

**ORIGINAL NEW APPLICATION**



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BEFORE THE ARIZONA CORPORATION COMMISSION

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**COMMISSIONERS**

JEFF HATCH-MILLER – Chairman  
WILLIAM A. MUNDELL  
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KRISTIN K. MAYES  
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AZ CORP COMMISSION  
DOCUMENT CONTROL

T-03267A-06-0622

Arizona Corporation Commission

**DOCKETED**

SEP 28 2006

DOCKETED BY *[Signature]* *[Signature]*

IN THE MATTER OF THE APPLICATION OF )  
MCLEODUSA TELECOMMUNICATIONS )  
SERVICES, INC. FOR APPROVAL TO )  
PARTICIPATE IN CERTAIN FINANCING )  
ARRANGEMENTS. )  
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DOCKET NO. T-03276A-06-\_\_\_\_\_  
  
**APPLICATION**

**I. INTRODUCTION**

McLeodUSA Telecommunications Services, Inc. (“MTSI” or “Applicant”), by its undersigned counsel and pursuant to Section 40-285 of the Arizona Revised Statutes and R14-2-804.B.1 of the Arizona Administrative Code and any other provision of the Code or regulations deemed applicable, requests approval, to the extent that such is necessary<sup>1</sup>, from the Arizona Corporation Commission (“Commission”) to participate in certain financing arrangements described more fully in Section IV of this Petition. Specifically, MTSI seeks approval for both its guarantee and pledge of its assets as security for senior second secured notes issued by its parent, McLeodUSA Incorporated (“McLeodUSA” or “Parent” or “Issuer”) in a private offering, and to participate in certain other financing activities as described below.

In support of this Application, the Applicant states as follows:

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<sup>1</sup> Although Petitioners are seeking any necessary approval for their participation in these financing arrangements, Petitioners are doing so without prejudice to their right to assert that this transaction is beyond the jurisdiction of the state commissions.

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1     **II.     THE PARTIES**

2             **A.     McLeodUSA Telecommunications Services, Inc. ("MTSI")**

3             MTSI is an Iowa corporation with principal offices located at One Martha's Way,  
4     Hiawatha, Iowa 52233 (319) 790-7800. MTSI provides integrated communications services,  
5     including local services, in 25 states in the Midwest, Southwest, Northwest, and Rocky Mountain  
6     regions. MTSI is a wholly owned subsidiary of McLeodUSA Holdings, Inc. which, in turn, is a  
7     wholly owned subsidiary of Parent.

8             In Arizona, MTSI is authorized to provide (1) resold and facilities-based local exchange  
9     and exchange access service pursuant to Decision No. 62627 issued by the Commission in Docket  
10    No. T-03267A-99-0705 on June 9, 2000 and (2) resold interexchange telecommunications services  
11    pursuant to Decision No. 68001 issued by the Commission in Docket No. T-03267A-96-0515 on  
12    July 17, 1998.

13            Further information concerning MTSI's legal, technical, managerial and financial  
14    qualifications to provide service was submitted with its applications for certification and  
15    subsequent filings with the Commission as noted above and is, therefore, a matter of public record.  
16    MTSI respectfully requests that the Commission take official notice of that information and  
17    incorporate it herein by reference.

18     **III.    DESIGNATED CONTACTS**

19            Inquiries or copies of any correspondence, orders, or other materials pertaining to this  
20    Application should be directed to:

21                             Michael W. Patten, Esq.  
22                             Roshka DeWulf & Patten, PLC  
23                             One Arizona Center  
24                             400 East Van Buren, Suite 800  
25                             Phoenix, Arizona 85004-3906  
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                              and

1 Jean L. Kiddoo  
2 Brett P. Ferenchak  
3 Bingham McCutchen LLP  
4 3000 K Street, NW, Suite 300  
5 Washington, DC 20007  
6 Tel: (202) 424-7500  
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8 Email: jean.kiddoo@bingham.com  
9 brett.ferenchak@bingham.com

6 William A. Haas, Esq.  
7 Vice President and Deputy General Counsel  
8 McLeodUSA Incorporated  
9 One Martha's Way  
10 Hiawatha, Iowa 52233  
11 Tel: (319) 790-7295  
12 Fax: (319) 790-7901  
13 Email: whaas@mcleodusa.com

10 **IV. REQUEST FOR APPROVAL TO PARTICIPATE IN CERTAIN FINANCING**  
11 **ARRANGEMENTS**

12 On September 28, 2006, MTSI's parent, McLeodUSA, issued approximately \$120 million  
13 in 10 ½% Senior Second Secured Notes due 2011 in a private offering (the "Notes"). As is typical  
14 in these types of transactions, Parent has agreed that it will initiate an offer to exchange the Notes  
15 for substantially identical notes ("Exchange Notes") registered under federal securities laws within  
16 a set period of time, in this case 180 days.<sup>2</sup> Each of Parent's subsidiaries other than MTSI has  
17 guaranteed the Notes and pledged all of their assets (subject to certain exceptions) as security for  
18 its obligations under the guarantee, and have agreed to do likewise with respect to the Exchange  
19 Notes. The indenture governing the Notes and the Exchange Notes permit McLeodUSA and its  
20 subsidiaries to, subject to certain requirements, incur additional indebtedness ("Permitted  
21 Indebtedness") and grant additional liens ("Permitted Liens") on its and its subsidiaries assets,  
22 including incurring up to \$26 million aggregate principal amount of indebtedness secured by liens  
23 that would be senior to the Notes and Exchange Notes.<sup>3</sup>

25 <sup>2</sup> In certain exceptional circumstances applicable to certain potential noteholders, the  
26 exchange notes may not in fact be registered. As used in this Application, the term "Exchange Notes"  
refers to all exchange notes whether or not registered under federal securities laws.

27 <sup>3</sup> Issuers of notes such as the Notes often have first priority senior indebtedness (such as  
revolving credit facilities) outstanding at the time the notes are issued. In McLeodUSA's case, the  
proceeds of the Notes are being used in part to eliminate McLeodUSA's existing senior secured credit

1 As required by the indenture governing the Notes, MTSI seeks approval, to the extent  
2 necessary, from the Commission to issue guarantees of the Notes, the Exchange Notes, and  
3 Permitted Indebtedness and to pledge its assets as security for its obligations pursuant to its  
4 guarantees, the Notes, the Exchange Notes, and Permitted Indebtedness. McLeodUSA also  
5 requests authority to incur or guarantee any Permitted Indebtedness (and grant Permitted Liens) to  
6 the extent authorized by the terms of the indenture governing the Notes and the Exchange Notes,  
7 as applicable.

8 The proceeds of the Notes have been used to pay off all outstanding amounts under the exit  
9 financing that was entered in the context of Applicant's Chapter 11 proceedings. The Commission  
10 approved the exit financing in Decision No. 68324 (December 9, 2005) from Docket No. T-  
11 03267A-05-0731. The proceeds have also served to cash collateralize existing letters of credit  
12 issued on behalf of McLeodUSA and its subsidiaries (including MTSI), and to pay fees and  
13 expenses associated with the offering. The remainder of the proceeds will be used for general  
14 corporate purposes. Applicant emphasizes that participation in the financing arrangements will  
15 not result in a change in MTSI's management or in its day-to-day operations in Arizona; nor will it  
16 adversely affect Applicant's current or proposed operations in Arizona. MTSI will still provide  
17 resold and facilities-based local exchange and exchange access service, as well as resold  
18 interexchange telecommunications in Arizona. Securing the debt will not require MTSI to  
19 increase either its current rates or its maximum rates. The arrangement also will not effect the  
20 \$600,000 performance bond currently in place with respect to MTSI's Arizona operations.  
21 Accordingly, and to the extent required, Applicant respectfully requests that the Commission  
22 approve the participation of MTSI in the financial arrangements described herein.

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27 facility. Therefore the indenture governing the Notes allows McLeodUSA to enter into a new facility(ies)  
in the future to which the Notes will be contractually subordinated (obligations under such facilities being  
defined as "First Lien Obligations" in the indenture governing the Notes).

1 **V. PUBLIC INTEREST CONSIDERATIONS**

2 Approval of the proposed financial arrangement described herein will serve the public  
3 interest in promoting competition among telecommunications carriers by providing MTSI with the  
4 opportunity to strengthen its competitive position through access to greater financial resources.  
5 MTSI will be better positioned to utilize available funds so that it can provide competitive services  
6 to benefit Arizona consumers more quickly and efficiently. Furthermore, by increasing the breadth  
7 and scope of telecommunications services made available through an increased ability to support  
8 existing operations and expand MTSI's operations, greater access to capital will also strengthen  
9 Applicant's ability to bring competitive telecommunications services to consumers in the State of  
10 Arizona. This financing transaction will be transparent to consumers and will not affect the rates  
11 of MTSI's services. In addition, consumers will benefit from the continued receipt of quality  
12 telecommunications services that are priced competitively.

13 MTSI competes in Arizona and other markets with numerous other carriers and enhanced  
14 service providers as well as the incumbent local exchange carrier and other competitive local  
15 exchange carriers. MTSI is also a non-dominant carrier and is not subject to rate of return  
16 regulation. In addition, because of the highly competitive environment in which both companies  
17 operate, the rates charged customers are subject to market discipline and the services offered  
18 generally are available from numerous other carriers. As a result, the source of funds and capital  
19 structure of MTSI has little effect on customers in Arizona or elsewhere. In the unlikely event that  
20 the capital structure for MTSI becomes too costly and rates rise, customers can migrate to other  
21 carriers. Thus, any adverse consequences from the financing decisions impact shareholders, not  
22 customers, and any favorable consequences benefit both its shareholders and consumers through  
23 higher profits, lower rates, and better service and services.

24 Moreover, because the public interest is best served with the presence of numerous  
25 telecommunications competitors in Arizona, providing competitors ample flexibility to arrange  
26 financing so that they can carry on business is vital – so long as there is no adverse public impact.  
27 But to deny this flexibility will discourage new competitors from competing in Arizona, and will

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1 entice existing competitors to seek a more favorable regulatory environment elsewhere. Neither of  
2 the outcomes mentioned above will enhance the public interest. Given the challenges facing  
3 telecommunications carriers, ensuring that funds are available to MTSI in this manner benefits  
4 Arizona consumers.

5 Finally, these financing arrangements will be transparent to consumers. Consumers will  
6 also benefit from the continued receipt of quality telecommunications services competitively  
7 priced in Arizona. These arrangements will not impair the MTSI's financial status, will not impair  
8 its ability to attract capital and it will not impair MTSI's ability to provide safe, reliable and  
9 adequate service.

10 **VI. CONCLUSION**

11 For the reasons stated above, Applicant submits that the public interest, convenience and  
12 necessity will be furthered by expeditious Commission approval of McLeodUSA  
13 Telecommunications Services, Inc.'s participation in the financing arrangements described herein.

14 RESPECTFULLY SUBMITTED this 28<sup>th</sup> day of September 2006.

15 ROSHKA DEWULF & PATTEN, PLC

16  
17  
18 By   
19 Michael W. Patten  
20 One Arizona Center  
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22 Phoenix, Arizona 85004

23 Counsel for McLeodUSA Telecommunications Services, Inc.

24 Jean L. Kiddoo  
25 Brett P. Ferenchak  
26 Bingham McCutchen LLP  
27 3000 K Street, N.W., Suite 300  
Washington, DC 20007

Of Counsel

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1 Original and 13 copies of the foregoing  
2 filed this 28<sup>th</sup> day of September 2006 with:

3 Docket Control  
4 Arizona Corporation Commission  
5 1200 West Washington Street  
6 Phoenix, Arizona 85007

7 Copy of the foregoing hand-delivered/mailed  
8 this 28<sup>th</sup> day of September 2006 to:

9 Lyn Farmer, Esq.  
10 Chief Administrative Law Judge  
11 Hearing Division  
12 Arizona Corporation Commission  
13 1200 West Washington  
14 Phoenix, Arizona 85007

15 Christopher C. Kempley  
16 Chief Counsel, Legal Division  
17 Arizona Corporation Commission  
18 1200 West Washington  
19 Phoenix, Arizona 85007

20 Ernest G. Johnson, Esq.  
21 Director, Utilities Division  
22 Arizona Corporation Commission  
23 1200 West Washington  
24 Phoenix, Arizona 85007

25  
26  
27  
By 

# ATTACHMENT

"A"

VERIFICATION

STATE OF IOWA

§  
§  
§

COUNTY OF LINN

I, William A. Haas, state that I am Vice President and Deputy General Counsel of McLeodUSA Incorporated, the parent company of McLeodUSA Telecommunications Services, Inc.; that I am authorized to make this Verification on behalf of McLeodUSA Telecommunications Services, Inc.; that the foregoing Application was prepared under my direction and supervision; and that the statements in the foregoing Application are true and correct to the best of my knowledge, information, and belief.

William A. Haas

Name: Williams A. Haas  
Title: Vice President and Deputy General Counsel  
McLeodUSA Incorporated

SWORN TO AND SUBSCRIBED before me on the 25<sup>th</sup> day of September, 2006.



Lorilei Christner  
Notary Public

My commission expires: Sept 28, 2008