CINCINNATI BELL INC
Form 10-Q
August 07, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE TRANSITION PERIOD FROM ______ TO ______

COMMISSION FILE NUMBER: 1-8519

CINCINNATI BELL INC.

Ohio	**31-1056105**
(State of Incorporation)	**(I.R.S. Employer Identification No.)**

221 East Fourth Street, Cincinnati, Ohio 45202

(Address of principal executive offices) (Zip Code)

(513) 397-9900

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act:

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

At July 31, 2007, there were 248,106,340 common shares outstanding and 155,250 shares of 6 3/4% Cumulative Convertible Preferred Stock outstanding.

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CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Dollars in millions, except per share amounts)

(Unaudited)

	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Revenue				
Services	$ 288.7	$ 275.5	$ 570.6	$ 545.4
Products	40.4	47.8	73.8	76.2
Total revenue	329.1	323.3	644.4	621.6
Costs and expenses				
Cost of services, excluding depreciation	103.0	93.6	199.6	188.4
Cost of products sold, excluding depreciation	42.3	51.9	78.8	85.2
Selling, general and administrative	65.8	61.7	131.3	120.0
Depreciation	36.0	34.3	71.5	68.1
Amortization	0.8	1.4	1.7	2.0
Shareholder claim settlement				6.3
Gain on sale of broadband assets		(2.9)		(2.9)
Restructuring charges	0.1	0.1	2.6	0.2
Total operating costs and expenses	248.0	240.1	485.5	467.3
Operating income	81.1	83.2	158.9	154.3
Minority interest expense				0.4
Interest expense	39.0	40.3	79.1	79.8
Other income, net	(0.2)	(0.1)	(2.2)	(0.2)
Income before income taxes	42.3	43.0	82.0	74.3
Income tax expense	18.1	18.7	35.3	35.9
Net income	24.2	24.3	46.7	38.4
Preferred stock dividends	2.6	2.6	5.2	5.2
Net income applicable to common shareowners	$ 21.6	$ 21.7	$ 41.5	$ 33.2
Basic earnings per common share	$ 0.09	$ 0.09	$ 0.17	$ 0.13
Diluted earnings per common share	$ 0.08	$ 0.09	$ 0.16	$ 0.13
Weighted average common shares outstanding (in millions)				
Basic	247.3	246.8	247.2	246.7
Diluted	257.6	252.4	256.4	251.9

The accompanying notes are an integral part of the condensed consolidated financial statements.

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Form 10-Q Part I Cincinnati Bell Inc.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in millions, except share amounts)

(Unaudited)

	June 30, 2007	December 31, 2006
Assets		
Current assets		
Cash and cash equivalents	$ 26.7	$ 79.4
Receivables, less allowances of $15.7 and $15.2	155.9	161.9
Materials and supplies	29.5	24.9
Deferred income tax benefits, net	78.4	63.3
Prepaid expenses and other current assets	23.5	17.9
Total current assets	314.0	347.4
Property, plant and equipment, net	856.6	818.8
Goodwill	55.4	53.3
Intangible assets, net	113.2	112.9
Deferred income tax benefits, net	565.7	631.4
Other noncurrent assets	47.8	50.0
Total assets	$ 1,952.7	$ 2,013.8
Liabilities and Shareowners Deficit		
Current liabilities		
Current portion of long-term debt	$ 7.4	$ 7.3
Accounts payable	90.9	74.1
Unearned revenue and customer deposits	45.3	42.9
Accrued taxes	42.0	52.8
Accrued interest	50.4	52.1
Accrued payroll and benefits	39.0	43.8
Other current liabilities	40.9	45.9
Total current liabilities	315.9	318.9
Long-term debt, less current portion	1,956.7	2,065.9
Accrued pension and postretirement benefits	362.6	359.6
Other noncurrent liabilities	61.5	61.0
Total liabilities	2,696.7	2,805.4
Shareowners deficit		
Preferred stock, 2,357,299 shares authorized, 155,250 shares (3,105,000 depositary shares) of 6 3/4% Cumulative Convertible Preferred Stock issued and outstanding at June 30, 2007 and December 31, 2006; liquidation preference $1,000 per share ($50 per depositary share)	129.4	129.4
Common shares, $.01 par value; 480,000,000 shares authorized; 256,387,368 and 255,669,983 shares issued; 248,097,440 and 247,471,538 outstanding at June 30, 2007 and December 31, 2006	2.6	2.6
Additional paid-in capital	2,923.7	2,924.9

Accumulated deficit	(3,485.6)	(3,527.2)
Accumulated other comprehensive loss	(166.9)	(174.5)
Common shares in treasury, at cost:		
8,289,928 and 8,198,445 shares at June 30, 2007 and December 31, 2006	(147.2)	(146.8)
Total shareowners deficit	(744.0)	(791.6)
Total liabilities and shareowners deficit	$ 1,952.7	$ 2,013.8

The accompanying notes are an integral part of the condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in millions)

(Unaudited)

	Six Months Ended June 30, 2007	2006
Cash flows from operating activities		
Net income	$ 46.7	$ 38.4
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation	71.5	68.1
Amortization	1.7	2.0
Gain on sale of broadband assets		(2.9)
Provision for loss on receivables	7.4	7.6
Noncash interest expense	2.6	2.5
Minority interest expense		0.4
Deferred income tax expense, including valuation allowance change	32.6	32.4
Pension and other postretirement expense in excess of payments	14.9	16.5
Other, net	1.0	0.1
Changes in operating assets and liabilities, net of effects of acquisitions		
(Increase) decrease in receivables	(0.7)	9.4
Increase in prepaid expenses and other current assets	(14.8)	(21.8)
Increase in accounts payable	10.7	8.5
Decrease in accrued and other current liabilities	(16.8)	(5.1)
Change in other assets and liabilities, net	(1.7)	1.5
Net cash provided by operating activities	155.1	157.6
Cash flows from investing activities		
Capital expenditures	(90.3)	(74.6)
Acquisitions of businesses and remaining minority interest in CBW	(4.6)	(86.7)
Other, net	0.1	2.0
Net cash used in investing activities	(94.8)	(159.3)
Cash flows from financing activities		
Issuance of long-term debt	75.0	
Increase in corporate credit facility, net		12.0
Repayment of debt	(183.2)	(5.7)
Issuance of common shares - exercise of stock options	2.3	0.7
Preferred stock dividends	(5.2)	(5.2)
Debt issuance costs	(1.3)	
Other, net	(0.6)	0.8
Net cash (used in) provided by financing activities	(113.0)	2.6
Net (decrease) increase in cash and cash equivalents	(52.7)	0.9

Cash and cash equivalents at beginning of year	79.4	25.7
Cash and cash equivalents at end of period	$ 26.7	$ 26.6

The accompanying notes are an integral part of the condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Description of Business and Accounting Policies

The following represents a summary of the business and accounting policies of Cincinnati Bell Inc. (the Company). A more detailed presentation can be found in the Company s 2006 Annual Report on Form 10-K.

Description of Business The Company provides diversified telecommunications services through businesses in three segments: Wireline, Wireless and Technology Solutions. During the second quarter of 2007, the Company realigned its reportable business segments to be consistent with changes to its management structure and reporting. Refer to Note 7 for further discussion concerning the Company s segments.

Basis of Presentation The Condensed Consolidated Financial Statements of the Company have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) and, in the opinion of management, include all adjustments necessary for a fair presentation of the results of operations, financial position, and cash flows for each period presented.

The adjustments referred to above are of a normal and recurring nature. Certain prior year amounts have been reclassified to conform to the current classifications with no effect on results of operations. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to SEC rules and regulations.

The Condensed Consolidated Balance Sheet as of December 31, 2006 was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. These Condensed Consolidated Financial Statements should be read in conjunction with the Company's 2006 Annual Report on Form 10-K. Operating results for the three and six month periods ended June 30, 2007 are not necessarily indicative of the results expected in subsequent quarters or for the year ending December 31, 2007.

Income Taxes The Company and its subsidiaries file income tax returns in the U.S. federal jurisdiction, and various states and local jurisdictions. With a few exceptions, the Company is no longer subject to U.S. federal, state or local examinations for years before 2003. In the first quarter of 2007, the Internal Revenue Service commenced an examination of the Company s U.S. federal income tax returns for 2004 and 2005. The Company expects these examinations to be completed by the end of 2007.

The Company adopted the provisions of Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes, (FIN 48) on January 1, 2007. As a result of the implementation of FIN 48, the Company recognized a $5.1 million increase in the liability for unrecognized tax benefits, which was accounted for as a reduction to the January 1, 2007 balance of retained earnings. After recognizing this impact upon adoption of FIN 48, the Company has a $14.7 million liability recorded for unrecognized tax benefits as of January 1, 2007 and June 30, 2007. The total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate is $14.5 million. The Company does not currently anticipate that the amount of unrecognized tax benefits will change significantly over the next year.

The Company recognizes accrued penalties related to unrecognized tax benefits in income tax expense. The Company recognizes accrued interest related to unrecognized tax benefits in interest expense. Accrued interest and penalties are insignificant at December 31, 2006 and June 30, 2007.

Regulatory Taxes The Company incurs federal regulatory taxes on certain revenue producing transactions. The Company is permitted to recover certain of these taxes by billing the customer, however, collections cannot exceed the amount due to the federal regulatory agency. These federal regulatory taxes are presented in sales and cost of services on a gross basis because, while the Company is required to pay the tax, it is not required to collect the tax from customers and, in fact, does not collect from customers in certain instances. The amount recorded as revenue for the three and six months ended June 30, 2007 was $4.7 million and $8.4 million and for the three and six months ended June 30, 2006 was $4.2 million and $8.0 million, respectively. The amount expensed for the three and six months ended June 30, 2007 was $5.4 million and $9.6 million and for the three and six months ended June 30, 2006 was $4.5 million and $8.9 million, respectively. The Company records all other taxes collected from customers on a net basis.

Stock-Based Compensation The Company values all share-based payments to employees at fair value on the date of grant and expenses this value over the applicable vesting period. The Company s policy for graded vesting awards is to recognize compensation expense on a straight-line basis over the vesting period. For all share-based payments, an assumption is made for an estimated forfeiture rate based on the historical behavior of employees. The Company s practice has been to make its annual grant of stock options and time-based restricted awards in December and annual performance-based awards in the first quarter. In addition, the Company also has historically granted a smaller number of stock-based awards at various times during the year for new employees, promotions and performance achievements.

In the second quarter of 2007, the Company s shareholders approved both The Cincinnati Bell Inc. 2007 Long Term Incentive Plan (the 2007 Long Term Plan) and The Cincinnati Bell Inc. 2007 Stock Option Plan For Non-Employee Directors (the 2007 Directors Plan), which replaced the Cincinnati Bell Inc. 1997 Long Term Incentive Plan and the Cincinnati Bell Inc. 1997 Stock Option Plan, respectively. The 2007 Long Term Plan provides for awards in the form of stock options, including incentive stock options (ISOs), stock appreciation rights and other awards (e.g., restricted stock, performance shares, share-based performance units, non-share based performance units and non-restricted stock) to eligible employees of the Company. The 2007 Long Term Plan authorizes the issuance of up to 8,000,000 common shares of which the maximum number of common shares that can be issued as ISOs and other awards is 2,000,000 and 2,400,000 common shares, respectively. The 2007 Directors Plan provides for awards to be granted in the form of stock options or restricted stock awards to members of the Board, who are not employees of the Company. The 2007 Directors Plan authorizes the issuance of up to 1,000,000 common shares for grant of stock-based awards, of which a maximum of 1,000,000 common shares may be issued as stock options and a maximum of 300,000 common shares may be issued as restricted stock awards.

Stock options

The following table summarizes stock option activity for the six months ended June 30, 2007:

	Number of options (in thousands)	Weighted-average option prices per share	Weighted-average remaining contractual life in years
Outstanding at December 31, 2006	21,153	$ 10.89	5.3
Granted	145	4.95	
Exercised	(580)	3.97	
Forfeited or expired	(691)	12.53	
Outstanding at June 30, 2007	20,027	$ 11.00	5.0
Exercisable at June 30, 2007	18,861	$ 11.39	4.6

The Company recognized compensation expense of $0.3 million related to option grants for the three months ended June 30, 2007 and $0.5 million for the six months ended June 30, 2007 and had $0.1 million of expense for both the three months and six months ended June 30, 2006. As of June 30, 2007, there was $1.3 million of unrecognized compensation expense related to non-vested stock options. This expense is expected to be recognized over a weighted average period of approximately three years. At June 30, 2007, the aggregate intrinsic value of stock options outstanding and exercisable was approximately $12.9 million and $10.1 million, respectively.

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The weighted average fair values at the date of grant for options granted were $1.79 and $1.34 for the three months ended June 30, 2007 and 2006, respectively, and $1.69 and $1.21 for the six months ended June 30, 2007 and 2006, respectively. The weighted average fair values at the date of grant were estimated using the Black-Scholes option-pricing model with the following assumptions:

	Six Months Ended June 30,	
	2007	2006
Expected volatility	28.9%	32.0%
Risk-free interest rate	4.6%	4.6%
Expected holding period - years	5	4
Expected dividends	0.0%	0.0%

The expected volatility assumption used in the Black-Scholes pricing model was based on historical volatility. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant. The expected holding period was estimated using the historical exercise behavior of employees and adjusted for abnormal activity. Expected dividends are based on the Company s history of paying dividends, as well as restrictions in place under the Company s debt covenants.

Performance-based awards

During the six months ended June 30, 2007, the Company granted performance-based awards that allow the recipients to receive up to 880,800 shares, which vest over three years and upon the achievement of certain performance-based objectives over the period 2007 to 2009. The fair value of the awards on the date of grant was $4.73 per share. During the six months ended June 30, 2006, the Company granted performance-based awards that allow the recipients to receive up to 819,750 shares, which vest over three years and upon the achievement of certain performance-based objectives over the period 2006 to 2008. The fair value of these awards on the date of grant was $4.29 per share. The Company recognized expense for performance-based awards of $0.9 million for three months ended June 30, 2007 and $1.3 million for the six months ended June 30, 2007, and $0.4 million expense for the three and six months ended June 30, 2006. As of June 30, 2007, there was $1.2 million of unrecognized compensation expense related to performance-based awards, substantially all of which is expected to be recognized in 2007.

Time-based restricted awards

In December 2006, rather than granting options as in previous years, the Company issued 253,199 time-based restricted shares, to lower level managers. These shares vest in one-third increments over a period of three years and had a fair value of $4.74 per share at the date of grant. There were no time-based restricted awards granted in either of the six months ended June 30, 2007 or 2006. The Company recognized expense of $0.1 million for both the six months ended June 30, 2007 and 2006 related to time-based restricted awards. As of June 30, 2007, there was $0.7 million of unrecognized compensation expense related to these shares. This expense is expected to be recognized over a weighted average period of approximately three years.

Comprehensive Income

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Net income	$ 24.2	$ 24.3	$ 46.7	$ 38.4
Amortization of pension and postretirement costs, net of taxes of $2.1 million and $4.3 million, respectively	3.9		7.6	
Comprehensive income	$ 28.1	$ 24.3	$ 54.3	$ 38.4

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Recently Issued Accounting Standards In September 2006, the FASB ratified Emerging Issues Task Force (EITF) Issue No. 06-1, Accounting for Consideration Given by a Service Provider to Manufacturers or Resellers of Equipment Necessary for an End-Customer to Receive Service from the Service Provider. This guidance requires the application of EITF No. 01-9, Accounting for Consideration Given by a Vendor to a Customer, when consideration is given to a reseller or manufacturer for benefit to the service provider s end-customer. EITF No. 01-9 requires the consideration given be recorded as a liability at the time of the sale of the equipment and, also, provides guidance for the classification of the expense. EITF No. 06-1 is effective for the first fiscal year that begins after June 15, 2007. Implementation of this Statement is not expected to have a material impact on the Company s financial statements.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS 157). The objective of the statement is to define fair value, establish a framework for measuring fair value and expand disclosures about fair value measurements. SFAS 157 will be effective for interim and annual reporting periods beginning after November 15, 2007. The Company has not yet assessed the impact of this statement on the Company s financial statements.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). The Statement permits entities to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. SFAS 159 will be effective for the first fiscal year that begins after November 15, 2007. The Company has not yet determined whether it will adopt the alternatives provided in this standard.

2. Acquisitions of Businesses

Local Telecommunication Business

In March 2007, the Company purchased a local telecommunication business, which offers voice, data and cable TV services, in Lebanon, Ohio for a purchase price of $7.0 million, of which $4.6 million was paid in March 2007. The Company funded the purchase with its available cash. The purchase price was primarily allocated to property, plant and equipment of $4.4 million, customer relationship intangible assets of $1.5 million and goodwill of $2.1 million. The financial results have been included in the Wireline segment and were immaterial to the Company s financial statements for the three and six months ended June 30, 2007. The preliminary purchase price allocation for this transaction may be adjusted upon completion of the Company s valuation of the related assets and liabilities of the business.

Acquisition of Remaining Interest in Cincinnati Bell Wireless LLC

On February 14, 2006, the Company purchased Cingular s 19.9% membership interest in Cincinnati Bell Wireless LLC (CBW). As a result, the Company paid purchase consideration of $83.0 million in cash to Cingular and incurred transaction expenses of $0.2 million. CBW is now a wholly-owned subsidiary of the Company. The Company funded the purchase with its Corporate credit facility and available cash.

The transaction was accounted for as a step acquisition using the purchase method of accounting in accordance with Statement of Financial Accounting Standards No. 141, Business Combinations. The Company applied the purchase price against the minority interest and then allocated the remainder to identifiable tangible and intangible assets and liabilities acquired as follows:

(dollars in millions)	
Minority interest	$ 27.8
Intangible assets	42.1
Goodwill	10.2
Other	3.1
Total purchase price	$ 83.2

The purchase price allocation was based upon the estimated fair values as of February 14, 2006 of the tangible and intangible assets and liabilities. Estimated fair value was compared to the book value already recorded, and 19.9% of the excess of estimated fair value over book value was allocated to the respective tangible and intangible assets and liabilities. The excess purchase price over the minority interest and fair value ascribed to the tangible and intangible assets and liabilities was recorded as goodwill. The Company anticipates both the goodwill and intangible assets to be fully deductible for tax purposes.

The following table presents detail of the purchase price allocated to intangible assets of CBW as of the date of acquisition:

(dollars in millions)	Fair Value	Weighted Average Amortization Period
Intangible assets subject to amortization:		
Customer relationships - subscribers	$ 11.6	7 years
Customer relationships - collocation towers	2.6	10 years
Contractual right - license	0.7	1 year
	14.9	7 years
Intangible assets not subject to amortization:		
Licenses - owned	21.0	n/a
Trademarks	6.2	n/a
Total intangible assets	$ 42.1	

This acquisition has no effect on the Company s operating income, which historically has included 100% of CBW s operating income. However, for periods after the acquisition date, the 19.9% minority interest in the net income (loss) of CBW was no longer recorded.

The unaudited financial information in the table below summarizes the results of operations of the Company, on a pro forma basis, as though the acquisition had occurred as of the beginning of the period presented:

(dollars in millions, except per share amounts)	Six Months Ended June 30, 2006
Revenue	$ 621.6
Net income	37.9
Earnings per share - basic and diluted	0.13

3. Earnings Per Common Share

Basic earnings per common share (EPS) is based upon the weighted average number of common shares outstanding during the period. Diluted EPS reflects the potential dilution that would occur if common stock equivalents were exercised or converted to common stock but only to the extent that they are considered dilutive to the Company s earnings. The following table is a reconciliation of the numerators and denominators of the basic and diluted EPS computations for the following periods:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions, except per share amounts)	**2007**	**2006**	**2007**	**2006**
Numerator:				
Net income	$ 24.2	$ 24.3	$ 46.7	$ 38.4
Preferred stock dividends	2.6	2.6	5.2	5.2
Numerator for basic and diluted EPS	$ 21.6	$ 21.7	$ 41.5	$ 33.2
Denominator:				
Denominator for basic EPS - weighted average common shares outstanding	247.3	246.8	247.2	246.7
Warrants	7.9	4.6	7.1	4.3
Stock-based compensation arrangements	2.4	1.0	2.1	0.9
Denominator for diluted EPS	257.6	252.4	256.4	251.9
Basic earnings per common share	$ 0.09	$ 0.09	$ 0.17	$ 0.13
Diluted earnings per common share	$ 0.08	$ 0.09	$ 0.16	$ 0.13
Potentially issuable common shares excluded from denominator for diluted EPS due to anti-dilutive effect	32.9	38.0	34.1	38.3

4. Debt

The Company s debt consists of the following:

(dollars in millions)	June 30, 2007	December 31, 2006
Current portion of long-term debt:		
Credit facility, tranche B term loan	$ 4.0	$ 4.0
Capital lease obligations and other debt	3.4	3.3
Current portion of long-term debt	7.4	7.3
Long-term debt, less current portion:		
Credit facility, tranche B term loan	209.0	391.0
Accounts receivable securitization facility	75.0	
7 1/4% Senior Notes due 2013	496.9	496.9
8 3/8% Senior Subordinated Notes due 2014, $640 million face amount*	626.3	631.5
7% Senior Notes due 2015, $250 million face amount*	241.9	245.0
7 1/4% Senior Notes due 2023	50.0	50.0
Various Cincinnati Bell Telephone notes	230.0	230.0
Capital lease obligations and other debt	26.9	20.7
	1,956.0	2,065.1
Net unamortized premiums	0.7	0.8
Long-term debt, less current portion	1,956.7	2,065.9
Total debt	$ 1,964.1	$ 2,073.2

* The face amount of these notes has been adjusted for the fair value of interest rate swaps classified as fair value derivatives at June 30, 2007 and December 31, 2006.

Accounts Receivable Securitization Facility

In March 2007, the Company and certain subsidiaries as detailed below entered into an accounts receivable securitization facility (receivables facility), which permits borrowings of up to $80 million, depending on the level of eligible receivables and other factors. The receivables facility has a term of five years, expiring in March 2012. Under the receivables facility, Cincinnati Bell Telephone LLC (CBT), Cincinnati Bell Extended Territories, Cincinnati Bell Wireless LLC, Cincinnati Bell Any Distance Inc. and Cincinnati Bell Complete Protection Inc. sell their respective trade receivables on a continuous basis to Cincinnati Bell Funding LLC (CBF), a wholly-owned limited liability entity. In turn, CBF grants, without recourse, a senior undivided interest in the pooled receivables to commercial paper conduits in exchange for cash while maintaining a subordinated undivided interest, in the form of over-collateralization, in the pooled receivables. The Company has agreed to continue servicing the receivables for CBF at market rates; accordingly, no servicing asset or liability has been recorded.

Although CBF is a wholly-owned consolidated subsidiary of the Company, CBF is legally separate from the Company and each of the Company s other subsidiaries. Upon and after the sale or contribution of the accounts receivable to CBF, such accounts receivable are legally assets of CBF, and as such are not available to creditors of other subsidiaries or the parent company.

For the purposes of consolidated financial reporting, the receivables facility is accounted for as a secured financing. Because CBF has the ability to prepay the receivables facility at any time by making a cash payment and effectively repurchasing the receivables transferred pursuant to the facility, the transfers do not qualify for sale treatment on a consolidated basis under Statement of Financial Accounting Standards No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities a replacement of FASB Statement 125. Based on eligible receivables at June 30, 2007, the Company s borrowing limit under the receivables facility was $80 million, of which the Company had borrowed $75 million. See discussion below for the use of these borrowings. Interest on the receivables facility is based on commercial paper rates plus 0.5%.

Other

In the first six months of 2007, the Company prepaid $180 million of the Tranche B Term Loan, using proceeds of $75 million from borrowings under the receivables facility and the remainder from available cash.

The Company entered into capital leases for data center building space and equipment totaling $7.6 million during the six months ended June 30, 2007. The leased assets secured the capital lease obligations.

5. Restructuring Charges

2007 Restructuring

In the first quarter of 2007, the Company incurred employee separation expense of $2.4 million primarily related to the outsourcing of certain accounting functions and the reduction in workforce of various other administrative functions. At June 30, 2007, $0.6 million of the reserve was included in Other current liabilities, and $0.3 million was included in Other noncurrent liabilities in the Condensed Consolidated Balance Sheets. The following table illustrates the activity in this reserve through June 30, 2007:

Type of costs (dollars in millions)	Initial Charge	Utilizations	Balance March 31, 2007	Utilizations	Balance June 30, 2007
Employee separation obligations	$ 2.4	$ (0.8)	$ 1.6	$ (0.7)	$ 0.9

2006 Restructuring

In September 2006, the Company incurred employee separation expense of $3.0 million primarily related to the outsourcing of certain supply chain functions. At June 30, 2007, the restructuring reserve balance of $0.9 million was included in Other current liabilities in the Condensed Consolidated Balance Sheets. At December 31, 2006, $1.5 million of the restructuring reserve balance was included in Other current liabilities and $0.4 million was included in Other noncurrent liabilities in the Condensed Consolidated Balance Sheets. The following table illustrates the activity in this reserve from December 31, 2006 through June 30, 2007:

Type of costs (dollars in millions)	Balance December 31, 2006	Utilizations	Balance March 31, 2007	Utilizations	Balance June 30, 2007
Employee separation obligations	$ 1.9	$ (0.5)	$ 1.4	$ (0.5)	$ 0.9

November 2001 Restructuring Plan

In November 2001, the Company adopted a restructuring plan which included initiatives to consolidate data centers, reduce the Company s expense structure, exit the network construction business, eliminate other non-strategic operations, and merge the digital subscriber line and certain dial-up Internet operations into the Company s other operations. The Company completed the plan as of December 31, 2002, except for certain lease obligations, which are expected to continue through June 2015.

At June 30, 2007 and December 31, 2006, $1.4 million of the restructuring reserve balance was included in Other current liabilities in the Condensed Consolidated Balance Sheets. The restructuring reserve included in Other noncurrent liabilities in the Condensed Consolidated Balance Sheets was $5.2 million and $5.8 million at June 30, 2007 and December 31, 2006, respectively. The following table illustrates the activity in this reserve from December 31, 2006 through June 30, 2007:

Type of costs (dollars in millions):	Balance December 31, 2006	Utilizations	Expense	Balance March 31, 2007	Utilizations	Expense	Balance June 30, 2007
Terminate contractual obligations	$ 7.2	$ (0.2)	$ 0.1	$ 7.1	$ (0.6)	$ 0.1	$ 6.6

6. Pensions and Postretirement Plans

The following information relates to all Company noncontributory defined benefit pension plans, postretirement health care, and life insurance benefit plans. Approximately 12% of these costs were capitalized to property, plant and equipment related to network construction in the Wireline segment for both the three and six months ended June 30, 2007 and approximately 10% of these costs were capitalized for the three and six months ended June 30, 2006. Pension and postretirement benefit costs are as follows:

	Pension Benefits		Postretirement and Other Benefits	
	Three Months Ended June 30,			
(dollars in millions)	**2007**	**2006**	**2007**	**2006**
Service cost	$ 2.1	$ 2.1	$ 0.9	$ 1.0
Interest cost on projected benefit obligation	7.0	6.9	5.2	4.8
Expected return on plan assets	(8.2)	(8.7)	(1.0)	(1.2)
Amortization of:				
Transition obligation			1.1	1.0
Prior service cost	0.8	0.9	1.9	2.0
Actuarial loss	1.0	1.0	1.1	1.3
Benefit costs	$ 2.7	$ 2.2	$ 9.2	$ 8.9

	Pension Benefits		Postretirement and Other Benefits	
	Six Months Ended June 30,			
(dollars in millions)	**2007**	**2006**	**2007**	**2006**
Service cost	$ 4.2	$ 4.3	$ 1.7	$ 1.9
Interest cost on projected benefit obligation	13.9	13.7	10.5	9.6
Expected return on plan assets	(16.5)	(17.4)	(2.0)	(2.4)
Amortization of:				
Transition obligation			2.1	2.1
Prior service cost	1.6	1.7	3.9	3.9
Actuarial loss	2.1	2.1	2.2	2.7
Benefit costs	$ 5.3	$ 4.4	$ 18.4	$ 17.8

7. Business Segment Information

Beginning in the second quarter of 2007, the Company has realigned its reportable business segments to be consistent with changes to its management structure and reporting. The Company now has three segments: Wireline, Wireless and Technology Solutions. The Wireline segment combines the operations of Cincinnati Bell Telephone LLC and Cincinnati Bell Extended Territories LLC, which were formerly included in the Local segment, and the operations of Cincinnati Bell Any Distance, Cincinnati Bell Complete Protection, the Company s payphone business and Cincinnati Bell Entertainment, which were formerly included in the Other segment. The Broadband segment, which does not have any substantive on-going operations, has been eliminated. The remaining liabilities associated with the former broadband operations are now included in Corporate activities. The Wireless and Technology Solutions segments were not impacted by the segment realignment. Prior year amounts have been reclassified to conform to the current segment reporting.

Certain corporate administrative expenses have been allocated to segments based upon the nature of the expense and the relative size of the segment.

The Company s business segment information follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(dollars in millions)	**2007**	**2006**	**2007**	**2006**
Revenue				
Wireline	$ 204.1	$ 203.4	$ 407.8	$ 405.4
Wireless	73.5	66.4	142.0	128.2
Technology Solutions	57.5	58.2	106.0	97.0
Intersegment	(6.0)	(4.7)	(11.4)	(9.0)
Total revenue	$ 329.1	$ 323.3	$ 644.4	$ 621.6
Intersegment revenue				
Wireline	$ 5.1	$ 3.7	$ 9.7	$ 6.9
Wireless	0.6	0.7	1.2	1.4
Technology Solutions	0.3	0.3	0.5	0.7
Total intersegment revenue	$ 6.0	$ 4.7	$ 11.4	$ 9.0
Operating income				
Wireline	$ 72.0	$ 77.6	$ 144.0	$ 153.6
Wireless	10.3	4.5	17.9	8.2
Technology Solutions	4.0	3.8	6.5	6.1
Corporate	(5.2)	(2.7)	(9.5)	(13.6)
Total operating income	$ 81.1	$ 83.2	$ 158.9	$ 154.3

Assets	**June 30, 2007**	**December 31, 2006**
Wireline	$ 713.1	$ 788.1
Wireless	343.1	382.1
Technology Solutions	145.9	112.5

Corporate and eliminations	750.6	731.1
Total assets	$ 1,952.7	$ 2,013.8

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8. Supplemental Guarantor Information
Cincinnati Bell Telephone Notes

CBT, a wholly-owned subsidiary of Cincinnati Bell Inc. (the Parent Company), has $230.0 million in notes outstanding that are guaranteed by the Parent Company and no other subsidiaries of the Parent Company. The guarantee is full and unconditional. The Parent Company s subsidiaries generate substantially all of its income and cash flow and generally distribute or advance the funds necessary to meet the Parent Company s debt service obligations. In the fourth quarter of 2006, the Company s payphone business became part of BRCOM Inc., a subsidiary of the Parent Company. The financial information presented below combines the Company s payphone business with the non-guarantors for all periods presented.

The following information sets forth the Condensed Consolidating Statements of Operations and Cash Flows for the three and six months ended June 30, 2007 and 2006 and Condensed Consolidating Balance Sheets of the Company as of June 30, 2007 and December 31, 2006 of (1) the Parent Company, as the guarantor (2) CBT, as the issuer, and (3) the non-guarantor subsidiaries on a combined basis:

Condensed Consolidating Statements of Operations

	Three Months Ended June 30, 2007				
(dollars in millions)	**Parent (Guarantor)**	**CBT**	**Other (Non-guarantors)**	**Eliminations**	**Total**
Revenue	$	$ 186.7	$ 152.5	$ (10.1)	$ 329.1
Operating costs and expenses	6.0	121.4	130.7	(10.1)	248.0
Operating income (loss)	(6.0)	65.3	21.8		81.1
Equity in earnings of subsidiaries, net of tax	48.7			(48.7)	
Interest expense	34.1	4.1	8.5	(7.7)	39.0
Other expense (income), net	(8.1)	1.8	(0.9)	7.0	(0.2)
Income before income taxes	16.7	59.4	14.2	(48.0)	42.3
Income tax expense (benefit)	(7.5)	21.0	4.6		18.1
Net income	24.2	38.4	9.6	(48.0)	24.2
Preferred stock dividends	2.6				2.6
Net income applicable to common shareowners	$ 21.6	$ 38.4	$ 9.6	$ (48.0)	$ 21.6

	Three Months Ended June 30, 2006				
	Parent (Guarantor)	**CBT**	**Other (Non-guarantors)**	**Eliminations**	**Total**
Revenue	$	$ 187.4	$ 144.4	$ (8.5)	$ 323.3
Operating costs and expenses	4.0	116.8	127.8	(8.5)	240.1
Operating income (loss)	(4.0)	70.6	16.6		83.2
Equity in earnings of subsidiaries, net of tax	47.7			(47.7)	
Interest expense	36.0	3.8	9.1	(8.6)	40.3
Other expense (income), net	(8.7)	0.1	(0.1)	8.6	(0.1)
Income before income taxes	16.4	66.7	7.6	(47.7)	43.0
Income tax expense (benefit)	(7.9)	23.8	2.8		18.7

Net income	24.3	42.9	4.8	(47.7)	24.3
Preferred stock dividends	2.6				2.6
Net income applicable to common shareowners	$ 21.7	$ 42.9	$ 4.8	$ (47.7)	$ 21.7

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Form 10-Q Part I Cincinnati Bell Inc.

Condensed Consolidating Statements of Operations

(dollars in millions)	Parent (Guarantor)	CBT	Other (Non-guarantors)	Eliminations	Total
	Six Months Ended June 30, 2007				
Revenue	$	$ 374.1	$ 289.8	$ (19.5)	$ 644.4
Operating costs and expenses	10.5	242.7	251.8	(19.5)	485.5
Operating income (loss)	(10.5)	131.4	38.0		158.9
Equity in earnings of subsidiaries, net of tax	94.1			(94.1)	
Interest expense	70.8	8.3	15.1	(15.1)	79.1
Other expense (income), net	(18.1)	1.8	(0.3)	14.4	(2.2)
Income before income taxes	30.9	121.3	23.2	(93.4)	82.0
Income tax expense (benefit)	(15.8)	43.0	8.1		35.3
Net income	46.7	78.3	15.1	(93.4)	46.7
Preferred stock dividends	5.2				5.2
Net income applicable to common shareowners	$ 41.5	$ 78.3	$ 15.1	$ (93.4)	$ 41.5

	Parent (Guarantor)	CBT	Other (Non-guarantors)	Eliminations	Total
	Six Months Ended June 30, 2006				
Revenue	$	$ 373.8	$ 264.6	$ (16.8)	$ 621.6
Operating costs and expenses	14.5	233.7	235.9	(16.8)	467.3
Operating income (loss)	(14.5)	140.1	28.7		154.3
Equity in earnings of subsidiaries, net of tax	92.0			(92.0)	
Interest expense	71.6	7.4	16.6	(15.8)	79.8
Other expense (income), net	(16.1)	0.1	0.4	15.8	0.2
Income before income taxes	22.0	132.6	11.7	(92.0)	74.3
Income tax expense (benefit)	(16.4)	47.5	4.8		35.9
Net income	38.4	85.1	6.9	(92.0)	38.4
Preferred stock dividends	5.2				5.2
Net income applicable to common shareowners	$ 33.2	$ 85.1	$ 6.9	$ (92.0)	$ 33.2

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Form 10-Q Part I Cincinnati Bell Inc.

Condensed Consolidating Balance Sheets

	As of June 30, 2007				
(dollars in millions)	**Parent (Guarantor)**	**CBT**	**Other (Non-guarantors)**	**Eliminations**	**Total**
Cash and cash equivalents	$ 25.2	$ 0.4	$ 1.1	$	$ 26.7
Receivables, net	0.1		155.1	0.7	155.9
Other current assets	15.3	50.4	87.1	(21.4)	131.4
Total current assets	40.6	50.8	243.3	(20.7)	314.0
Property, plant and equipment, net	0.1	592.5	264.0		856.6
Goodwill and intangibles, net		3.6	165.0		168.6
Investments in and advances to subsidiaries	972.2	15.8		(988.0)	
Other noncurrent assets	351.9	11.5	298.4	(48.3)	613.5
Total assets	$ 1,364.8	$ 674.2	$ 970.7	$ (1,057.0)	$ 1,952.7
Current portion of long-term debt	$ 4.0	$ 0.6	$ 2.8	$	$ 7.4
Accounts payable		42.2	48.7		90.9
Other current liabilities	90.4	80.7	47.4	(0.9)	217.6
Total current liabilities	94.4	123.5	98.9	(0.9)	315.9
Long-term debt, less current portion	1,625.2	236.0	95.5		1,956.7
Other noncurrent liabilities	389.2	67.8	35.9	(68.8)	424.1
Intercompany payables			409.5	(409.5)	
Total liabilities	2,108.8	427.3	639.8	(479.2)	2,696.7
Shareowners equity (deficit)	(744.0)	246.9	330.9	(577.8)	(744.0)
Total liabilities and shareowners equity (deficit)	$ 1,364.8	$ 674.2	$ 970.7	$ (1,057.0)	$ 1,952.7

	As of December 31, 2006				
	Parent (Guarantor)	**CBT**	**Other (Non-guarantors)**	**Eliminations**	**Total**
Cash and cash equivalents	$ 75.9	$ 1.5	$ 2.0	$	$ 79.4
Receivables, net	0.3	71.0	90.6		161.9
Other current assets	13.9	36.2	73.2	(17.2)	106.1
Total current assets	90.1	108.7	165.8	(17.2)	347.4
Property, plant and equipment, net	0.1	589.7	229.0		818.8
Goodwill and intangibles, net			166.2		166.2
Investments in and advances to subsidiaries	1,047.7			(1,047.7)	
Other noncurrent assets	365.1	12.0	349.8	(45.5)	681.4
Total assets	$ 1,503.0	$ 710.4	$ 910.8	$ (1,110.4)	$ 2,013.8
Current portion of long-term debt	$ 4.0	$ 0.9	$ 2.4	$	$ 7.3

Accounts payable	0.5	32.7	40.9		74.1
Other current liabilities	96.7	92.1	49.0	(0.3)	237.5
Total current liabilities	101.2	125.7	92.3	(0.3)	318.9
Long-term debt, less current portion	1,815.6	236.2	14.1		2,065.9
Other noncurrent liabilities	377.8	65.0	40.2	(62.4)	420.6
Intercompany payables		37.3	432.5	(469.8)	
Total liabilities	2,294.6	464.2	579.1	(532.5)	2,805.4
Shareowners equity (deficit)	(791.6)	246.2	331.7	(577.9)	(791.6)
Total liabilities and shareowners equity (deficit)	$ 1,503.0	$ 710.4	$ 910.8	$ (1,110.4)	$ 2,013.8

Condensed Consolidating Statements of Cash Flows

	Six Months Ended June 30, 2007				
(dollars in millions)	**Parent (Guarantor)**	**CBT**	**Other (Non-guarantors)**	**Eliminations**	**Total**
Cash flows provided by (used in) operating activities	$ (33.2)	$ 181.7	$ 6.6	$	$ 155.1
Capital expenditures		(47.5)	(42.8)		(90.3)
Acquisition of business		(4.6)			(4.6)
Other investing activities		0.6	(0.5)		0.1
Cash flows used in investing activities		(51.5)	(43.3)		(94.8)
Funding between Parent and subsidiaries, net	168.0	(130.7)	(37.3)		
Issuance of debt			75.0		75.0
Repayment of debt	(182.0)	(0.6)	(0.6)		(183.2)
Other financing activities	(3.5)		(1.3)		(4.8)
Cash flows provided by (used in) financing activities	(17.5)	(131.3)	35.8		(113.0)
Decrease in cash and cash equivalents	(50.7)	(1.1)	(0.9)		(52.7)
Beginning cash and cash equivalents					