CINCINNATI BELL INC
Form 10-Q
August 04, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended June 30, 2016

o 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 o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

Large accelerated filer	x	Accelerated filer	o
Non-accelerated filer	o	Smaller reporting company	o

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

At July 31, 2016, there were 210,173,102 common shares outstanding.

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Form 10-Q Part I Cincinnati Bell Inc.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in millions, except per share amounts)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Revenue				
Services	$244.9	$229.4	$486.4	$459.2
Products	54.3	56.4	101.7	119.5
Total revenue	299.2	285.8	588.1	578.7
Costs and expenses				
Cost of services, excluding items below	124.8	114.4	248.0	228.0
Cost of products sold, excluding items below	46.0	47.8	85.5	100.4
Selling, general and administrative, excluding items below	56.2	57.0	109.4	109.2
Depreciation and amortization	44.8	34.0	88.2	66.6
Other	—	2.9	—	7.7
Total operating costs and expenses	271.8	256.1	531.1	511.9
Operating income	27.4	29.7	57.0	66.8
Interest expense	19.9	28.0	40.2	60.7
Loss on extinguishment of debt, net	5.2	13.5	2.8	13.5
Gain on sale of CyrusOne investment	(118.6)	(295.2)	(118.6)	(295.2)
Other (income) expense, net	(1.1)	1.3	(1.1)	4.8
Income from continuing operations before income taxes	122.0	282.1	133.7	283.0
Income tax expense	44.4	101.4	49.1	102.0
Income from continuing operations	77.6	180.7	84.6	181.0
Income from discontinued operations, net of tax	—	10.9	—	59.8
Net income	77.6	191.6	84.6	240.8
Preferred stock dividends	2.6	2.6	5.2	5.2
Net income applicable to common shareowners	$75.0	$189.0	$79.4	$235.6
Basic net earnings per common share				
Basic earnings per common share from continuing operations	$0.36	$0.85	$0.38	$0.84
Basic earnings per common share from discontinued operations	$—	$0.05	$—	$0.29
Basic net earnings per common share	$0.36	$0.90	$0.38	$1.13
Diluted net earnings per common share				
Diluted earnings per common share from continuing operations	$0.36	$0.84	$0.38	$0.84
Diluted earnings per common share from discontinued operations	$—	$0.05	$—	$0.28
Diluted net earnings per common share	$0.36	$0.89	$0.38	$1.12

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

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CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Dollars in millions)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net income	$77.6	$191.6	$84.6	$240.8
Other comprehensive income				
Foreign currency translation gain (loss)	—	0.2	(0.1)	(0.1)
Defined benefit pension and postretirement plans				
Net gain arising from remeasurement during the period, net of tax of $0.6	—	1.1	—	1.1
Amortization of prior service benefits, net of tax of ($1.3), ($1.4), ($2.7), ($2.8)	(2.4)	(2.4)	(4.7)	(4.8)
Amortization of net actuarial loss, net of tax of $2.2, $3.8, $4.3, $6.2	3.9	6.9	7.8	11.0
Reclassification adjustment for curtailment loss included in net income, net of tax of $0.1	—	0.2	—	0.2
Other comprehensive income	1.5	6.0	3.0	7.4
Total comprehensive income	$79.1	$197.6	$87.6	$248.2

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

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CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in millions, except share amounts)
(Unaudited)

	June 30, 2016	December 31, 2015
Assets		
Current assets		
Cash and cash equivalents	$9.6	$ 7.4
Receivables, less allowances of $11.9 and $12.4	157.5	157.1
Inventory, materials and supplies	23.1	20.6
Prepaid expenses	15.7	13.1
Other current assets	3.0	2.2
Total current assets	208.9	200.4
Property, plant and equipment, net	1,021.7	975.5
Investment in CyrusOne	27.4	55.5
Goodwill	14.3	14.3
Deferred income taxes, net	132.5	182.9
Other noncurrent assets	18.4	17.8
Total assets	$1,423.2	$ 1,446.4
Liabilities and Shareowners' Deficit		
Current liabilities		
Current portion of long-term debt	$14.7	$ 13.8
Accounts payable	142.5	128.9
Unearned revenue and customer deposits	26.7	29.2
Accrued taxes	12.0	14.5
Accrued interest	8.0	11.2
Accrued payroll and benefits	27.9	31.2
Other current liabilities	24.5	25.0
Other current liabilities from discontinued operations	0.6	5.4
Total current liabilities	256.9	259.2
Long-term debt, less current portion	1,125.7	1,223.8
Pension and postretirement benefit obligations	217.5	225.0
Other noncurrent liabilities	40.1	36.6
Total liabilities	1,640.2	1,744.6
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, 2016 and December 31, 2015; liquidation preference $1,000 per share ($50 per depositary share)	129.4	129.4
Common shares, $.01 par value; 480,000,000 shares authorized; 209,277,290 and 210,017,999 shares issued; 209,136,240 and 209,876,949 shares outstanding at June 30, 2016 and December 31, 2015	2.1	2.1
Additional paid-in capital	2,569.6	2,576.0
Accumulated deficit	(2,749.6)	(2,834.2)
Accumulated other comprehensive loss	(168.0)	(171.0)
Common shares in treasury, at cost	(0.5)	(0.5)
Total shareowners' deficit	(217.0)	(298.2)
Total liabilities and shareowners' deficit	$1,423.2	$ 1,446.4

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

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in millions)

	Six Months Ended June 30,	
	2016	2015
Cash flows from operating activities		
Net income	$84.6	$240.8
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	88.2	95.2
Loss on extinguishment of debt	2.8	13.5
Provision for loss on receivables	4.3	4.3
Gain on sale of CyrusOne investment	(118.6)	(295.2)
Noncash portion of interest expense	1.7	2.5
Deferred income tax provision	48.6	129.4
Pension and other postretirement payments in excess of expense	(2.8)	(8.4)
Stock-based compensation	3.5	2.1
Deferred gain on sale of wireless spectrum licenses - discontinued operations	—	(112.6)
Amortization of deferred gain - discontinued operations	—	(6.5)
Gain on transfer of lease obligations - discontinued operations	—	(15.9)
Other, net	(3.6)	5.3
Changes in operating assets and liabilities:		
(Increase) decrease in receivables	(5.5)	4.9
(Increase) decrease in inventory, materials, supplies, prepaid expenses and other current assets	(5.0)	0.4
Increase (decrease) increase in accounts payable	14.0	(17.0)
Decrease in accrued and other current liabilities	(17.0)	(13.0)
(Increase) decrease in other noncurrent assets	(0.6)	0.8
Increase in other noncurrent liabilities	3.5	2.1
Net cash provided by operating activities	98.1	32.7
Cash flows from investing activities		
Capital expenditures	(121.6)	(132.5)
Dividends received from CyrusOne	4.9	15.0
Proceeds from sale of CyrusOne investment	142.5	426.0
Other, net	(0.7)	(0.1)
Net cash provided by investing activities	25.1	308.4
Cash flows from financing activities		
Net increase (decrease) in corporate credit and receivables facilities with initial maturities less than 90 days	15.4	(16.6)
Repayment of debt	(124.6)	(361.4)
Debt issuance costs	(1.9)	(0.4)
Dividends paid on preferred stock	(5.2)	(5.2)
Common stock repurchase	(4.6)	—
Other, net	(0.1)	(0.6)
Net cash used in financing activities	(121.0)	(384.2)
Net increase (decrease) in cash and cash equivalents	2.2	(43.1)
Cash and cash equivalents at beginning of period	7.4	57.9
Cash and cash equivalents at end of period	$9.6	$14.8

Noncash investing and financing transactions:		
Accrual of CyrusOne dividends	$1.5	$4.5
Acquisition of property by assuming debt and other noncurrent liabilities	$10.1	$2.9
Acquisition of property on account	$34.2	$33.0

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

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Description of Business and Accounting Policies

Description of Business — Cincinnati Bell Inc. and its consolidated subsidiaries ("Cincinnati Bell", "we", "our", "us" or the "Company") provides diversified telecommunications and technology services. The Company generates a large portion of its revenue by serving customers in the Greater Cincinnati and Dayton, Ohio areas. An economic downturn or natural disaster occurring in this, or a portion of this, limited operating territory could have a disproportionate effect on our business, financial condition, results of operations and cash flows compared to similar companies of a national scope and similar companies operating in different geographic areas.

As of June 30, 2016, we operate our business through the following segments: Entertainment and Communications and IT Services and Hardware.

The company has 3,400 employees as of June 30, 2016, and approximately 30% of its employees are covered by a collective bargaining agreement with Communications Workers of America (“CWA”) that will be in effect through May 12, 2018.

The Company has receivables with one large customer, General Electric Company ("GE"), that makes up 22% of the outstanding accounts receivable balance at June 30, 2016 and December 31, 2015. GE represented 12% and 11% of consolidated revenue for the three and six months ended June 30, 2016, respectively, compared to 11% and 12% during the same periods in 2015.

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

The adjustments referred to above are of a normal and recurring nature. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) have been condensed or omitted pursuant to SEC rules and regulations for interim reporting.

The Condensed Consolidated Balance Sheet as of December 31, 2015 was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP. These Condensed Consolidated Financial Statements should be read in conjunction with the Company’s 2015 Annual Report on Form 10-K. Operating results for the three and six months ended June 30, 2016 are not necessarily indicative of the results expected for the full year or any other interim period.

The closing of our wireless operations in March 2015 represented a strategic shift in our business. Therefore, certain wireless assets, liabilities and results of operations are reported as discontinued operations in our financial statements. See Note 9 for all required disclosures.

Use of Estimates — Preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported. Actual results could differ from those estimates. In the normal course of business, the Company is subject to various regulatory and tax proceedings, lawsuits, claims and other matters. The Company believes adequate provision has been made for all such asserted and unasserted claims in accordance with U.S. GAAP. Such matters are subject to many uncertainties and outcomes that are not predictable with assurance.

Restructuring Liability — As of June 30, 2016, restructuring liabilities have been established for employee separations, lease abandonments and other charges. As of June 30, 2016 and December 31, 2015, $0.2 million and $0.9 million, respectively, of the restructuring liabilities were included in “Other current liabilities,” in the Condensed Consolidated Balance Sheets. As of June 30, 2016 and December 31, 2015, $0.2 million was included in “Other noncurrent liabilities” in the Condensed Consolidated Balance Sheets.

Income Taxes — The Company’s income tax provision for interim periods is determined through the use of an estimated annual effective tax rate applied to year-to-date ordinary income, as well as the tax effects associated with discrete items. The Company expects its effective rate to exceed statutory rates primarily due to non-deductible expenses.

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Recently Issued Accounting Standards — In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-09, Compensation - Stock Compensation, which simplifies various aspects related to how share-based payments are accounted for and presented in the financial statements. The new standard is effective for public business entities for annual reporting periods beginning after December 15, 2016. The Company is currently in the process of evaluating the impact of adoption of this ASU on the Company's consolidated financial statements and plans to adopt the standard effective January 1, 2017.

In February 2016, the FASB issued ASU 2016-02, Leases, which represents a wholesale change to lease accounting. The standard introduces a lessee model that brings most leases on the balance sheet as well as aligning certain underlying principles of the new lessor model with those in Accounting Standards Codification ("ASC") 606. The new standard is effective for public business entities for fiscal years beginning after December 15, 2018, and lessees and lessors are required to use a modified retrospective transition method for existing leases. The Company is currently in the process of evaluating the impact of adoption of this ASU on the Company's consolidated financial statements.

The FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, in January 2016, which amends the guidance in U.S. GAAP on the classification and measurement of financial instruments. The amended guidance requires entities to carry all investments in equity securities at fair value through net income unless the entity has elected the practicability exception to fair value measurement. This standard will be effective for the fiscal year ending December 31, 2018 and will require a cumulative-effect adjustment to beginning retained earnings on this date. The Company is currently in the process of evaluating the impact of adoption of this ASU on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, which changes the presentation of debt issuance costs in the financial statements. Specifically, this amendment requires that costs associated with the issuance of debt be presented on the balance sheet as a direct deduction from the related debt liability. The Company retrospectively adopted the amended standard effective January 1, 2016. The Condensed Consolidated Balance Sheet for the period ending December 31, 2015 has been restated to reflect this change in accounting principle. Note issuance costs of $8.0 million were reclassed from “Other noncurrent assets” to “Long-term debt, less current portion.” Note 3 has been updated to reflect the adjustment. On the effective date of ASU 2015-03, the Company made a one-time policy election to record costs incurred in connection with obtaining revolving credit agreements as an asset and to amortize these costs ratably over the term of the agreement. This accounting treatment is consistent with how deferred financing costs were accounted for prior to adoption of ASU 2015-03.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. This standard also includes expanded disclosure requirements that result in an entity providing users of financial statements with comprehensive information about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. In August 2015, ASU 2015-14 was issued deferring the effective date of ASU 2014-09 to annual reporting periods beginning after December 15, 2017 with an optional early application date for annual reporting periods beginning after December 15, 2016. The Company has elected to adopt the standard in the first quarter of the fiscal year ending December 31, 2018. In March 2016, the FASB issued ASU 2016-08, an update to ASU 2014-09, clarifying the implementation guidance on principal versus agent considerations. The Company is in the process of evaluating the impact of the standard for the IT Services and Hardware segment that is a reseller of Telecom and IT hardware. Under the current guidance, these equipment revenues are generally recorded on a gross basis. The Company is continuing to evaluate the impact of adoption of ASU 2014-09, as well as all subsequent amendments to this standard, on the Company's consolidated financial statements.

No other new accounting pronouncement issued or effective during the year had, or is expected to have, a material impact on the consolidated financial statements.

2. 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 upon the issuance of common shares for awards under stock-based compensation plans, the exercise of warrants or the conversion of preferred stock, but only to the extent that they are considered dilutive.

The following table shows the computation of basic and diluted EPS:

(in millions, except per share amounts)	Three Months Ended June 30, 2016			Three Months Ended June 30, 2015		
	Continuing Operations	Discontinued Operations	Total	Continuing Operations	Discontinued Operations	Total
Numerator:						
Net income	$77.6	$ —	$77.6	$180.7	$ 10.9	$191.6
Preferred stock dividends [1]	2.6	—	2.6	2.6	—	2.6
Net income applicable to common shareowners - basic and diluted	$75.0	$ —	$75.0	$178.1	$ 10.9	$189.0
Denominator:						
Weighted average common shares outstanding - basic	209.8	209.8	209.8	209.7	209.7	209.7
Stock-based compensation arrangements	0.6	0.6	0.6	0.4	0.4	0.4
Conversion of preferred shares	—	—	—	4.5	4.5	4.5
Weighted average common shares outstanding - diluted	210.4	210.4	210.4	214.6	214.6	214.6
Basic earnings per common share	$0.36	$ —	$0.36	$0.85	$ 0.05	$0.90
Diluted earnings per common share	$0.36	$ —	$0.36	$0.84	$ 0.05	$0.89

(1) Calculation of diluted earnings per common share for the three months ended June 30, 2015 excludes preferred stock dividends as the preferred shares are considered converted.

(in millions, except per share amounts)	Six Months Ended June 30, 2016			Six Months Ended June 30, 2015		
	Continuing Operations	Discontinued Operations	Total	Continuing Operations	Discontinued Operations	Total
Numerator:						
Net income	$84.6	$ —	$84.6	$181.0	$ 59.8	$240.8
Preferred stock dividends	5.2	—	5.2			