STI to acquire indirect controlling interest in ESI and its affiliates;
- ESI states that the proposed method of financing the holding company and the resultant capital structure is that STI will finance the transaction through its

issuance as borrower of: (a) up to $154 million in senior notes ("Senior Notes") and (b) up to an additional $40 million in senior subordinated notes ("Senior Subordinated Notes"). The proposed method of financing is discussed further in the next section;

- There will be no changes in the rates, terms and conditions of service provided by ESI as a result of the parent-level transfer of control. The cost of capital for ESI is expected to be comparable to current levels;
- ESI also states that the financial strength and other resources of STI and HIG will position ESI to have access to adequate capital for the current and expected future service needs of its customers. STI at this point has no specific plan for investment of specific amounts in ESI; and
- ESI also states that the contemplated transaction will eliminate all of ESI's issued debt. It will become guarantor of debt issued by STI. STI, which is investing substantial assets to acquire an indirect controlling interest in ESI, is committed to invest the sums necessary for ESI to maintain and enhance its level of services in the State of Arizona. The $30 million Credit Facility would be available for that purpose.

A.R.S. § 40-285

15. As part of its Application, ESI asks for approval under A.R.S. Section 40-285 to encumber its assets. ESI states that STI expects to finance the parent–level transaction through debt financing obtained by STI as issuer/borrower, with ESI and the other subsidiaries of STI providing both secured and unsecured guarantees of the debt issued by STI.

16. ESI points out that in Decision No. 66639, dated December 18, 2003, and Decision No. 66942, dated April 21. 2004, this Commission approved ESI's borrowing of up to $59.5 million through secured credit facilities from General Electric Capital Corporation and a number of other lenders. The debt was in the form of a $25.5 million revolving credit agreement and $34 million in term loans. The debt was secured by ESI's assets and stock. In addition, ESI's immediate parent, EI and certain other affiliates of ESI were guarantors of that debt. This

financing package, according to ESI, repaid and replaced similarly-structured credit facilities of up to $72.5 million that the Commission had previously-approved in Decision No. 64741 dated April 17, 2002.

17. ESI states that the current $25.5 million revolving credit facility will be replaced with a comparable $30.0 million syndicated revolving credit facility incurred by STI guaranteed by ESI (among others) and again secured, in part, by ESI's assets and stock (the "Credit Facility"). The final maturity date of the Credit Facility will be July 31, 2009. In its Amendment to its Application, ESI states that the final maturity date of the Credit Facility has been amended to September 2009. ESI states that the proceeds of the Credit Facility will be used for ongoing working capital needs of STI and its subsidiaries, and for general corporate purposes, which would include the funding of ESI's ongoing operations in Arizona and 43 other jurisdictions, as was the prior revolving credit facility. ESI also states that the interest terms under this replacement facility are comparable to those most-recently approved by the Commission in Decision No. 66639 dated December 18, 2003, and Decision No. 66942 issued April 21, 2004.

18. ESI also states that it will be a secured guarantor of up to $154 million in senior notes to be issued by STI, in connection with STI's acquisition of all of the stock of EHI ("Senior Notes"). ESI also states that the Senior Notes will also be guaranteed, on a similar basis, by Evercom, EHI and the other affiliates of ESI, including other subsidiaries of STI. The guarantees of STI's Senior Notes will be secured by the assets (including any stock) owned by the guarantors, although the security interest of the holders of the Senior Notes in the collateral will be second in priority to the security interest granted to the lenders under the Credit Facility. Finally, STI will issue an additional $40 million in senior subordinated notes ("Senior Subordinated Notes"), for which ESI, Evercom, EHI and the other affiliates of ESI, including other subsidiaries of STI, will provide unsecured guarantees on a senior subordinated basis. The proceeds of these guaranteed debt obligations of STI will be used to repay the previously-approved ESI debt obligations in the amount of $40 million, pay the purchase price of the EHI stock in the amount of approximately $87 million, with the balance to be used for working capital in support of ESI's operations and STI's other inmate telecommunications operation through its other subsidiary, T-NETIX, Inc.

19. ESI seeks Commission approval of the secured guarantee since all of ESI's current debt obligations, approximately $40 million, will be repaid and the facilities terminated. ESI states that in addition ESI will provide secured guarantees with respect to debt, however similar guarantees are being provided by all of the other affiliates of ESI, including other subsidiaries of STI. ESI also states that the financial strength and other resources of STI and HIG will position ESI to have access to adequate capital for the current and expected future needs of its customers.

Discussion and Staff Recommendations

20. Under A.A.C. R14-2-804 (C) the Commission will review the transactions to determine if they would impair the financial status of the public utility, otherwise prevent it from attracting capital at fair and reasonable terms, or impair the ability of the public utility to provide safe, reasonable and adequate service.

21. A.R.S. §40-285 (A) requires Commission approval for any encumbrance of a public service corporation's assets that are necessary or useful in the performance of its duties to the public.

22. Staff recommends approval of the indirect merger at the parent level of ESI under A.C.C. R14-2-801 et seq. and guarantee by ESI of STI's notes and credit facility. Staff believes, based upon ESI's representations, that the transaction will not impair the financial status of the public utility, prevent it from attracting capital at fair and reasonable terms, or impair the ability of the public utility to provide safe, reasonable and adequate service. As ESI states, the financial strength and other resources of STI and HIG will position ESI to have access to adequate capital for the current and expected future needs of its customers. ESI further states that its cost of capital is expected to be comparable to current levels. Finally, the funds are to be used in part for working capital in support of ESI's operations.

23. Staff also recommends approval of the encumbrance of ESI's assets under A.R.S. §40-285 since this will enable ESI to eliminate all of its direct debt and have access to the financial resources of its parent company and is in the public interest.

24. Item 9 of A.A.C. R14-2-803 (A) requires ESI to file copies of all relevant documents and filings with the United States Securities and Exchange Commission and other

federal and state agencies pertaining to the proposed transactions with the Commission. Staff believes the filing of copies of these documents should be a condition of approval. This information should be docketed within 90 days from the effective date of the Order of this matter.

CONCLUSIONS OF LAW

1. ESI is an Arizona public service corporation within the meaning of Article XV, Section 2, of the Arizona Constitution and A.R.S. §40-285.

2. The Commission has jurisdiction over ESI and the subject matter in this proceeding.

3. The Commission, having reviewed the filing and Staff's Memorandum dated, October 15, 2004, concludes that ESI has provided appropriate notice of its intend to organize a public utility holding as defined in the Affiliated Interests Rules A.A.C. R14-2-801 and A.A.C. R14-2-802. In addition, ESI has furnished information required in A.A.C. R14-2-803 (A) items 1 through 11, except item 9.

4. Staff's findings and recommendation, as set forth in Findings of Fact Nos. 22, 23 and 24 above, are reasonable and should be adopted by the Commission.

ORDER

IT IS THEREFORE ORDERED that, pursuant to A.R.S. §40-285 and A.A.C. R14-2-801 et. seq, ESI's Application for encumbrance of its Arizona assets is granted.

IT IS FURTHER ORDERED that ESI's Application for indirect transfer of control at the parent level under the Affiliated Interest Rules is granted subject Finding of Fact 24 above.

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IT IS FURTHER ORDERED that if the Applicant fails to docket proof that copies of all relevant documents and filings with the United States Securities and Exchange Commission and other federal and state agencies pertaining to the proposed transactions with the Commission within 90 days from the effective date of the Order of this matter the indirect transfer and control of ESI and related transactions shall be denied.

IT IS FURTHER ORDERED that this Order shall be effective immediately.

BY ORDER OF THE ARIZONA CORPORATION COMMISSION

CHAIRMAN COMMISSIONER COMMISSIONER

COMMISSIONER COMMISSIONER

IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive Secretary of the Arizona Corporation Commission, have hereunto, set my hand and caused the official seal of this Commission to be affixed at the Capitol, in the City of Phoenix, this _______ day of _________________2004.

BRIAN C. McNEIL
Executive Secretary

DISSENT:______________________

EGJ:JFB:rdp/MAS

SERVICE LIST FOR: EVERCOM SYSTEMS, INC.
DOCKET NO. T-03479A-04-0549

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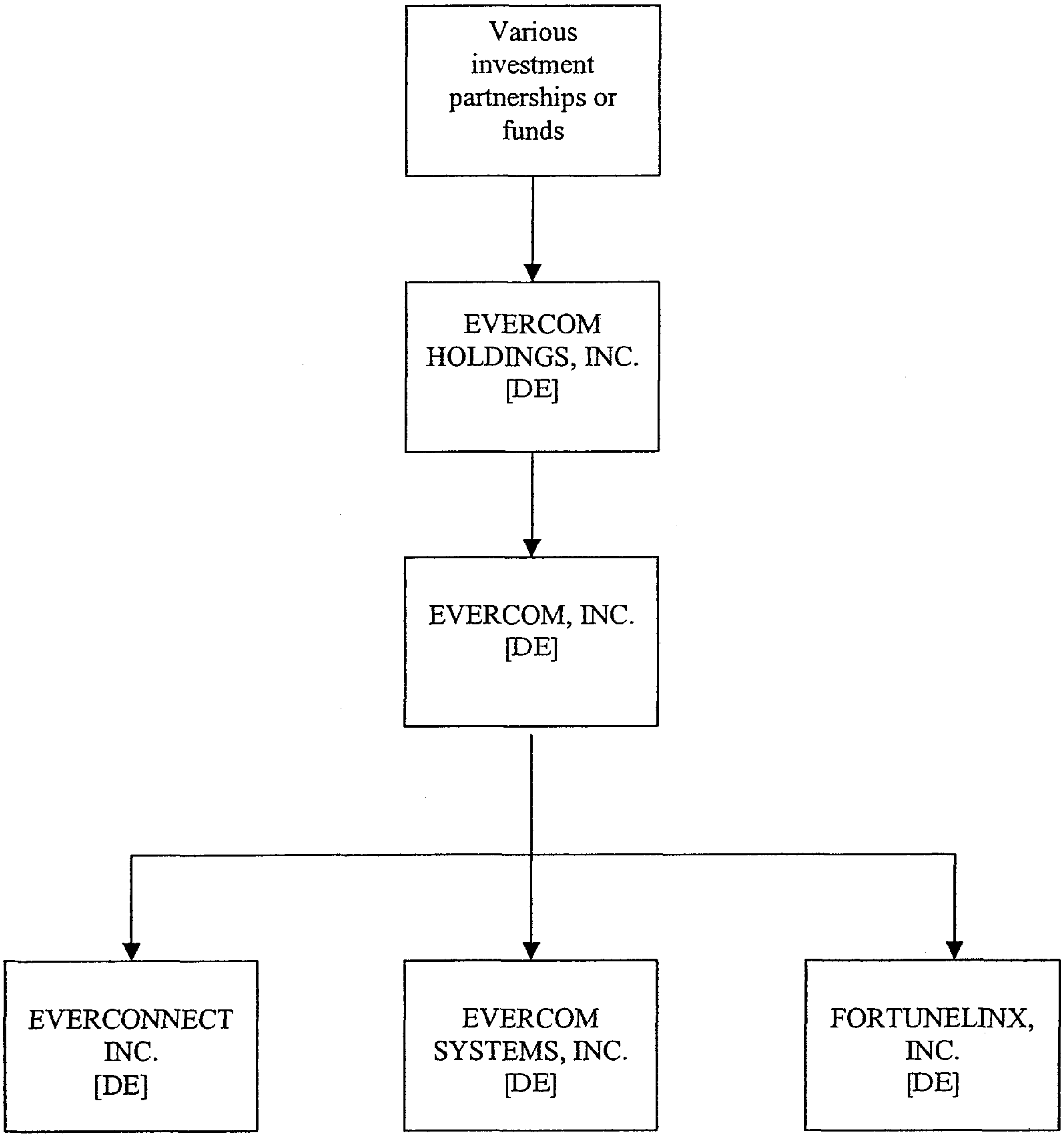
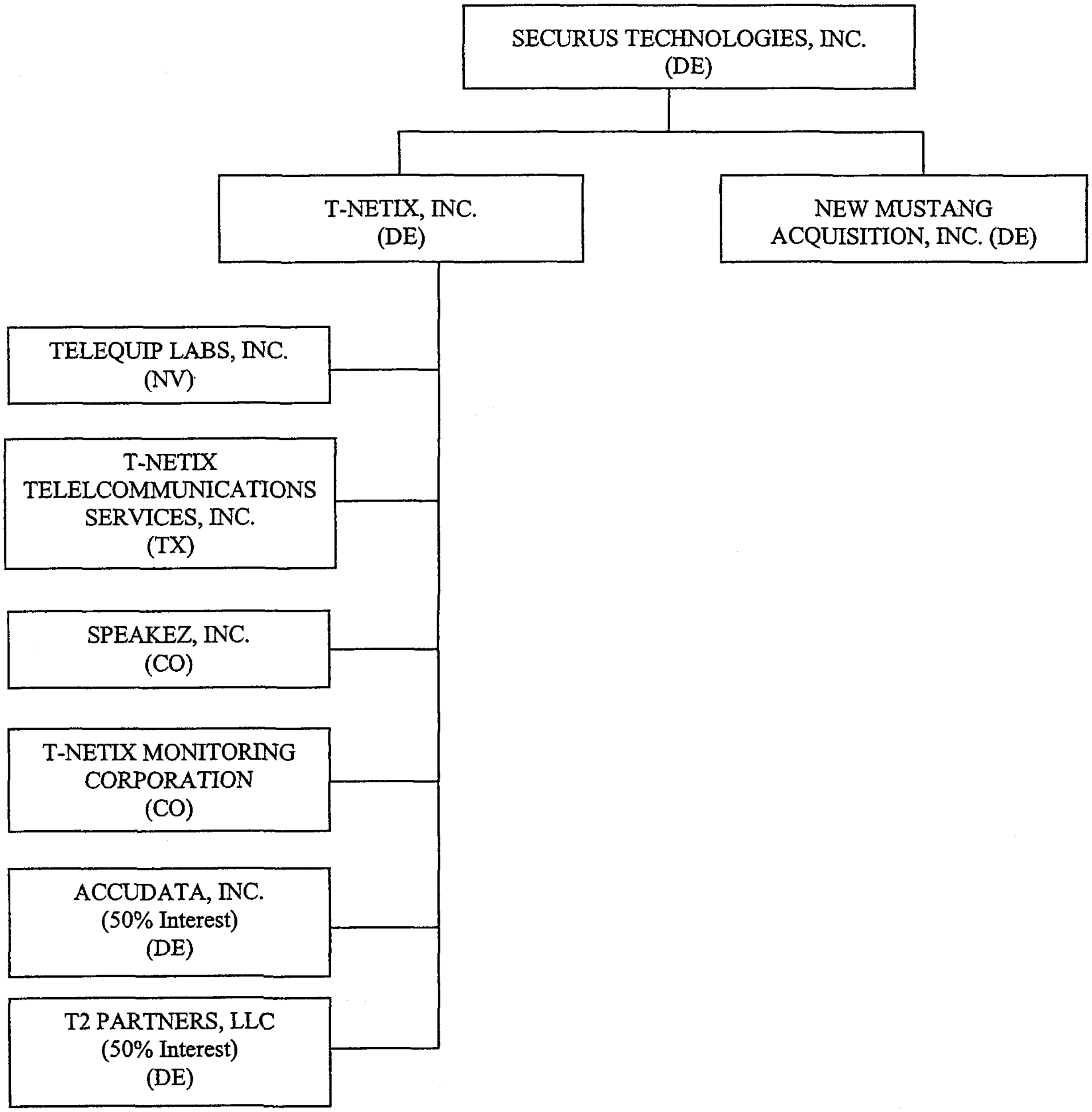
ATTACHMENT A

Current Ownership Structure



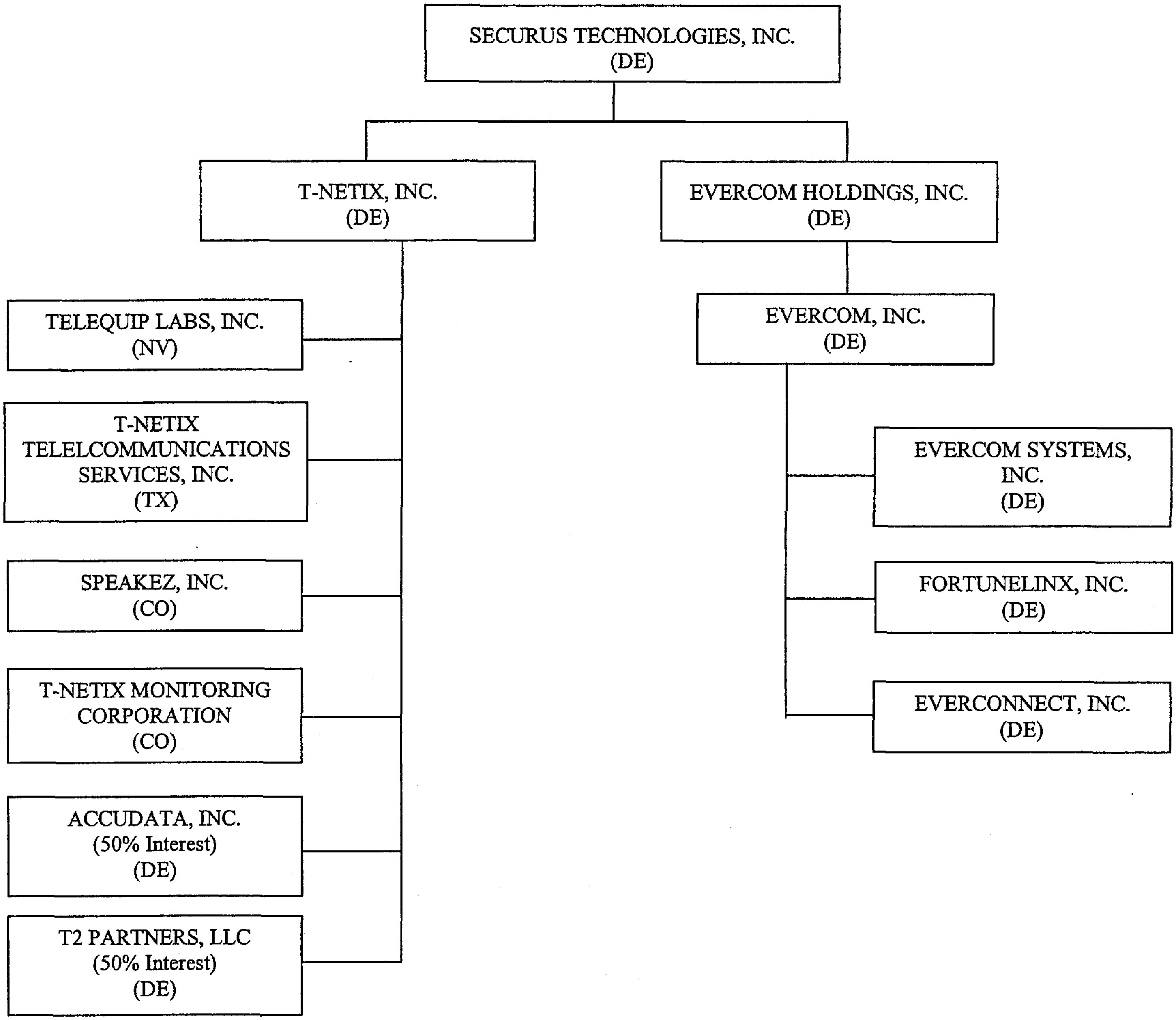
ATTACHMENT B

SECURUS TECHNOLOGIES, INC. – PRE-MERGER SUBSIDIARIES STRUCTURE



ATTACHMENT C

SECURUS TECHNOLOGIES, INC. – POST MERGER SUBSIDIARIES STRUCTURE



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