Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Application for Transfer of Certain Verizon	)	WC Docket No. 07-22
Spectrum Licenses in Maine, New	)	
Hampshire and Vermont to FairPoint	)	

Reply Comments of the Communications Workers of America International Brotherhood of Electrical Workers

Kenneth R. Peres, PhD.
George Kohl
501 Third St. N.W.
Washington, D.C. 20001
(202) 434-1185 (phone)
(202) 434-1201 (fax)
kperes@cwa-union.org

Edwin D. Hill
900 Seventh St. N.W.
Washington, D.C. 20001
(202-728-6021)
(202-728-6157)

May 11, 2007

Table of Contents

I. INTRODUCTION

The financial and operational risks involved with the proposed purchase of Verizon's Maine, New Hampshire and Vermont (NNE) operations by FairPoint overwhelm any purported benefits. FairPoint, already a highly leveraged company, will have great difficulty meeting the significantly greater dividend and debt commitments that will result from this transaction while simultaneously investing enough capital to maintain current plant, improve service quality, set up entirely new operational, administrative and billing systems, hire more workers and expand broadband availability.

The Commission should address the significant risks that will result from this transaction. Consumers will bear the cost in the form of higher rates and/or worse service when FairPoint proves unable to operate the NNE exchanges successfully and efficiently. Workers will bear the costs in the form of lost jobs, benefits and job security. Communities will suffer due to a lack of capital and labor resources allocated to the build-out of technologically advanced and affordable broadband infrastructure. More than three million residents in the three states are dependent on the Commission to ensure that the public interest is protected.

The arguments presented by FairPoint and Verizon (Applicants) in their *Opposition to Petitions to Deny*[1] have exacerbated instead of allayed our concerns. The Applicants continue to argue against a full merger review by the Commission – even though they actually should welcome such a review if they truly believe their statements about the public interest benefits of the transaction. What are they trying to hide? What are they afraid of? The Applicants continue in their attempt to limit the purview of the

---

[1] WC Docket No. 07-22, *Opposition to Petitions to Deny, Submitted by attorneys for Verizon and FairPoint*, May 7, 2007 (Opposition to Petitions).

Commission by reducing the understanding of "public interest" to competition and concentration. The Applicants continue to address the risks involved in the transaction only in terms of promises and intent – not in terms of enforceable commitments.

The Applicants also continue to oppose the creation of a complete and comprehensive record in this proceeding by attempting to wall off the vital information obtained from the record in the proceedings in the three states. After all, those proceedings could form the most efficient means for the Commission to obtain information about the Applicants' assumptions and projections that form the foundation for their contentions about the public interest benefits of the transaction.

The importance of a comprehensive analysis of projections and assumptions can be illustrated by the MCI/WorldCom merger. In its 1998 evaluation of this merger, the Commission dismissed as "speculative" commentators' analysis of the weakened financial capacity of post-merger MCI WorldCom. Yet, within two years after the Commission granted approval, MCI WorldCom began to implode and precipitated a worldwide depression in the telecommunications sector.

Given the financial and operational weaknesses associated with the proposed sale, the Commission must act on the basis of a comprehensive record and full analysis, with the burden of proof on the Applicants to demonstrate that the proposed transaction serves the public interest. The Commission must evaluate the public interest in terms of "citizenship, character, financial, technical, and other qualifications" of the proposed buyer, and not limit its public interest review to a "lesser showing" as proposed by the Applicants. If the Commission determines, as we believe it will, that the proposed transfer does not serve the public interest, it must either deny the petition or, in the alternative, set hard and specific conditions in terms of capital expenditures, service quality, customer rates, economic development and broadband build out

II. FAIRPOINT – THE FEAR OF COMMITMENT

The basic argument by the Applicants in their *Opposition to Petitions* can be summarized in two words: "Trust Us." FairPoint assures us that they have everything covered. FairPoint promises to increase capital expenditures;[2] improve service quality;[3] significantly expand broadband availability;[4] provide wholesale services to Competitive Local Exchange Carriers (CLECs) seamlessly and without any changes in rates;[5] create 600 additional jobs;[6] and do it all right away at significantly less cost than one of the largest and most experienced telecommunications companies in the world.[7] FairPoint assures us that all this can be done even as it significantly increases its debt and dividend commitments and develops and implements 600 new operational, administrative and support systems.[8]

All this sounds great - who could possibly say no to better service, increased jobs, and more build-out at lower cost?[9] However, there is a significant difference between a "promise" or "intention" and an enforceable commitment.

---

[2] Opposition to Petitions, p. i
[3] op. cit. p. 21
[4] op. cit., pp. ii, 18
[5] op. cit. pp. 32-34.
[6] op. cit., p. ii.
[7] Opposition to Petitions, p. 14
[8] FairPoint Form S-4 filed with the SEC, dated April 7, 2007, section on risk factors.
[9] FairPoint also points to its high level of DSL/broadband access that it has achieved at its current rural carriers (Opposition to Petitions, p. 19). However, as the Commission is well aware, FairPoint and all of its operating subsidiaries enjoy a cost recovery regime for their capital expenditures. Indeed, in it's 2005 10K, FairPoint noted: "Our annual capital expenditures for our rural telephone operations have historically been significant. Because existing regulations allow us to recover our operating and capital costs, plus a reasonable return on our invested capital in regulated telephone assets, capital expenditures have historically constituted an attractive use of our cash flow." (p. 49) While FairPoint actually has a financial incentive to invest in broadband deployment at its existing subsidiaries, it will enjoy no such benefit or incentive at the NNE properties.

FairPoint may have the best intentions in the world - and it is certainly willing to promise just about anything to anyone – but FairPoint balks when asked to turn its promises into a Commission order with enforceable commitments.

> There is likewise no need to micromanage the company's capital expenditures or broadband build-out given FairPoint's **promises** to increase per-line spending and expand broadband access above current levels in the region (emphasis added).[10]

There are good reasons not to trust FairPoint. FairPoint just does not have the technical and managerial experience or the financial wherewithal to step into the shoes of Verizon.

III. FAIRPOINT WILL BE OPERATIONALLY & MANAGERIALLY CHALLENGED

A. FairPoint's Lack of Experience & Expertise

This is a transaction of unprecedented size, scope, and complexity for FairPoint. There is absolutely nothing in the company's corporate history that prepares management for a transaction of this magnitude. FairPoint touts its experience in acquiring "more than thirty companies…", as if the proposed acquisition of Verizon's 1.51 million access lines is just another in a series of similar transactions.[11] However, FairPoint has never had any experience with an acquisition of this size. Indeed, the acquired operations will have 26 times more access lines than the largest local exchange company currently owned by FairPoint.

FairPoint's lack of experience is illustrated by the need to hire an outside consultant to create systems – from scratch - to try to just maintain the level of service that Verizon currently provides. FairPoint's existing systems, and in-house personnel, are

[10] Opposition to Petitions, p. iii.
[11] Op cit., p. 8

woefully inadequate for the task at hand. FairPoint has never done anything like this before and there is no reason to believe that the company can do it now.

FairPoint tries to ignore this vast difference in the scale of acquisitions by attempting to assure the Commission that it has developed "significant in-house expertise in managing dispersed operations."[12] The reality is that FairPoint lacks significant experience or expertise in many of the key areas of the proposed transaction.

- FairPoint management has never had a wholesale customer. They have no systems or experience with interconnection agreements, collocation, wholesale agreements, etc.
- FairPoint management has never provided operator services. Such services were always acquired from Verizon or another large local exchange company (LEC). If this transaction is approved, FairPoint will be the large LEC on which other smaller carriers will rely for operator services.
- FairPoint has never managed a work force of more than few people in each location. If the transaction is approved, FairPoint will have to manage a work force that is more than four times the size of its entire existing work force, spread out over a three-state area.
- FairPoint management has never been responsible for a network of hundreds of thousands of poles, hundreds of wire centers, dozens of central offices - and the need to deploy a work force and other resources over such a vast network.

B. FairPoint's Record of Past Failures Is Particularly Relevant

FairPoint objects to our making an issue of its past experience in areas not directly involving the acquisition of a small rural telephone company. For example, FairPoint attempts to explain its failed CLEC venture by stating that it was "an experiment in a new market… that proved to be ill-timed."[13] However, this was the only time that FairPoint has attempted to develop a business on such a large scale. This is important not because it failed at the CLEC business – it certainly was not alone in that. It is important because FairPoint made an enormous bet on a large-scale operation, losing hundreds of millions

[12] ibid.
[13] Ibid.

of dollars, and wiping out the company's net worth, and then some. Largely as a result of this failed venture, FairPoint's shareholder equity went from $64.4 million in 2000 to a negative $149.5 million in 2001, a negative swing of $213.9 million.[14] The simple truth is that FairPoint's management was not able to manage the scope and complexity of the operation. Yet, this is FairPoint's only experience with any business venture that even begins to approach the size and complexity of the proposed transaction, and it failed miserably. Moreover, five of FairPoint's key officers – Eugene B. Johnson, Walter E. Leach, Jr., Shirley J. Linn, Lisa R. Hood, and Peter G. Nixon – held significant positions at FairPoint during part or this entire financial debacle.[15]

FairPoint also tries to dismiss any reference to its bumbled transition to a centralized and outsourced billing operation in Maine. FairPoint responds that the billing systems fiasco was an "aberration arising from unique circumstances that cannot be expected to occur here."[16] FairPoint attempts to deflect responsibility from itself onto the vendor. However, it was FairPoint that chose the vendor, wrote the contract, failed to oversee properly the work and understand what was going on, and approved the cutover to a new system that wasn't ready.

These experiences foreshadow what could happen with the proposed purchase of Verizon's Maine, New Hampshire and Vermont operations where FairPoint will be dependent on not just one vendor, but dozens. In this situation, FairPoint's contractors will not have just a few people working on one discrete system, but hundreds of contract employees involved with 600 discrete systems – all happening simultaneously. FairPoint never attempted anything close to this before.

---

[14] FairPoint Communications, SEC Form 10K, 2002
[15] FairPoint Communications, SEC Form 10K, 1998, 2001, and 2006
[16] Opposition to Petitions, p. 29.

C. FairPoint's Service Quality Will Erode

FairPoint uses two misplaced arguments in its attempt to dismiss any concerns about its ability to provide quality services in the NNE. The issue is not whether FairPoint provides quality service in its current exchanges, the majority of which serve fewer than 2,500 customers. The relevant issue is whether FairPoint will be able to either maintain or, in some cases, improve upon Verizon's service performance. As detailed extensively in our Petition to Deny, FairPoint has not made any commitment to invest the capital resources needed to improve Verizon's dismal service quality record, especially in relation to clearing out-of-service conditions. Indeed, FairPoint's estimated capital expenditures per line in 2008 will be significantly less than what Verizon invested in its NNE operations in 2006. To make matters even worse, FairPoint will not have the additional financial resources needed to maintain quality service due to the added debt and dividend commitments that management burdened the company with in order to fund the proposed transaction.

The quality of Verizon's service needs to be improved. A recent report by an examiner with the Maine Public Utilities Commission (PUC) stated:

> …a review of Verizon's service quality results during the current AFOR [Alternative Form of Regulation in effect since 2001] reveals that service quality has declined. The increase in missed metrics indicates that Verizon's performance is getting worse. In addition, Verizon has not met the benchmark for Residential Troubles Not Cleared metric during any year of the Second AFOR and often, particularly since 2003/04, it has missed that benchmark by wide margins (more than 50% in excess of the benchmark). Last year and this year, the performance is even worse.[17]

[17] Maine Public Utilities Commission, Docket No. 2005-155, *Examiner's Report (Revenue Requirement and Service Quality Issues)*, May 9, 2007, p. 247.

Verizon's service quality was so poor that the Maine PUC examiner even recommended that the state's service quality measurement and penalty structure be strengthened.

> We address the service quality issue at this time…because we find that certain important aspects of Verizon Maine's service quality are inadequate and also deteriorating. For these reasons, we find that it is necessary to adopt a stronger SQI [Service Quality Index] and rebate/penalty structure now, rather than wait…[18]

In our Petition to Deny we focused on the standard to clear out-of-service troubles within 24 hours. Clearing troubles in a timely manner is critical as a matter of public health and safety. The lack of service for any appreciable time is dangerous especially in the cases of emergencies and accidents. The Applicants' attempted to minimize Verizon's poor out-of-service record by arguing that Verizon's performance was above average.[19] Yet, Verizon's quality of service in terms of out-of-service performance is substantially worse than any other telecommunications operator in the area. For example, for the first quarter of 2007 in Maine, Verizon failed to clear 28% of its out-of-service troubles in 24 hours; the second worst performance was Sidney Telephone which failed to clear 5.8% of its troubles. [20]

The Applicants also tried to minimize Verizon's poor performance by asserting that service in one area is not indicative of poor service in other areas Verizon unsuccessfully attempted to utilize this same argument in the Maine proceeding previously mentioned.

> Verizon argues that…missing a specific metric or standard is not always indicative of a service quality issue. We disagree. As demonstrated by Verizon's performance, when there is one area of weakness, there are often others.[21]

[18] Maine Hearing Examiner Report, p. 8.
[19] Opposition to Petitions, pp. 23-24.
[20] Maine Public Utilities Commission, *Local Telephone Service Quality Reports*, 1st Quarter 2007.
[21] Maine Hearing Examiner Report, p. 8.

Yet, when confronted with the need to improve service quality in Verizon's NNE territory FairPoint reverts to promises and intentions but refuses to make any enforceable commitments to invest the needed capital or to obtain better service measurements.

The Applicants' other misplaced argument focuses on FairPoint's service quality record: specifically, a New York Public Service Commission commendation for service quality.[22] However, FairPoint fails to mention a few salient points. FairPoint's ability to provide commendable service in its relatively small New York subsidiaries does not prove in any way that it will be able to provide commendable service in Verizon's Maine, New Hampshire and Vermont service area. FairPoint's New York subsidiaries are relatively small and had a history of providing good service quality before being acquired by FairPoint.[23] Conversely, Verizon's NNE operations are 41 times the size of FairPoint's largest New York subsidiary and have experienced a very spotty history of service quality.[24]

FairPoint also fails to mention that the New York Public Service Commission (PSC) was so concerned about FairPoint's "relatively weak financial position" that it felt compelled to impose a significant number of conditions when it approved the company's acquisition of Berkshire Telephone Corporation.[25] These conditions were imposed to protect the subsidiary's financial health, capital investment, service quality and consumer rates. The conditions included the following:

- a service quality plan with the suspension of dividend payments and the imposition of customer rebates for substandard service;
- cost savings to flow to consumers;

[22] Opposition to Petitions, pp. 255-56.
[23] New York Public Service Commission, Case 03-C-0972, *Order Approving Merger Subject to Conditions, Issued and Effective March 18, 2005*.
[24] See WC Docket No. 07-22, CWA-IBEW Petition to Deny.
[25] Ibid.

- insure adequate capital investment by limiting dividend payments to the difference between Ebitda and 100% of depreciation expenses;
- limitations on the ability of FairPoint to use Berkshire as a cash cow through limitations on dividend payments, debt and inter-affiliate transactions.

FairPoint accepted the conditions imposed by the NY PSC. It is important to bear in mind that the NY PSC imposed these conditions in the context of a relatively miniscule transaction ($20.3 million and 7,200 access line equivalents) with dramatically smaller attendant risks – both to FairPoint and the business it was acquiring.[26]

IV. FAIRPOINT'S FINANCIAL INSTABILITY UNDERSCORES THE NEED FOR THE COMMISSION TO OBTAIN AS FULL AND COMPLETE A RECORD AS POSSIBLE

The proposed sale also contains significant financial risk. Verizon itself raised significant concerns about FairPoint's viability when it made commitments to pay up to $40 million of FairPoint's transaction costs and have Verizon Wireless purchase FairPoint's 7.5% stake in a wireless subsidiary in New York for $55 million. Thus, Verizon funneled $95 million to FairPoint in order to subsidize almost all of FairPoint's pre-closing transaction costs. However, the Commission, unlike Verizon, must be concerned with FairPoint's financial condition **after** the transaction closes. Consequently, the Commission must identify the significant risks that FairPoint's financial condition pose to the public interest.

[26] FairPoint Communications, SEC Form 10K, 2006

A. FairPoint's High Dividend, Acquisition Strategy Poses Significant Risks

FairPoint presents itself as "Financially Stable and Poised to Operate and Invest" in the Northern New England properties.[27] However, its shareholder equity has declined by over 21% since its Initial Public Offering in early 2005, and by 6.7% during the first quarter of 2007 alone.[28] The underlying reason for this decline in shareholder equity is simple: FairPoint pays out significantly more in dividends than it earns in net income; for 2006, it had net income of $0.88 per share but paid out $1.59 per share in dividends.

FairPoint blithely assures the Commission that its dividend policy "will not drain capital" and argues that dividends "could be reduced if additional funding were necessary."[29] While FairPoint's Board of Directors are certainly authorized to set dividend payments (and may be required, under certain exigencies, to reduce or even eliminate dividends), such an action would certainly have a devastating impact on FairPoint's share price and on the company's ability to raise capital at a reasonable price. FairPoint's dividend yield (currently above 8.5%) is among the highest of any publicly traded equity.[30] One can only imagine the stock market's response to a reduction or elimination in the company's dividends.

One of FairPoint's "strategic objectives" is to "continue to grow by acquisition."[31] Indeed, FairPoint is fundamentally a holding company specializing in a certain type of acquisitions. There can be no doubt that its dividend policy is integrally linked to its

[27] Opposition to Petitions, p. 10

[28] FairPoint Communications, SEC Forms 10Q, 1st Quarter 2005 and 2007. FairPoint's total shareholder equity was $266.7 million at March 31, 2005, $224.7 million at year-end 2006, and $209.7 million at March 31, 2007.

[29] Opposition to Petitions, p. 15

[30] FairPoint's stock closed at $17.76 on May 10, 2007, producing an indicated dividend yield of 8.95%

[31] Walter Leach Declaration, p. 3. Indeed, Mr. Leach's entire job revolves around acquisitions: "I am responsible for all aspects of FairPoint's merger and acquisition activity, as well as strategic planning." Leach declaration, p. 1. Also see Opposition to Petitions, p. 8 and footnote 17.

intrepid acquisition strategy, providing the company with acquisition "currency" and facilitating its ability to raise new capital. In the instant case, more than one-third of the stated consideration for the NNE properties is in the form of FairPoint stock. Absent FairPoint's extremely high dividend level and even with the benefits the Applicants argue accrue to the transaction as a result of the Reverse Morris Trust structure, it seems highly unlikely that Verizon would have even considered FairPoint for this deal.

Since FairPoint has stated that acquisitions will continue to be part of its "strategic objectives" in the future, there will be enormous pressure on the company to maintain its high dividend policy. While FairPoint ***promises*** that its dividend policy will take a back seat to required investments in the Northern New England properties, the Commission should rigorously test the company's ability to keep its promises under a range of scenarios.

B. FairPoint's Ability to Obtain Stated Cost Savings Is Speculative and Risky

FairPoint also argues that it "will achieve significant cost savings" and scoffs at the CWA/IBEW's concerns that it will be unable to achieve the $60 to $75 million in operating expenditures that are the lynch-pin of its entire plan.[32] The CWA/IBEW cannot provide a more specific analysis based on confidential data that it has received through the regulatory proceedings in Maine, New Hampshire and Vermont. However, a straight-forward analysis of publicly available financial data from FairPoint and Verizon Northern New England should undermine any third-party's confidence in FairPoint's braggadocio.

FairPoint asserts that it will be able to obtain the $60 to $75 million by supplying "the services itself, using its own state-of-the-art systems infrastructure and lower

[32] Opposition to Petitions, p. 14

overhead per line, reducing these costs from the levels that FairPoint projects Verizon would have incurred."[33] However, FairPoint's average operating expense per access line for its 31 operating companies significantly exceed that of Verizon's Northern New England companies. For the five years for which comparable data is available (2002-2006), FairPoint's average annual per line operating expense was $108 higher (17.3%) than those for the Verizon Northern New England companies ($736 versus $628 for the five years, $829 versus $718 in 2006). And while FairPoint's average per line operating expenses increased at a slightly lower pace over the 2002-2006 period (5.4% versus 6.1% annually), it's most recent year-over-year, March Quarter 2006 to March Quarter 2007 average operating expense per access line grew by 8.1% (even after deducting the $7.6 million and $2.4 million transaction expenses it incurred during the most recent two quarters).[34]

FairPoint's track record with its own, much more manageable operations undermines its assertion that it will be able to squeeze 22% to 28%[35] out of the Northern New England properties' operating expenses. The fact that its own operations have significantly higher unit (access line) operating expenses, which have risen at a pace that is well above inflation, casts significant doubt on its ability to fulfill its promises.

FairPoint's ability to obtain cost savings can also be undermined by other factors. For example, the Maine Hearing Examiner found that in 2004 Verizon overcharged customers by $32.4 million.[36] While at this writing we do not know what penalties

[33] Opposition to Petitions, pp. 14-15, citing to Leach Declaration at p. 13
[34] FairPoint Communications, SEC Form S-4 and SEC Form 10Q, March 2007 quarter. Comparable data for Northern New England's 1st quarter 2007 is not available.
[35] Based on the newly disclosed $270 million in Verizon-allocated "back office" charges, which represent a 12.5% increase over the 2005 level.
[36] Maine Hearing Examiner Report, p. 273.

and/or remedies the Public Utility Commission will impose, it is clear that one possible outcome would be a significant roll-back in Verizon's Maine's revenue base. This is precisely the type of unplanned event that highlights the risky nature of this proposed transaction. While it would be painful, Verizon clearly has the resources to absorb such a roll-back. On the other hand, FairPoint would be extremely hard pressed to execute its plan (even assuming everything else went perfectly, which we very much doubt will be the case) in the face of such an event.

C. The Commission Should Conduct an Extensive Merger Review Obtaining All Necessary Documents and Thoroughly Analyzing the Applicants' Projections and Assumptions

The Applicants have called the CWA/IBEW financial analysis hypothetical and speculative. However, the analysis is neither. CWA and IBEW were not able to provide a more specific analysis of the proposed transaction because the relevant financial data was obtained under protective orders in the Maine, New Hampshire and Vermont proceedings. FairPoint has not been willing to share the real financial picture with the public or this Commission.

Consequently, the CWA and IBEW urge the Commission to obtain this same information and conduct its own analysis. Neither the Commission nor anyone else should simply rely on FairPoint's unsupported assertions. The Commission must obtain the "real" data and look at the resources FairPoint actually will have as well as carefully examine FairPoint's own projections in relation to line loss, capital expenditures, shareholder equity, and its ability to service its debt and pay its promised dividends. The Commission should conduct a thorough investigation based on the most comprehensive information it can obtain. This would include all the proprietary disclosure agreements that, as admitted by the Applicants, supersede and modify all public documents the Applicants have released. In addition, the Applicants' rationale for the professed pubic interest benefits of the transaction relies upon pro forma statements that are based on questionable assumptions. The Commission could conduct its own comprehensive discovery process and/or benefit from the extensive discovery process taking place in the proceedings before the Maine, New Hampshire and Vermont regulatory commissions.

V. OTHER SUPPOSED PUBLIC INTEREST BENEFITS AND PRECEDENTS CITED BY APPLICANTS ARE SUSPECT

A. Verizon's Tax Avoidance Strategy Harms the Public Interest

One of the great weaknesses of the proposed transaction is the difference in scale and size between FairPoint and the NNE operations. However, the Applicants try to spin this differential as well as the tax free basis of the proposed transaction as a public interest benefit.

> Ironically, some of the benefits of the proposed transaction are directly tied to the disparity in the companies' sizes and market positions. The difference in size permitted the companies to utilize a Reverse Morris Trust to effect their proposed transaction, by which the transaction is expected to qualify as a tax-free transaction.[37]

While the applicants assert that FairPoint received something of a discount on the Northern New England properties in recognition of Verizon's tax savings, neither FairPoint nor Verizon offer any evidence to support this assertion

In this case, the Reverse Morris Trust mechanism has harmed, not benefited, the public interest. Verizon evidently focused its search for a buyer on those companies that would qualify for tax-free treatment per the Reverse Morris Trust (RMT).

---

[37] Opposition to Petitions, pp. 11-12.

> …the value maximizing equation for Verizon is to structure the deal as a Reverse Morris Trust then sell the spin-co to an existing company, with extant management, back office and other required infrastructure to run the combined company so that value is not destroyed in creating such corporate infrastructure. [38]

Unfortunately, FairPoint – while qualifying for the tax –free RMT – does not have the "extant management, back office and other required infrastructure" to run the combined company and, thus, must invest hundreds of millions of dollars extra.

By focusing on tax avoidance, Verizon also undermined the public interest by imposing opportunity costs. Specifically, the Reverse Morris Trust mechanism eliminates from consideration any company with equity that is greater than the value of the deal. Verizon's tax-free emphasis thus precluded any sale to those companies that would actually have the resources, experience and "required infrastructure" to conduct the NNE operations successfully such as Century Tel, Citizens or Windstream.[39]

This transaction appears to have been guided by tax avoidance as opposed to the financial and operational efficacy of the purchaser, i.e., FairPoint. In recognition of FairPoint's weakness, Verizon funneled $95 million through various means in order to subsidize FairPoint's pre-closing transaction costs.

Thus, not only does Verizon avoid $600-$700 million in taxes but also shifts a few hundred million dollars in expenses onto FairPoint to recreate systems that Verizon already possesses. The ratepayers in Maine, New Hampshire and Vermont suffer from a double whammy – they end up subsidizing a transaction that will leave them worse off and facing significantly more risk.

---

[38] Frank Louthan IV, *Verizon: Analyzing Future Line Sales under Reverse Morris Trust Scenarios*, Raymond James Associates, January 20, 2007.
[39] Ibid.

The applicants also cited the Alltel spin-off/Valor merger as a similar type of transaction. However, there are a number of problems with these arguments. The Alltel /Valor deal was a very different type of transaction. Alltel took its entire wireline operation - including all of its back office and support operations - and spun them off into a new company that merged with Valor. That new company, Windstream, was up and running from day one with all of the same back office systems and network operations that used to be part of Alltel. This is not what will happen in FairPoint's acquisition of Verizon's NNE operations. FairPoint and its consultants are going to work for at least a year - and probably much longer - to try to create new systems and operations centers from scratch. They haven't even identified where these operations will be located let alone who will staff them or what they will look like. The only analog is the Hawaii Tel experience that FairPoint does not want to talk about because it went so poorly.

B. FairPoint's Strategy to Obtain a Waiver of the All or Nothing Rule Would Undermine the Public Interest

FairPoint is attempting to "game" the system in another way to increase their private interest while harming the public interest. Specifically, FairPoint has asked for a waiver of the Section 61.41 "all or nothing" price cap rule in connection with its acquisition of Verizon's NNE operations.[40] Section 61.41 provides that any price cap company that acquires, merges with or otherwise becomes affiliated with a price cap company, the acquiring company becomes subject to price cap regulation and must file

[40] Petition of FairPoint Communications, Inc. for Waiver of Sections 61.41(b) and (c) of the Commission's Rules, WC Docket No. 07-66, Feb. 21, 2007 ("Waiver Petition"); FCC Public Notice, Petition of Communications Inc., for a Wavier of the All-Or-Nothing Rules in Connection with Its Acquisition o f Certain Verizon Properties in Maine, New Hampshire, and Vermont, WC Docket No. 07-66, April 4, 2007.

price cap tariffs within a year.[41] Under these rules, FairPoint's acquisition of the Verizon exchanges would obligate FairPoint to become subject to price cap regulation for both its existing and acquired exchanges.

A waiver would allow FairPoint to continue to operate its existing exchanges under rate-of-return regulation after the transaction without converting them to price cap regulation as required by Section 61.41. Granting the petition would allow FairPoint to shift costs among affiliates in order to raise rates on consumers while increasing earnings, outcomes that the Commission's rules are designed to prevent. The Commission has never granted a petition on this scale that would allow an acquiring company to operate some affiliates under rate-of-return regulation and some affiliates under price caps.[42]

VI. CONCLUSION

As recommended in our Petition to Deny, the Commission should conduct an extensive review of the proposed transaction. The Commission should not rely on FairPoint's promises and statements of intent. An extensive review should include a comprehensive analysis of the Applicants' assumptions and projections. One of the most efficient means to obtain the documents and information needed for this analysis is to utilize the record constructed in the proceedings of the regulatory agencies in the three directly affected states where the Applicants' witnesses will be subject to cross examination. If the Commission determines, as we believe it will, that the proposed transaction does not serve the public interest it should deny the petition. In the alternative,

[41] 47 C.F.R. §61.41(c) (2). *See Policy and Rules Concerning Rates for Dominant Carriers,* Second Report and Order, 5FCC Rcd 6786, 6821 (1990), Erratum, 5 FCC Rcd 7664 (Com. Car. Bur. 1990) ("*LEC Price Cap Order),* modified on recon., Order on Reconsideration, 6 FCC Rcd 2637 (1991) ("*LEC Price Cap Reconsideration Order).*

[42] WC Docket No. 07-66, Comments of the Communications Workers of America and International Brotherhood of Electrical Workers, May 4, 2007.

the Commission should construct strict and enforceable conditions that would require FairPoint to adequately invest in infrastructure, protect against FairPoint's ability to treat the NNE operations as a cash cow, limit the amount of debt that can be dumped on the NNE operations, insure that the transition of operational and support systems from Verizon to FairPoint will based on its smooth and efficient functioning for two years, ensure the delivery of quality services and require FairPoint to build out broadband throughout the region as it has promised.

Respectfully Submitted,

George Kohl
Assistant to the President/Director of Research
Communications Workers of America

Edwin D. Hill
International President
International Brotherhood of Electrical Workers

May 11, 2007

DECLARATION OF KENNETH R. PERES

My name is Kenneth R. Peres. I am a Research Economist with the Communications Workers of America. My business address is 501 Third Street N.W., Washington, D.C. 2001.

The Communications Workers of America is a labor organization representing 700,000 workers, working in wireline telecommunications, cable, wireless, broadcasting, construction and maintenance, government, utility, publishing, manufacturing, airlines, higher education, and other public and private sector organizations.

The International Brotherhood of Electrical Workers is a labor organization representing 750,000 workers who work in a wide variety of fields, including utilities, construction, broadcasting, telecommunications, manufacturing, railroads and government.

Together, CWA and IBEW represent 2,800 Verizon workers in Maine, New Hampshire and Vermont.

I am familiar with the contents of the foregoing Reply Comments. The factual assertions made in the Comments are true to the best of my knowledge and belief.

I declare under penalty of perjury that the foregoing is true and correct.
Executed on May 11, 2007.

Kenneth R. Peres

Kenneth R. Peres

CERTIFICATE OF SERVICE

I, Kenneth R. Peres, certify that on this 11th day of May, 2007, I served a true copy of the foregoing Reply Comments by electronic mail (except where indicated) and U.S. Postal Service first class mail, postage prepaid, upon the following:

David Rivard*
40 N. Shore Rd.
Derry, NH 03038

Edwin Hill
900 Seventh Street, NW
Washington, DC 20001

Sumita Mukhoty
Policy Division, International Bureau
Federal Communications Commission
445 Twelfth Street, SW
Washington, DC 20554
Sumita.Mukhoty@fcc.gov

Michael E. Glover
Karen Zacharia
Leslie V. Owsley
VERIZON
1515 North Court House Rd Suite 500
Arlington, VA 22201

Shirley J. Linn
Robin E. Tuttle
FairPoint Communications, INC.
521 E. Morehead Street, Suite 250
Charlotte, NC 28202
(202) 637-2200

Jim Bird
Office of General Counsel
Federal Communications Commission
445 Twelfth Street, SW
Washington, DC 20554
jim.bird@fcc.gov

Adam Kirschenbaum
Competition Policy Division
Wireline Competition Bureau
Federal Communications Commission
445 Twelfth Street, SW
Washington, DC 20554
Adam.Kirschenbaum@fcc.gov

Erin McGrath
Mobility Division
Wireless Telecommunications Bureau
Federal Communications Commission
445 Twelfth Street, SW
Washington, DC 20554
erin.mcgrath@fcc.gov

Nancy J. Victory
Bennett L. Ross
WILEY REIN LLP
1776 K Street, N.W.
Washington, DC 20006
NVictory@wileyrein.com

Karen Brinkmann, Brian W. Murray
Elizabeth R. Park, Kelley M. Marsden
LATHAM & WATKINS LLP
555 Eleventh Street, N.W., Suite 1000
Washington, DC 20004
karen.brinkmann@lw.com

Kenneth R. Peres
Kenneth R. Peres

* U.S. Postal Service only