

Hawaiian Telcom Holdco, Inc.
Form 10-Q
November 12, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark one)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2013

OR

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: 001-34686

Hawaiian Telcom Holdco, Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

16-1710376

(I.R.S. Employer Identification No.)

1177 Bishop Street

Honolulu, Hawaii 96813

(Address of principal executive offices)

808-546-4511

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, 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 No

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 definition of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer
(Do not check if smaller reporting company)

Smaller reporting company

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes No

As of November 12, 2013, 10,339,517 shares of the registrant's common stock were outstanding.

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****Hawaiian Telcom Holdco, Inc.****Condensed Consolidated Statements of Income****(Unaudited, dollars in thousands, except per share amounts)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Operating revenues	\$ 97,682	\$ 96,647	\$ 290,643	\$ 288,910
Operating expenses:				
Cost of revenues (exclusive of depreciation and amortization)	41,829	41,176	122,073	121,407
Selling, general and administrative	27,965	26,547	84,860	82,567
Gain on sale of property			(6,546)	
Depreciation and amortization	19,974	18,023	58,532	51,965
Total operating expenses	89,768	85,746	258,919	255,939
Operating income	7,914	10,901	31,724	32,971
Other income (expense):				
Interest expense	(4,089)	(5,490)	(14,712)	(16,890)
Loss on early extinguishment of debt			(3,660)	(5,112)
Interest income and other	7	10	28	28
Total other expense	(4,082)	(5,480)	(18,344)	(21,974)
Income before income tax provision (benefit)	3,832	5,421	13,380	10,997
Income tax provision (benefit)	1,771	(194)	5,521	(346)
Net income	\$ 2,061	\$ 5,615	\$ 7,859	\$ 11,343
Net income per common share -				
Basic	\$ 0.20	\$ 0.55	\$ 0.76	\$ 1.11
Diluted	\$ 0.18	\$ 0.52	\$ 0.71	\$ 1.06
Weighted average shares used to compute net income per common share -				
Basic	10,337,488	10,246,335	10,321,905	10,230,719
Diluted	11,206,159	10,708,454	11,096,177	10,658,517

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See accompanying notes to condensed consolidated financial statements.

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Hawaiian Telcom Holdco, Inc.

Condensed Consolidated Statements of Comprehensive Income

(Unaudited, dollars in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Net income	\$ 2,061	\$ 5,615	\$ 7,859	\$ 11,343
Other comprehensive income (loss), net of tax -				
Unrealized holding gains (losses) arising during period	6	(1)	(22)	(2)
Retirement plan	222	260	667	33,648
Income tax charge on comprehensive income	(88)		(263)	
Other comprehensive income, net of tax -	140	259	382	33,646
Comprehensive income	\$ 2,201	\$ 5,874	\$ 8,241	\$ 44,989

See accompanying notes to condensed consolidated financial statements.

Table of Contents**Hawaiian Telcom Holdco, Inc.****Condensed Consolidated Balance Sheets****(Unaudited, dollars in thousands, except per share amounts)**

	September 30, 2013	December 31, 2012
Assets		
Current assets		
Cash and cash equivalents	\$ 45,114	\$ 66,993
Receivables, net	36,706	34,082
Material and supplies	15,268	11,352
Prepaid expenses	5,344	5,161
Deferred income taxes	5,892	5,727
Other current assets	2,751	2,181
Total current assets	111,075	125,496
Property, plant and equipment, net	517,874	507,197
Intangible assets, net	41,052	39,075
Goodwill	11,783	1,569
Deferred income taxes	94,908	102,680
Other assets	12,315	9,075
Total assets	\$ 789,007	\$ 785,092
Liabilities and Stockholders' Equity		
Current liabilities		
Current portion of long-term debt	\$ 3,000	\$ 3,000
Accounts payable	39,102	36,351
Accrued expenses	16,227	20,537
Advance billings and customer deposits	16,159	15,185
Other current liabilities	5,387	3,961
Total current liabilities	79,875	79,034
Long-term debt	292,248	292,410
Employee benefit obligations	121,014	132,004
Other liabilities	9,309	4,784
Total liabilities	502,446	508,232
Commitments and contingencies (Note 12)		
Stockholders' equity		
Common stock, par value of \$0.01 per share, 245,000,000 shares authorized and 10,338,737 and 10,291,897 shares issued and outstanding at September 30, 2013 and December 31, 2012, respectively	103	103
Additional paid-in capital	167,401	165,941
Accumulated other comprehensive loss	(28,068)	(28,450)
Retained earnings	147,125	139,266
Total stockholders' equity	286,561	276,860
Total liabilities and stockholders' equity	\$ 789,007	\$ 785,092

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See accompanying notes to condensed consolidated financial statements.

Table of Contents**Hawaiian Telcom Holdco, Inc.****Condensed Consolidated Statements of Cash Flows****(Unaudited, dollars in thousands)**

	Nine Months Ended September 30,	
	2013	2012
Cash flows from operating activities:		
Net income	\$ 7,859	\$ 11,343
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	58,532	51,965
Loss on early extinguishment of debt	3,660	5,112
Gain on sale of property	(6,546)	
Employee retirement benefits	(10,324)	(11,001)
Provision for uncollectibles	2,003	2,526
Stock based compensation	1,886	1,343
Deferred income taxes	6,018	
Changes in operating assets and liabilities:		
Receivables	(4,142)	(1,552)
Material and supplies	(3,916)	(2,153)
Prepaid expenses and other current assets	(1,064)	(2,600)
Accounts payable and accrued expenses	(2,064)	1,768
Advance billings and customer deposits	323	980
Other current liabilities	106	296
Other	2,446	1,021
Net cash provided by operating activities	54,777	59,048
Cash flows from investing activities:		
Capital expenditures	(69,809)	(61,019)
Acquisitions	(11,858)	
Proceeds on sale of property	13,118	
Net cash used in investing activities	(68,549)	(61,019)
Cash flows from financing activities:		
Repayment of capital lease	(406)	
Repayment of debt including premium	(302,333)	(306,000)
Proceeds from borrowing	298,500	295,500
Loan refinancing costs	(3,442)	(4,130)
Taxes paid related to net share settlement of equity awards	(426)	(53)
Net cash used in financing activities	(8,107)	(14,683)
Net change in cash and cash equivalents	(21,879)	(16,654)
Cash and cash equivalents, beginning of period	66,993	82,063
Cash and cash equivalents, end of period	\$ 45,114	\$ 65,409
Supplemental disclosure of cash flow information:		
Interest paid, net of amounts capitalized	\$ 14,416	\$ 17,054

See accompanying notes to condensed consolidated financial statements.

Table of Contents**Hawaiian Telcom Holdco, Inc.****Condensed Consolidated Statement of Changes in Stockholders Equity**

(Unaudited, dollars in thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders Equity
Balance, January 1, 2013	10,291,897	\$ 103	\$ 165,941	\$ (28,450)	\$ 139,266	\$ 276,860
Stock based compensation			1,886			1,886
Sale of stock under warrants	297					
Common stock issued for stock compensation plans, net of shares withheld and withholding paid for employee taxes	46,543		(426)			(426)
Net income					7,859	7,859
Other comprehensive income, net of tax				382		382
Balance, September 30, 2013	10,338,737	\$ 103	\$ 167,401	\$ (28,068)	\$ 147,125	\$ 286,561
Balance, January 1, 2012	10,190,526	\$ 102	\$ 164,328	\$ (57,518)	\$ 29,284	\$ 136,196
Stock based compensation			1,343			1,343
Common stock issued for stock compensation plans, net of shares withheld and withholding paid for employee taxes	56,109		(53)			(53)
Net income					11,343	11,343
Other comprehensive income, net of tax				33,646		33,646
Balance, September 30, 2012	10,246,635	\$ 102	\$ 165,618	\$ (23,872)	\$ 40,627	\$ 182,475

See accompanying notes to condensed consolidated financial statements.

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Hawaiian Telcom Holdco, Inc.

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Description of Business

Business Description

Hawaiian Telcom Holdco, Inc. and subsidiaries (the Company) is the incumbent local exchange carrier for the State of Hawaii with an integrated telecommunications network. The Company offers a variety of telecommunication services to residential and business customers in Hawaii including local telephone, network access and data transport, long distance, Internet, television and wireless phone service. The Company also provides communications equipment sales and maintenance, and network managed services.

Organization

The Company has one direct wholly-owned subsidiary, Hawaiian Telcom Communications, Inc. which has two direct wholly-owned subsidiaries Hawaiian Telcom, Inc. and Hawaiian Telcom Services Company, Inc. Hawaiian Telcom, Inc. operates the regulated incumbent local exchange carrier and Hawaiian Telcom Services Company, Inc. operates all other businesses.

2. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America. Certain information and disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted and condensed. In the opinion of the Company's management, all adjustments (consisting of only normal and recurring accruals) have been made to present fairly the financial position, the results of operations and cash flows for the periods presented. The results of operations for the periods presented are not necessarily indicative of the results to be expected for the full year. Although the Company believes that the disclosures are adequate to make the information presented not misleading, these financial statements should be read in conjunction with the Company's audited consolidated financial statements as of and for the year ended December 31, 2012.

Cash and Cash Equivalents

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Cash and cash equivalents include cash and money market accounts with maturities at acquisition of three months or less. The majority of cash balances at September 30, 2013 are held in one bank in demand deposit accounts.

Supplemental Non-Cash Investing and Financing Activities

Accounts payable included \$6.2 million and \$2.4 million at September 30, 2013 and 2012, respectively, for additions to property, plant and equipment.

Taxes Collected from Customers

The Company presents taxes collected from customers and remitted to governmental authorities on a gross basis, including such amounts in the Company's reported operating revenues. Such amounts represent primarily Hawaii state general excise taxes and HPUC fees. Such taxes and fees amounted to \$1.9 million and \$5.6 million for the three and nine months ended September 30, 2013 and \$1.6 million and \$5.3 million for the three and nine months ended September 30, 2012, respectively.

Table of Contents***Earnings per Share***

Basic earnings per share is based on the weighted effect of all common shares issued and outstanding, and is calculated by dividing earnings by the weighted average shares outstanding during the period. Diluted earnings per share is calculated by dividing earnings, adjusted for the effect, if any, from assumed conversion of all potentially dilutive common shares outstanding, by the weighted average number of common shares used in the basic earnings per share calculation plus the number of common shares that would be issued assuming conversion of all potentially dilutive common shares outstanding. The denominator used to compute basic and diluted earnings per share was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Basic earnings per share - weighted average shares	10,337,488	10,246,335	10,321,905	10,230,719
Effect of dilutive securities:				
Employee and director restricted stock units	173,405	124,301	166,461	124,871
Warrants	695,266	337,818	607,811	302,927
Diluted earnings per share - weighted average shares	11,206,159	10,708,454	11,096,177	10,658,517

The computation of weighted average dilutive shares outstanding excluded restrictive stock units to acquire 18,610 shares and 18,612 shares of common stock for the three and nine month period ended September 30, 2012, respectively. The unrecognized compensation on a per unit basis for these restricted stock units was greater than the average market price of the Company's common stock for the period presented. Therefore, the effect would be anti-dilutive. There was no such exclusion for the three and nine month periods ended September 30, 2013.

3. Acquisitions***SystemMetrics Corporation***

On September 30, 2013, the Company completed its acquisition of all of SystemMetrics Corporation (SystemMetrics) common stock for \$16.3 million. Of the total purchase price, \$11.9 million was payable at closing, net of cash acquired and purchase price adjustments. A balance of \$3.3 million is subject to an earn-out over a three year period. Payment of the earn-out is contingent on SystemMetrics meeting certain performance metrics and continued employment of the SystemMetrics key executive. The purchase transaction has been accounted for as a business combination. For financial reporting purposes, the earn-out will be accounted for as compensation expense as earned.

SystemMetrics provides virtual and physical data center colocation services in the State of Hawaii along with other telecommunication services that are complementary to the Company's operations. Transaction costs amounted to \$0.4 million. These costs were primarily professional fees and recognized as general and administrative expenses as incurred.

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The Company followed the acquisition method of accounting and allocated the purchase price to the tangible and intangible assets acquired and liabilities assumed based on their preliminary fair values, and the estimates and assumptions are subject to change within the measurement period, which is one year from the acquisition date. The excess of the purchase price over those fair values was recorded as goodwill. The following table summarizes the assets acquired and the liabilities assumed (dollars in thousands):

Assets -		
Property and equipment	\$	3,781
Intangible assets		4,380
Goodwill		10,368
Other assets		643
		19,172
Liabilities -		
Current liabilities		3,684
Non-current liabilities		2,304
Deferred income taxes		1,326
		7,314
Net acquisition price	\$	11,858

Because the acquisition occurred on September 30, 2013, the financial results of SystemMetrics had no impact on the Company's consolidated statements of income for the three or nine months ended September 30, 2013.

The fair value of property, plant and equipment was based on the highest and best use of the specific properties. To determine fair value the Company considered and applied primarily the cost approach. This approach considers the amount required to construct or purchase a new asset of equal utility at current prices with adjustments to the value for physical deterioration, functional obsolescence and economic obsolescence. The fair value of intangible assets including the brand name and customer relationship intangibles were based on discounted cash flows from projections of results of operations for SystemMetrics.

The goodwill recognized is attributed to the anticipated synergies to be achieved by combining the operations of the Company and SystemMetrics. The goodwill is not deductible for income tax reporting purposes and is anticipated to be attributed to a newly formed data center segment.

The following unaudited pro forma results of operations are provided for the three and nine months ended September 30, 2013 and 2012 as if the acquisition of SystemMetrics occurred on January 1, 2012. The pro forma combined results of operations have been prepared by adjusting the historical results of the Company to include the historical results of SystemMetrics. Adjustments were made to the historical results for the purchase price allocation which primarily impacts depreciation and amortization, to eliminate the interest on certain debt financing which was not assumed in the purchase, to eliminate certain intercompany revenue between the entities and to reallocate the transaction related expenses from the 2013 to the 2012 periods.

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These supplemental pro forma results of operations are provided for illustrative purposes only and do not purport to be indicative of the actual results that would have been achieved by the combined company for the periods presented or that may be achieved by the combined company in the future. The pro forma results of operations do not include any costs savings or synergies that resulted, or will result, from the acquisition or any estimated costs that will be incurred to integrate SystemMetrics. Future results may vary significantly from the results reflected in this pro forma financial information because of future events and transactions as well as other factors.

The pro forma results are as follows (dollars in thousands):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2013	2012	2013	2012
Revenues	\$ 99,649	\$ 98,512	\$ 296,443	\$ 294,411
Expenses	91,610	87,885	264,808	262,631
Operating income	8,039	10,627	31,635	31,780
Other income (expense)	(4,082)	(5,480)	(18,344)	(21,974)
Income before income tax benefit	3,957	5,147	13,291	9,806
Income tax expense (benefit)	1,301	(298)	4,970	(799)
Net income	\$ 2,656	\$ 5,445	\$ 8,321	\$ 10,605

Wavecom Solutions Corporation

On December 31, 2012, the Company completed its acquisition of Wavecom Solutions Corporation (Wavecom) for \$8.7 million in cash, net of cash acquired and final purchase adjustments. Wavecom provides telecommunication services in the State of Hawaii which are complementary to the Company s operations.

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The Company followed the acquisition method of accounting and allocated the purchase price to the tangible and intangible assets acquired and liabilities assumed based on their preliminary fair values, and the estimates and assumptions are subject to change within the measurement period, which is one year from the acquisition date. The measurement period remains open as of September 30, 2013 as the Company continues to evaluate additional information obtained related to the amount recognized for certain estimated liabilities. The excess of the purchase price over those fair values was recorded as goodwill. During the three months ended March 31, 2013, the Company made adjustments to the preliminary purchase price allocation based on additional information as to the existence and value of certain assets. In addition, the net acquisition price changed with the final purchase adjustments agreed to by the seller. The measurement period adjustments did not have a significant impact on the Company's condensed consolidated statements of income for the nine months ended September 30, 2013. In addition, these adjustments did not have a significant impact on the Company's consolidated balance sheets as of December 31, 2012. Therefore, the Company has not retrospectively adjusted the comparative 2012 financial information presented herein. The adjustments are as follows (dollars in thousands):

	Recognized as of Acquisition	Measurement Period Adjustments	Recognized as of Acquisition As Revised
Assets -			
Property and equipment	\$ 11,898	\$ 876	\$ 12,774
Intangible assets	1,060	(410)	650
Goodwill	1,569	(154)	1,415
Other assets	1,663		1,663
	16,190	312	16,502
Liabilities -			
Current liabilities	2,360		2,360
Payable from Wavcom to the Company	4,037		4,037
Non-current liabilities	1,450		1,450
	7,847		7,847
Net acquisition price	\$ 8,343	\$ 312	\$ 8,655

4. Receivables

Receivables consisted of the following (dollars in thousands):

	September 30, 2013	December 31, 2012
Customers and other	\$ 40,328	\$ 36,713
Allowance for doubtful accounts	(3,622)	(2,631)
	\$ 36,706	\$ 34,082

Table of Contents**5. Long-Lived Assets**

Property, plant and equipment consisted of the following (dollars in thousands):

	September 30, 2013	December 31, 2012
Property, plant and equipment	\$ 705,519	\$ 639,343
Less accumulated depreciation and amortization	(187,645)	(132,146)
	\$ 517,874	\$ 507,197

Depreciation expense amounted to \$19.3 million and \$56.5 million for the three and nine months ended September 30, 2013, respectively. Depreciation expense amounted to \$17.3 million and \$49.9 million for the three and nine months ended September 30, 2012, respectively.

In February 2013, the Company entered into an agreement to sell a parcel of land and warehouse not actively used in the Company's operations for a purchase price of \$13.9 million. The sale was subject to due diligence by the buyer and approval of the Hawaii Public Utilities Commission (HPUC). The HPUC approval was received in May 2013 and the sale was consummated in June 2013. The net proceeds, net of commissions and other costs paid through escrow of \$0.8 million, amounted to \$13.1 million. A gain on the sale of \$6.5 million was recognized in the second quarter of 2013 as management concluded the land sold was not grouped with the assets subject to the composite depreciation method. The HPUC approval requires the Company to spend \$0.3 million on training employees on broadband telecommunication deployment and operation. In addition, the HPUC approval provides for the Company to make improvements to its broadband network in an amount equal to the net proceeds less the training cost commitment. The planned training expenses and network capital spending will be recognized as the costs are incurred.

In January 2013, the Company entered into an agreement to sell most of its radio towers for \$3.6 million. The sale was subject to due diligence by the buyer. In November 2013, the buyer, as a result of a change in its ownership, issued a termination notice of the purchase per the provisions of the agreement.

The gross carrying amount and accumulated amortization of identifiable intangible assets are as follows (dollars in thousands):

	September 30, 2013			December 31, 2012		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
Subject to amortization						
Customer relationships	\$ 21,709	\$ 8,194	\$ 13,515	\$ 17,850	\$ 6,285	\$ 11,565
Trade name and other	320	83	237	210		210
	22,029	8,277	13,752	18,060	6,285	11,775
Not subject to amortization						

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Brand name	27,300		27,300	27,300	27,300
	27,300		27,300	27,300	27,300
	\$ 49,329	\$ 8,277	\$ 41,052	\$ 45,360	\$ 6,285 \$ 39,075

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Amortization expense amounted to \$0.7 million and \$2.0 million for the three and nine months ended September 30, 2013, respectively. Amortization expense amounted to \$0.7 million and \$2.1 million for the three and nine months ended September 30, 2012, respectively. Estimated amortization expense for the next five years and thereafter is as follows (dollars in thousands):

2013 (remaining months)	\$	828
2014		2,896
2015		2,498
2016		2,100
2017		1,703
Thereafter		3,727
	\$	13,752

With the acquisition of SystemMetrics, the Company recognized customer relationship intangibles of \$3.6 million with a useful life of 13 years and a trade name of \$0.1 million with a useful life of four years. The determination of useful lives for customer relationships was based on historical and expected customer attrition rates. The Company will use an accelerated amortization method reflecting the rate of expected customer attrition.

In conjunction with the acquisition of Wavecom, the Company adjusted the carrying value of goodwill in the first quarter of 2013 as further discussed in Note 3. The revised goodwill amounted to \$1.4 million and is included in the wireline segment. In conjunction with the acquisition of SystemMetrics, the Company recognized goodwill of \$10.4 million which is expected to be attributed to the data center colocation services segment.

6. Accrued Expenses

Accrued expenses consisted of the following (dollars in thousands):

	September 30, 2013	December 31, 2012
Salaries and benefits	\$ 12,666	\$ 15,642
Interest	2,541	3,607
Other taxes	1,020	1,288
	\$ 16,227	\$ 20,537

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Long-term debt consists of the following (dollars in thousands):

	Interest Rate at September 30, 2013	Final Maturity	September 30, 2013	December 31, 2012
Term loan	5.00%	June 2019	\$ 299,888	\$ 299,250
Original issue discount			(4,640)	(3,840)
			295,248	295,410
Current			3,000	3,000
Noncurrent			\$ 292,248	\$ 292,410

The term loan outstanding at September 30, 2013 provides for interest at the Alternate Base Rate, a rate which is indexed to the prime rate with certain adjustments as defined, plus a margin of 3.00% or a Eurocurrency rate on deposits of one, two, three or six months but no less than 1.00% per annum plus a margin of 4.00%. The Company has selected the Eurocurrency rate as of September 30, 2013 resulting in an interest rate currently at 5.00%.

The term loan provides for interest payments no less than quarterly. In addition, quarterly principal payments of \$0.8 million are required. The balance of the loan is due at maturity on June 6, 2019. The Company must prepay, generally within three months after year end, 50% or 25% of excess cash flow, as defined. The percent of excess cash flow required for prepayment is dependent on the Company's leverage ratio. The excess cash flow prepayment for the year ended December 31, 2012 amounted to \$2.1 million and was paid in March 2013. The Company must also make prepayments on loans in the case of certain events such as large asset sales.

The Company also has a revolving credit facility which matures on October 3, 2015. The facility has an available balance of \$30.0 million with no amounts drawn as of or for the periods ending September 30, 2013 and 2012. A commitment fee is payable quarterly to the lender under the facility. Interest on amounts outstanding is based on, at the Company's option, the bank prime rate plus a margin of 3.0% to 6.0% or the Eurocurrency rate for one, two, three or six month periods plus a margin of 4.0% to 5.5%. The margin is dependent on the Company's leverage, as defined in the agreement, at the time of the borrowing.

Refinancing 2013

In June 2013, the Company refinanced its term loan debt. The Company paid a premium on the repayment of the old term loan of \$3.0 million. In addition, the Company paid \$3.4 million in underwriting fees and legal costs. The premium on repayment of debt, existing original issue discount, existing deferred financing costs, underwriting fees and legal costs were accounted for in accordance with accounting standards for modification of debt instruments with different terms. The Company compared each syndicated lenders' loan under the old term loan with the syndicated lenders' loan under the new term loans. For loans under the new term loan that were substantially different, the Company recognized the exchange of debt instruments as a debt extinguishment. For loans under the new term loan that were not substantially different, the Company accounted for the exchange of debt instruments as a modification. As a result of the refinancing, the Company deferred \$2.7 million of financing

related costs and recognized a loss on early extinguishment of debt of \$3.7 million.

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Refinancing 2012

In connection with the February 2012 refinancing of the term loan debt, the Company paid a premium on the repayment of the old term loan of \$6.0 million. In addition, the Company paid \$4.1 million in underwriting fees and legal costs. The premium on repayment of debt, and underwriting fees and legal costs were accounted for in accordance with accounting standards for modification of debt instruments with different terms. The Company compared each syndicated lenders' loan under the old term loan with the syndicated lenders' loan under the new term loans. For loans under the new term loan that were substantially different, the Company recognized the exchange of debt instruments as a debt extinguishment. For loans under the new term loan that were not substantially different, the Company accounted for the exchange of debt instruments as a modification. As a result of the refinancing, the Company capitalized \$5.0 million of the premium on the repayment of debt and refinancing fees and expensed the remainder resulting in a loss on early extinguishment of debt of \$5.1 million.

Maturities

The annual requirements for principal payments on long-term debt as of September 30, 2013 are as follows (dollars in thousands):

Year ended December 31,		
2013 (remainder of year)	\$	750
2014		3,000
2015		3,000
2016		3,000
2017		3,000
Thereafter		287,138
	\$	299,888

8. Employee Benefit Plans

The Company sponsors a defined benefit pension plan, with benefits frozen as of March 1, 2012, and postretirement health and life insurance benefits for union employees. The Company also sponsors a cash balance pension plan for nonunion employees, with benefits frozen as of April 1, 2007, and certain management employees receive postretirement health and life insurance under grandfathered provisions of a terminated plan.

The Company amended its union pension plan on January 24, 2012 for the freeze of benefits effective March 1, 2012. This resulted in a reduction of the projected benefit obligation by \$30.2 million which is the difference between the accumulated benefit obligation and projected benefit obligation at that date. The liability as of January 24, 2012 was measured using a discount rate of 4.54%. The union pension trust assets were also measured as of this date. The reduction in the net recorded liability of \$33.4 million was used to offset actuarial losses previously recognized in accumulated other comprehensive loss.

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The Company accrues the costs of pension and postretirement benefits over the period from the date of hire until the date the employee becomes fully eligible for benefits. The following provides the components of benefit costs for the three and nine months ended September 30, 2013 and 2012 (dollars in thousands):

Pension

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Service cost (benefit)	\$	\$ (50)	\$	\$ 1,488
Interest cost	2,055	2,557	6,166	7,493
Expected asset return	(2,934)	(2,890)	(8,804)	(8,601)
Amortization of loss	148	131	444	373
Net periodic benefit cost	\$ (731)	\$ (252)	\$ (2,194)	\$ 753

Other Postretirement Benefits

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Service cost	\$ 277	\$ 221	\$ 832	\$ 724
Interest cost	516	576	1,548	1,772
Amortization of loss	74	7	223	88
Net periodic benefit cost	\$ 867	\$ 804	\$ 2,603	\$ 2,584

The Company previously disclosed in its consolidated financial statements for the year ended December 31, 2012 that it expected to contribute \$12.1 million to its pension plan in 2013. As of September 30, 2013, the Company has contributed \$9.4 million. The Company presently anticipates contributing the full amount during the remainder of 2013.

9. Income Taxes

The income tax provision differs from the amounts determined by applying the statutory federal income tax rate of 34% to the income before income tax provision for the following reasons (dollars in thousands):

Three Months Ended
September 30,

Nine Months Ended
September 30,

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	2013	2012	2013	2012
Income tax provision at statutory rate	\$ 1,303	\$ 1,843	\$ 4,549	\$ 3,739
Increase (decrease) resulting from:				
State income taxes, net of federal income tax	(86)	137	122	208
Other	554		850	
Valuation allowance		(2,174)		(4,293)
Income tax provision (benefit)	\$ 1,771	\$ (194)	\$ 5,521	\$ (346)

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Through December 31, 2012, the Company maintained a full valuation allowance over its net deferred income tax assets. Based on consistent earnings after its 2010 emergence from Chapter 11 through December 31, 2012, the Company released its valuation allowance as of that date. For the three months and nine months ended September 30, 2012, the existence of the full valuation allowance resulted in an income tax benefit reflecting certain tax credits.

The Company evaluates its tax positions for liability recognition. As of September 30, 2013, the Company had no unrecognized tax benefits. No interest or penalties related to tax assessments were recognized in the Company's condensed consolidated statements of income for the three and nine months ended September 30, 2013 or 2012. All tax years from 2009 remain open for both federal and Hawaii state purposes.

On September 13, 2013, the Treasury Department and the Internal Revenue Service issued regulations that provide guidance with respect to the treatment of materials and supplies, capitalization of amounts paid to acquire or produce tangible property, and the determination of whether an expenditure with respect to tangible property is a deductible repair or must be capitalized. The Company evaluated the impact of the new regulations and concluded that the new regulations will not have a significant impact on its consolidated financial statements.

10. Stock Compensation

The Company has an equity incentive plan. The Compensation Committee of the Company's Board of Directors may grant awards under the plan in the form of incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units and other stock-based awards. The maximum number of shares issuable under the new equity incentive plan is 1,400,000 shares. All grants under the equity incentive plan will be issued to acquire shares at the fair value on date of grant.

As of September 30, 2013, all awards were restricted stock units. Activity with respect to outstanding restricted stock units for the nine months ended September 30, 2013 and 2012 was as follows:

	Shares	Weighted-Average Grant-Date Fair Value
2013		
Nonvested at January 1, 2013	223,224	\$ 15
Granted	181,330	20
Vested	(67,233)	17
Forfeited	(22,918)	17
Nonvested at September 30, 2013	314,403	\$ 17
2012		
Nonvested at January 1, 2012	248,951	\$ 17
Granted	118,647	16
Vested	(59,264)	26
Forfeited	(19,205)	26
Nonvested at September 30, 2012	289,129	\$ 15

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The Company recognized compensation expense of \$0.7 million and \$1.9 million for the three and nine months ended September 30, 2013, respectively. The Company recognized compensation expense of \$0.5 million and \$1.3 million for the three and nine months ended September 30, 2012, respectively. The fair value as of the vesting date for the restricted stock units that vested during the nine months ended September 30, 2013 and 2012 was \$1.3 million and \$1.0 million, respectively. Upon vesting, unit holders have the option to net share-settle to cover the required withholding tax and the remaining amount is converted into an equivalent number of shares of common stock. The total shares withheld were 20,692 and 3,160 for the nine months ended September 30, 2013 and 2012, respectively, and were based on the value of the restricted stock units as determined by the Company's closing stock price. Total payments for the employees' tax obligations to the tax authorities were \$0.4 million and less than \$0.1 million for the nine months ended September 30, 2013 and 2012, respectively. Other than reimbursements for tax withholdings, there was no cash received under all share-based arrangements.

11. Other Comprehensive Income

Reclassifications out of accumulated other comprehensive income (loss) for the three months and nine months ended September 30, 2013 and 2012 were as follows (dollars in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Retirement plans				
Amortization of loss	222	138	667	461
Income tax charge on comprehensive income	(88)		(263)	
Net of tax	\$ 134	\$ 138	\$ 404	\$ 461

The amortization of loss was recognized primarily in selling, general and administrative expense for both the nine months ended September 30, 2013 and 2012.

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12. Commitments and Contingencies

Collective Bargaining Agreement

The Company maintains a collective bargaining agreement with the International Brotherhood of Electrical Workers Local 1357 (IBEW). The agreement covers approximately half of the Company's work force. In December 2012, the IBEW announced their members had ratified a new collective bargaining agreement with the Company with an effective date of January 1, 2013 for a term of five years.

Third Party Claims

In the normal course of conducting its business, the Company is involved in various disputes with third parties, including vendors and customers. The outcome of such disputes is generally uncertain and subject to commercial negotiations. The Company periodically assesses its liabilities in connection with these matters and records reserves for those matters where it is probable that a loss has been incurred and the loss can be reasonably estimated. Based on management's most recent assessment, the Company believes that the risk of loss in excess of liabilities recorded is not material for all outstanding claims and disputes and the ultimate outcome of such matters will not have a material adverse effect on the Company's results of operations, cash flows or financial position.

Litigation

The Company is involved in litigation arising in the normal course of business. The outcome of this litigation is not expected to have a material adverse impact on the Company's condensed consolidated financial statements.

13. Fair Value of Financial Instruments

The following method and assumptions were used to estimate the fair value of each class of financial instruments for which it is practical to estimate the fair value.

Cash and cash equivalents, accounts receivable and accounts payable The carrying amount approximates the fair value. The valuation is based on settlements of similar financial instruments all of which are short-term in nature and generally settled at or near cost. Cash is measured as Level 1.

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Investment securities The fair value of investment securities is based on quoted market prices. Investment securities are included in other assets on the condensed consolidated balance sheets.

Debt The fair value of debt is based on the value at which the debt is trading among holders.

The estimated fair value of financial instruments is as follows (dollars in thousands):

	Carrying Value		Fair Value
September 30, 2013			
Assets - investment in U.S. Treasury obligations (Level 1)	\$ 891	\$	891
Liabilities - long-term debt (carried at amortized cost, Level 2)	295,248		300,638
December 31, 2012			
Assets - investment in U.S. Treasury obligations (Level 1)	\$ 905	\$	905
Liabilities - long-term debt (carried at amortized cost, Level 2)	295,410		302,000

Fair Value Measurements

Fair value for accounting purposes is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price).

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Accounting standards establish a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement).

Assets measured at fair value on a recurring basis represent investment securities included in other assets. Liabilities carried at cost with fair value disclosure on a recurring basis represent long-term debt. A summary is as follows (dollars in thousands):

	September 30, 2013	December 31, 2012
Asset value measurements using:		
Quoted prices in active markets for identical assets (Level 1)	\$ 891	\$ 905
Significant other observable inputs (Level 2)		
Significant unobservable inputs (Level 3)		
	\$ 891	\$ 905
Liability value measurements using:		
Quoted prices in active markets for identical liabilities (Level 1)	\$	\$
Significant other observable inputs (Level 2)	300,638	302,000
Significant unobservable inputs (Level 3)		
	\$ 300,638	\$ 302,000

Assets and liabilities measured at fair value on a non-recurring basis for the nine months ended September 30, 2013 represent those recognized in conjunction with the acquisition of SystemMetrics as of September 30, 2013. A summary of the valued assets and liabilities is included in Note 3 including a discussion of the valuation methodology. The majority of assets and liabilities were valued using level 3 unobservable inputs.

14. Segment Information

The Company operates in two reportable segments (Wireline Services and Other) based on how resources are allocated and performance is assessed by the Company's Chief Executive Officer, the Company's chief operating decision maker. The Wireline Services segment provides local telephone service including voice and data transport, enhanced custom calling features, network access, directory assistance and private lines. In addition, the Wireline Services segment provides Internet, long distance services, television, managed services, customer premise equipment, data solutions, billing and collection, and pay telephone services.

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The following table provides operating financial information for the Company's two existing reportable segments (dollars in thousands):

	Wireline Services	Other	Intersegment Elimination	Total
For the three months ended September 30, 2013				
Operating revenues				
Local voice and other retail services	\$ 64,809	\$ 1,061	\$ (385)	\$ 65,485
Network access services	32,197			32,197
	\$ 97,006	\$ 1,061	\$ (385)	\$ 97,682
Depreciation and amortization	\$ 19,974		\$	\$ 19,974
Net income	1,922	139		2,061
For the nine months ended September 30, 2013				
Operating revenues				
Local voice and other retail services	\$ 190,919	\$ 3,236	\$ (1,152)	\$ 193,003
Network access services	97,640			97,640
	\$ 288,559	\$ 3,236	\$ (1,152)	\$ 290,643
Depreciation and amortization	\$ 58,532		\$	\$ 58,532
Net income	7,297	562		7,859
Capital expenditures	68,599			68,599
Assets as of December 31, 2012	\$ 784,585	\$ 507	\$	\$ 785,092
For the three months ended September 30, 2012				
Operating revenues				
Local voice and other retail services	\$ 63,721	\$ 1,114	\$ (309)	\$ 64,526
Network access services	32,121			32,121
	\$ 95,842	\$ 1,114	\$ (309)	\$ 96,647
Depreciation and amortization	\$ 18,023		\$	\$ 18,023
Net income	5,557	58		5,615
For the nine months ended September 30, 2012				
Operating revenues				
Local voice and other retail services	\$ 188,806	\$ 3,598	\$ (1,028)	\$ 191,376
Network access services	97,534			97,534
	\$ 286,340	\$ 3,598	\$ (1,028)	\$ 288,910
Depreciation and amortization	\$ 51,965		\$	\$ 51,965
Net income	10,920	423		11,343
Capital expenditures	59,409			59,409

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**Item 2. Management's Discussion and Analysis of
Financial Condition and Results of Operations**

Forward-Looking Statements

This quarterly report contains forward-looking statements. These statements relate to future events or our future financial performance (including our anticipated cost structure) and involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as may, should, expects, intends, plans, anticipates, believes, estimates, predicts, potential, continues, assumption or the use of other comparable terminology. These statements (including statements related to our anticipated cost structure) are only predictions. Actual events or results may differ materially from those anticipated or projected due to a number of factors. These factors include, but are not limited to:

- our ability to execute our strategic plan;
- failures in critical back-office systems and IT infrastructure;
- our ability to maintain arrangements with third-party service providers;
- changes in regulations and legislation applicable to providers of telecommunications services;
- changes in demand for our products and services;
- our ability to integrate recent business acquisitions;
- technological changes affecting the telecommunications industry; and
- our indebtedness could adversely affect our financial condition.

These and other factors may cause our actual results to differ materially from any forward-looking statement. Refer to our Annual Report on Form 10-K for a detailed discussion of risks that could materially adversely affect our business, financial condition or results of operations. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also materially adversely affect our business operations.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. These forward-looking statements are made as of the date of issuance of these quarterly condensed consolidated financial statements, we assume no obligation to update or revise them or to provide reasons why actual results may differ.

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We do not undertake any responsibility to release any revisions to these forward-looking statements to take into account events or circumstances that occur after the date of issuance of these quarterly condensed consolidated financial statements. Additionally, we do not undertake any responsibility to update you on the occurrence of any unanticipated events which may cause actual results to differ from those expressed or implied by the forward-looking statements contained in this quarterly report.

Background

In the following discussion and analysis of financial condition and results of operations, unless the context otherwise requires, we, us or the Company refers, collectively, to Hawaiian Telcom Holdco, Inc. and its subsidiaries.

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Segments and Sources of Revenue

We operate in two reportable segments (Wireline Services and Other) based on how resources are allocated and performance is assessed by our chief operating decision maker. Our chief operating decision maker is our Chief Executive Officer.

Wireline Services

The Wireline Services segment derives revenue from the following sources:

Local Voice Services We receive revenue from providing local exchange telephone services. These revenues include monthly charges for basic service, local private line services and enhanced calling features.

Network Access Services We receive revenue for access to our network for wholesale carrier data, business customer data including Dedicated Internet Access, switched carrier access and subscriber line charges imposed on end users. Switched carrier access revenue compensates us for origination, transport and termination of calls for long distance and other interexchange carriers.

Long Distance Services We receive revenue from providing long distance services to our customers.

High-Speed Internet (HSI) Services We provide HSI to our residential and business customers.

Video Services Our video services marketed as Hawaiian Telcom TV is an advanced entertainment service offered to customers in select areas.

Equipment and managed services We provide installation and maintenance of customer premise equipment as well as managed service for customer telephone and IT networks.

Other

We receive revenue from wireless services, including the sale of wireless handsets and other wireless accessories.

Table of Contents**Results of Operations for the Three and Nine Months Ended September 30, 2013 and 2012***Operating Revenues*

The following tables summarize our volume information as of September 30, 2013 and 2012, and our operating revenues for the three and nine months ended September 30, 2013 and 2012. For comparability, we also present volume information as of September 30, 2013 compared to June 30, 2013.

Volume Information

September 2013 compared to September 2012

	September 30, 2013	September 30, 2012	Number	Change	Percentage
Voice access lines					
Residential	190,013	207,732	(17,719)		-8.5%
Business (1)	194,623	185,849	8,774		4.7%
Public	4,246	4,467	(221)		-4.9%
	388,882	398,048	(9,166)		-2.3%
High-Speed Internet lines					
Residential	90,253	86,570	3,683		4.3%
Business	19,163	18,260	903		4.9%
Wholesale	986	1,014	(28)		-2.8%
	110,402	105,844	4,558		4.3%
Long distance lines					
Residential	119,096	128,760	(9,664)		-7.5%
Business (1)	79,320	75,529	3,791		5.0%
	198,416	204,289	(5,873)		-2.9%
Video					
Subscribers	15,796	8,444	7,352		87.1%
Homes Enabled	111,000	59,422	51,578		86.8%

(1) Business voice access lines and business long distance lines included approximately 11,000 and 6,100, respectively, as of September 30, 2013 related to the acquisition of Wavecom.

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September 2013 compared to June 2013

	September 30, 2013	June 30, 2013	Number	Change	Percentage
Voice access lines					
Residential	190,013	194,365	(4,352)		-2.2%
Business	194,623	195,756	(1,133)		-0.6%
Public	4,246	4,291	(45)		-1.0%
	388,882	394,412	(5,530)		-1.4%
High-Speed Internet lines					
Residential	90,253	89,737	516		0.6%
Business	19,163	18,986	177		0.9%
Wholesale	986	998	(12)		-1.2%
	110,402	109,721	681		0.6%
Long distance lines					
Residential	119,096	121,591	(2,495)		-2.1%
Business	79,320	79,956	(636)		-0.8%
	198,416	201,547	(3,131)		-1.6%
Video					
Subscribers	15,796	13,618	2,178		16.0%
Homes Enabled	111,000	100,000	11,000		11.0%

Operating Revenues (dollars in thousands)

For Three Months

	Three Months Ended September 30,		Change	Percentage
	2013	2012	Amount	
Wireline Services				
Local voice services	\$ 34,195	\$ 35,257	\$ (1,062)	-3.0%
Network access services				
Business data	6,282	4,600	1,682	36.6%
Wholesale carrier data	14,850	15,676	(826)	-5.3%
Subscriber line access charge	9,442	9,619	(177)	-1.8%
Switched carrier access	1,623	2,226	(603)	-27.1%
	32,197	32,121	76	0.2%
Long distance services	6,091	6,735	(644)	-9.6%
High-Speed Internet	9,999	9,013	986	10.9%
Video	3,717	1,528	2,189	143.3%
Equipment and managed services	7,228	8,715	(1,487)	-17.1%
Other	3,579	2,472	1,107	44.8%
	97,006	95,841	1,165	1.2%

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Wireless	676	806	(130)	-16.1%
	\$ 97,682	\$ 96,647	\$ 1,035	1.1%
Channel				
Business	\$ 42,739	\$ 41,618	\$ 1,121	2.7%
Consumer	35,298	34,486	812	2.4%
Wholesale	16,473	17,634	(1,161)	-6.6%
Other	3,172	2,909	263	9.0%
	\$ 97,682	\$ 96,647	\$ 1,035	1.1%

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For Nine Months

	Nine Months Ended September 30,		Amount	Change	Percentage
	2013	2012			
Wireline Services					
Local voice services	\$ 103,859	\$ 106,684	\$ (2,825)		-2.6%
Network access services					
Business data	18,885	14,152	4,733		33.4%
Wholesale carrier data	45,123	47,310	(2,187)		-4.6%
Subscriber line access charge	28,507	29,211	(704)		-2.4%
Switched carrier access	5,125	6,861	(1,736)		-25.3%
	97,640	97,534	106		0.1%
Long distance services	18,804	21,342	(2,538)		-11.9%
High-Speed Internet	29,495	26,948	2,547		9.5%
Video	8,784	3,060	5,724		187.1%
Equipment and managed services	19,724	23,604	(3,880)		-16.4%
Other	10,253	7,168	3,085		43.0%
	288,559	286,340	2,219		0.8%
Wireless	2,084	2,570	(486)		-18.9%
	\$ 290,643	\$ 288,910	\$ 1,733		0.6%
Channel					
Business	\$ 125,820	\$ 123,481	\$ 2,339		1.9%
Consumer	104,794	102,778	2,016		2.0%
Wholesale	50,248	53,903	(3,655)		-6.8%
Other	9,781	8,748	1,033		11.8%
	\$ 290,643	\$ 288,910	\$ 1,733		0.6%

The decrease in local services revenues was caused primarily by the decline of \$2.0 million and \$5.7 million of voice access lines for the three and nine month periods, respectively. This was offset by \$0.9 million and \$2.9 million of revenue for the three and nine month periods, respectively, from Wavecom customers acquired in December 2012. Continued competition in the telecommunications industry has increasingly resulted in customers using technologies other than traditional phone lines for voice and data. Residential customers are increasingly using wireless services in place of traditional wireline phone services as well as moving local voice service to VoIP technology offered by competitors. Generally, VoIP technology offered by cable providers is less expensive than traditional wireline phone service, requiring us to respond with more competitive pricing. Additionally, Competitive Local Exchange Carriers (CLECs) and our cable competitor continue to focus on business customers and selling services to our customer base.

In an effort to slow the rate of line loss, we are continuing retention and acquisition programs, and are increasingly focusing efforts on bundling of services. We have instituted various saves campaigns designed to focus on specific circumstances where we believe customer churn is controllable. These campaigns include targeted offers to at risk customers as well as other promotional tools designed to enhance customer retention. We also emphasize win-back and employee referral programs. Additionally, we are intensifying our efforts relative to developing tools and training to enhance our customer service capability to improve customer retention and growth.

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Business data revenue for the three and nine months ended September 30, 2013 increased when compared to the prior year period because of \$1.2 million and \$3.8 million, respectively, of revenue from Wavecom customers acquired in December 2012. Wholesale carrier revenue decreased because of revenues received from Wavecom in 2012 which we no longer recognize as Wavecom is a wholly-owned subsidiary. In addition, the impact of the decline in voice access lines is reflected in subscriber line access charges and switched carrier access charges.

The decrease in long distance revenue was primarily because of the decline in long distance lines and customers moving to wireless and VoIP based technologies for long distance calling.

HSI revenues increased when compared to the prior year primarily because of an approximate 4.3% growth in our HSI subscribers as well as improved revenue per subscriber with increased bandwidth offerings.

On July 1, 2011, we commercially launched our video service on the island of Oahu. We are rolling out Hawaiian Telcom TV to selected areas to ensure delivery of superior service and an ongoing excellent customer experience. Our volume is ramping up as more homes become enabled for video service. We expect to expand both the availability and the capabilities of our Hawaiian Telcom TV service over the next several years through additional capital investment and innovation.

Equipment and managed services sales have decreased for the three and nine month periods because of changes in the volume of sales and installations of customer premise equipment for certain large government customers during the three and nine months ended September 30, 2013 compared to the same periods in the prior year. Revenue from equipment sales varies from period to period based on the volume of large installation projects. The volume of such projects in future periods is uncertain.

The increase in other wireline services revenue for the three and nine months ended September 30, 2013 compared to the same periods in the prior year is because of revenue from Wavecom of \$0.4 million and \$1.2 million, respectively. In addition, business VoIP equipment usage fees amounted to \$0.6 million and \$1.4 million for the three and nine months ended September 30, 2013 and were negligible in the prior year periods.

Wireless revenues declined when compared to the same periods in the prior year as there has been a reduction in marketing effort as we focus on other products.

SystemMetrics

The acquisition of SystemMetrics increases the scale and scope of our data center operations by adding a state-of-the-art facility in Honolulu with up to 6,500 square feet of data center capacity and room for expansion. SystemMetrics currently generates annual revenues of approximately \$8.0 million. With the acquisition, we anticipate marketing an expanded bundle of communication and data products to our business customers that includes enhanced physical and virtual colocation services.

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The following tables summarize our costs and expenses for the three and nine months ended September 30, 2013 compared to the costs and expenses for the three and nine months ended September 30, 2012 (dollars in thousands):

For Three Months

	Three Months Ended September 30,		Amount	Change	Percentage
	2013	2012			
Cost of revenues (exclusive of depreciation and amortization)	\$ 41,829	\$ 41,176	\$ 653		1.6%
Selling, general and administrative expenses	27,965	26,547	1,418		5.3%
Depreciation and amortization	19,974	18,023	1,951		10.8%