STATE OF NEW HAMPSHIRE

BEFORE THE

PUBLIC UTILITIES COMMISSION

DOCKET NO. DT 07-011

**Joint Petition of Verizon New England Inc., et al.
and FairPoint Communications, Inc.
Transfer of New Hampshire Assets of
Verizon New England Inc. et al.**

Supplemental Testimony of

John Antonuk

On Behalf of

The Public Utilities Commission

Of New Hampshire

September 10, 2007

Q. Please state your name, employer, business address and position.

A. My name is John Antonuk. My business address is 65 Main Street, P.O. Box 1237, Quentin, Pennsylvania 17083. I am a founder, and serve as the president of The Liberty Consulting Group ("Liberty").

Q. Are you the same John Antonuk who previously filed testimony on behalf of the Staff of the New Hampshire Public Utilities Commission in this proceeding?

A. Yes.

Q. Please describe the purpose of your testimony.

A. The purpose of my testimony is to describe conditions necessary to ensure that the transfer of Verizon's New Hampshire franchise and systems to FairPoint Communications is for the public good. We have reviewed the testimony of the other intervenors, and have compared it with the testimony that I and the other Liberty witnesses (Robert Falcone, Charles King and Randall Vickroy) representing Staff raised regarding the proposed acquisition of the Verizon northern New England assets by FairPoint. We have analyzed our position in light of the other testimony filed. That review and our continuing analysis have allowed us to reach a point where we are able to set forth what we consider to be a comprehensive set of conditions that we believe must be met to support the conclusion that the Commission should approve the transfer of Verizon's New Hampshire local exchange operations to FairPoint.

This testimony provides a description of those conditions, which is consistent with, but more detailed and specific than what our direct testimonies contained. It does not, however, deal at the same level of detail with a number of concerns raised by various

CLECs, electric utilities, municipalities, and other interested parties. We are not at present prepared to take a final position on those concerns, pending further understanding about them, based on discussions with those who have proposed them.

To the extent it proposes a set of conditions that differ from or are hard to rationalize with the concerns other stakeholders have addressed in testimony, one can characterize this filing as rebuttal testimony (as called for in the Commission's procedural schedule). While not arguing with this legal characterization, we see it, in practical terms, more as an effort to integrate certain key concerns raised in this proceeding, to offer a framework designed to overcome those concerns, and to assure that the transfer adequately addresses and protects customer interests.

Q. What is your current recommendation to the Commission as to the approval of this transaction?

A. Based on our analysis, Staff concludes that the risks, particularly with respect to the financial viability of FairPoint, far outweigh the benefits of the transaction as proposed and that in its current form, the transfer from Verizon to FairPoint cannot be found to be for the public good. However, we believe that with the addition of certain protective conditions, the transaction would be in the public interest and we would recommend approval. Exhibit A provides a list of the specific concerns we have about the transaction and the conditions we propose to address each. Each of the conditions needs to be made enforceable and a consequence for not achieving or meeting a commitment should be established before approval.

Q. Please summarize the conclusions of the Staff witnesses regarding the proposed FairPoint acquisition of the Verizon properties.

A. The Staff testimony has identified a number of positive aspects that can bring benefits to New Hampshire. These aspects include FairPoint's potential to focus more effectively than Verizon on meeting the needs of New Hampshire customers and FairPoint management's apparent desire to improve service and offer a wider variety of products and services to New Hampshire's residents and businesses. We continue, however, to have major concerns about FairPoint's ability to deliver on its commitments and expectations, while maintaining a financial condition healthy enough to allow it continuing access to the capital it will take to meet public service responsibilities over the long term. Put simply, FairPoint's financial condition is not strong enough to allow it to thrive except under assumptions far too optimistic for the Commission to rely upon in judging the transfer.

A more realistic view of key operating and financial factors shows that FairPoint will not be able to maintain the financial strength needed to satisfy its lenders or to give confidence that it will continue to have reasonable access to capital markets. FairPoint is in the position of having to rely on foregoing dividends in the event that operating expenses turn out to be higher than it has forecast in this docket. Although we believe that some restrictions can and should be placed on the conditions under which FairPoint would be able to pay dividends to its shareholders, we put no confidence in the notion that foregoing dividends is a satisfactory source of "cushion" for withstanding operating and financial factors not consistent with FairPoint's optimistic assumptions.

FairPoint's financial structure requires a high debt-to-equity ratio and high dividend payouts, which makes it atypical from a traditional telecommunications utility perspective, generally, and certainly far different from what Verizon has used to support

its operations in this region. FairPoint shareowner interest in the company is highly driven by dividends. Believing that the company can maintain investor confidence in the face of large dividend cuts over a potentially indefinite period and with no reasonable assurance about their duration is very problematic. Dividend uncertainties of this type will make attracting equity and debt capital difficult. It clearly does not serve the public interest for the state's major telecommunications provider to begin from a thin financial position that will face severe threat under conditions less optimistic than those that form the basis of FairPoint's financial modeling in this case.

Several witnesses in this proceeding have identified a number of suspect assumptions in FairPoint's financial modeling. The assumptions of particular concern to us involve the following factors:

- The costs that will mount under a Transition Service Agreement (TSA) that may extend significantly past the projected four months after closing that FairPoint claims is sufficient to develop new operations support systems (OSS)
- The assumption that FairPoint will benefit from synergies amounting to over $60 million per year.
- The capital expenses assumed necessary to attain increased broadband availability.
- The capital expenses assumed necessary to attain a satisfactory level of customer service.

The considerations that lead us to question these assumptions cause us also to question the quality of service that FairPoint will be in a position to deliver to customers if these assumptions are not realized.

Q. What are your concerns about FairPoint's OSS development time and the TSA costs?

A. Staff is concerned that FairPoint's assumption that it will cut over to its new, fully developed systems within four months after close is extremely optimistic and places an enormous financial risk on the success of the transfer. As expressed in its direct testimony, Verizon will not make its operations support systems available for FairPoint's use. They are large, complex systems that FairPoint, supported by its contractor, CapGemini, will have to re-create from scratch. FairPoint has not before been required to employ similar systems in its current local exchange operations. The comparatively small size of FairPoint's current operations is underscored by the fact that the acquisition here will increase FairPoint's size by six times. FairPoint's experience in systems development is limited. When it developed a much smaller system (a billing system begun in 2005 to serve its current operations), FairPoint encountered major problems, which it only recently appears to be resolving.

FairPoint's contractor, CapGemini, also has not previously developed systems that support such a comprehensive set of telecommunications functions. This is not surprising, as the only other company that has attempted a similar telecommunications back-office systems development undertaking was Hawaiian Telcom, the acquirer of Verizon's Hawaii operations. Hawaiian Telcom also used a contractor who had not developed such systems before, and that project resulted in a major disaster for the company. Hawaiian Telcom continues to have difficulties associated with the new systems more than two years after its acquisition and a complete change of development vendors.

FairPoint claims it will be able to complete its OSS development within four months after closing, which is only 16 months after first engaging CapGemini. During that period, FairPoint will need to purchase very expensive support from Verizon through the TSA to supply the capabilities that the new systems will ultimately provide. The cost of the TSA amounts to more than $14 million per month plus a one-time charge of $34 million. By contrast, Hawaiian Telcom ended its TSA with Verizon 20 months after first engaging its systems development vendor. Even this period proved far too short; Hawaiian Telcom has experienced major systems problems that it still has not fully resolved. If FairPoint misses its target completion date, the TSA costs will continue to mount.

Although the terms of the TSA provide for reductions (of $500 thousand per month cumulative) in the monthly charges between the ninth and twelfth months after closing, the monthly cost returns to the original amount plus $500 thousand in the thirteenth month, and the monthly charge continues to increase by $500 thousand indefinitely for every month thereafter. This means that the TSA costs that FairPoint now plans to be only around $100 million for four months' use would mount to over $200 million after 12 months and to over $300 million after 18 months. Beyond the risk of debt agreement violation, the resulting financial impact will create an incentive for FairPoint to terminate the TSA prematurely, leading to poor service for New Hampshire customers. The financial impact can also provide a powerful inducement for FairPoint to delay or terminate the measures needed to improve service quality and to extend broadband availability; *i.e.*, key benefits that FairPoint projects under its stewardship.

1 **Q. Please explain your concern that the cost of the TSA can lead FairPoint to terminate**
2 **the TSA prematurely, causing poor service for New Hampshire customers.**
3 A. The recent experience of Hawaiian Telcom, which is the only comparable recent example
4 in the telecommunications industry, suggests that the financial impact of the TSA can
5 lead to decisions that have severe consequences for customers. Like the proposed
6 FairPoint transaction, the Hawaiian Telcom transaction involved the use of a costly TSA
7 with Verizon to provide critical daily operating support between closing and system
8 cutover and with terms that provided a strong incentive to cut over to the newly
9 developed systems as quickly as possible. In the Hawaiian Telcom case, these
10 circumstances led to a premature cutover that produced major systems failures. Poor
11 customer service, significant additional expense for the company, and loss of customers
12 resulted. Such customer losses would exacerbate financial distress that would already be
13 substantial, as a result of the direct increase in TSA expenditures.
14 We understand and are pleased that FairPoint is aware of the problems that
15 Hawaiian Telcom experienced, and is working to avoid them. The team it has assembled,
16 however, has never experienced a transition of this type and magnitude. FairPoint is
17 overly optimistic about its ability to overcome these challenges quickly and
18 economically. The TSA's increasing monthly costs after month 12 and the requirement
19 for all services to be flash cut at one time are particularly troubling. The risk of
20 withdrawal from the TSA before the newly developed systems are fully working is
21 unacceptably high, especially if FairPoint's very optimistic projections of the
22 development timeframes prove to be flawed. Hawaiian Telcom's withdrawal from its

TSA with Verizon occurred four months later than FairPoint is currently planning, when measured from the time both engaged their systems development contractors.

Q. What are your concerns about synergies?

A. As expressed in the direct testimony, FairPoint expects to gain over $60 million per year in efficiencies when it has cut over to its new systems. Verizon operates on a scale that totally dwarfs that of FairPoint by any reasonable measure, even after the acquisition. For example, northern New England represents only about 3.6 percent of Verizon's access lines. This does not even consider Verizon's huge operations in other businesses, such as wireless. FairPoint's ability to gain efficiencies upon losing such economies of scale is very doubtful. At the least, an assumption of synergies should be supported by clear, convincing analysis, which FairPoint has not done. Even more importantly, such an assumption should be balanced against the efficiency losses that will certainly occur. Those losses can come from multiple sources.

First, FairPoint is counting on an existing population of more than 2,700 Verizon employees. In the meantime, those employees could: (a) retire while their post-employment benefits will still come from Verizon, (b) transfer to other Verizon operations in the general geographic region, or (c) resign and look for another job. Many employees currently slated for transfer to FairPoint may avail themselves of those options, and perhaps others. Furthermore, many of the employees who do transfer to FairPoint may not be fully qualified or trained in their jobs, because they may have only recently replaced experienced Verizon employees who elected to retire, resign, or transfer to other Verizon positions. There is evidence that since the announcement of this transaction, the attrition rate among the Verizon employees at stake has been significantly

1 greater than normal. The need to train and integrate into the organization new or less
2 experienced employees will reduce FairPoint's ability to realize synergies.
3 Second, FairPoint must assemble from scratch a team of some 700 people to replace
4 employees who will remain with Verizon after closing. The 700 new employees will need
5 to have a very broad range of technical, management, and operating skills to fill the gap
6 left by those Verizon employees. The available pool of experienced workers for the
7 required positions, such as network management, is not likely to be large. FairPoint has
8 not offset its positive synergy assumptions to account for the significant time it will take
9 FairPoint to establish new work centers; to find, hire, and train people with the variety of
10 skills needed; and to integrate new hires into an effective organization to support
11 operations six times larger than it currently has.
12 Third, FairPoint has assembled a senior management team that includes many new
13 members. It will be operating under a new board of directors, as well. The point here is
14 not that this small group will experience cost-raising inefficiencies directly, but rather
15 that it will take it some time to achieve the control over the other much larger employee
16 groups necessary to get them operating at peak efficiency.
17 In addition to cost impacts, the potential inexperience and inadequate training of a
18 good portion of FairPoint's work force that these considerations suggest is likely to
19 produce negative effects on customer service. Not only will those employees work less
20 efficiently than would a seasoned staff, they are also more likely to make mistakes that
21 affect customers.
22 **Q. Do you have any recommendations to address your concerns about FairPoint's**
23 **financial health?**

1 A. Yes. As seen in Exhibit A, we recommend that the Commission review and approve all
2 FairPoint debt agreements and place some restrictions on dividend payments. However,
3 effectively addressing our financial concerns requires more than restrictions on dividends
4 and comfort with the specific conditions that lenders will require. FairPoint and Verizon
5 must adjust the terms of the transaction in such a way that FairPoint can project a sound
6 financial picture based on more realistic assumptions. We believe that a more
7 appropriate assumption for the length of the TSA is 18 months rather than the current
8 four months assumed by FairPoint. We further believe it is more realistic to assume there
9 will be no net synergies, as the substantial synergies projected by FairPoint will be
10 negated by the concerns we have identified.

11 **Q. Do you have any recommendation to address the customer service risks you have**
12 **noted regarding withdrawal from the TSA, the back-office systems development,**
13 **and FairPoint's staffing challenges?**

14 A. As noted in Exhibit A, we recommend that FairPoint and Verizon negotiate adjustments
15 to the terms of the TSA to reduce the financial burden on FairPoint, reduce the incentive
16 for FairPoint to withdraw from it prematurely, and insure an efficient cutover without
17 disruptions of service. We also recommend that FairPoint provide the Commission with
18 monthly updates to its staffing plans and progress starting prior to close. FairPoint should
19 also agree to Commission approval prior to cutover of system test plans, test criteria and
20 test results of systems, processes, and personnel.

21 **Q. What are your concerns about the costs of extending broadband access?**

22 A. FairPoint has not performed sufficient due diligence to determine what infrastructure
23 additions and modifications will be required to meet its stated broadband commitments.

In particular, as Robert Falcone and Charles King have observed, FairPoint has done very little work to assess conditions downstream from interoffice facilities, such as determining loop conditions and remote terminal cabinet space, both of which are critical to the ability and the cost to provide broadband access. In particular, loop conditions (loop length, loading, etc.) may have a very strong influence on what bandwidth FairPoint will ultimately be able to deliver.

Decisions to extend broadband facilities are largely a function of two key factors; incremental revenues to be gained by further expansion and the costs involved. Verizon has not yet chosen, on the basis of whatever analysis it generally makes of such factors, to expand broadband into the parts of New Hampshire FairPoint is considering. One can therefore assume that for many of the areas in question, costs are too high or revenue is not sufficient to support expansion. If it is reasonable to assume that the areas still in need of broadband build-out are the net higher-cost-per-customer areas of the state, and if it is also reasonable to assume that the costs of extending access increase significantly as we get closer to 100 percent availability, then we must conclude that there is substantial cost uncertainty involved in estimating the costs to provide DSL access to those New Hampshire customers who do not have it.

It is troubling not to see any cost analyses based on actual field condition examinations. Equally troubling is the uncertainty surrounding the question of whether Verizon has not supported FairPoint's requests for access to facilities, or whether FairPoint has not adequately sought it. Whatever the case, we believe that attaching significance to the expectations that FairPoint has created about broadband access requires a clear method for significantly narrowing the uncertainty surrounding its costs.

That narrowing becomes even more critical for a company whose prospects for success depend upon the financial conditions and uncertainties described above.

A recent FCC survey shows that New Hampshire currently ranks last among the states reporting broadband availability. FairPoint's current broadband plan can help rectify this situation, but underestimating the expense of its plan has a significant probability of causing a delay or scale back in that plan. In other words, for its commitment to be meaningful, FairPoint must demonstrate that it can meet it.

Q. What is your recommendation to insure customers enjoy the benefits of the Broadband plan proposed by FairPoint?

A. To protect New Hampshire customers from the potential that FairPoint may fall back from its current broadband plan if it turns out to be more difficult and costly to achieve than anticipated, FairPoint should be required to meet specific broadband targets at 18 and 24 months after close. We further recommend that part of the value of Verizon's directory advertising imputation be traded for a substantial long-run DSL availability commitment. Moreover, New Hampshire residents and businesses deserve the option of purchasing DSL at industry standard speeds, which means that ADSL, for example, should be available with bandwidth of at least 1.5 Megabits in the downstream direction. FairPoint should ensure that the DSL service it will provide to New Hampshire residents and businesses meets those standards.

Q. What are your concerns about the infrastructure costs of improving service quality?

A. FairPoint's lack of knowledge of the New Hampshire network and the root causes of service performance problems place it in a poor position to determine what will prove necessary to resolve service quality concerns. FairPoint believes that the addition of a few

technicians at a nominal cost per year can solve existing problems. FairPoint has not done sufficient analysis from which to determine that this very marginal solution (given the hundreds of persons now employed in relevant activities) will be effective. As our direct testimonies noted, there are clear indications that this solution will not be effective. Moreover, one has to ask why, if adding a few employees at a nominal cost could have ended the debates in New Hampshire about service quality, Verizon did not do so long ago. FairPoint's financial cushion is already overtaxed (even under its optimistic assumptions); it would be folly not to acknowledge the very real financial risk inherent in FairPoint's ability to make significant service improvements.

If we are correct that these costs will be higher than expected, FairPoint may decide to delay or scale back its commitment to meet Commission service quality standards. In addition, the remediation work beginning at the Raymond central office and the construction on the Pinkham Notch ring are two major network capital projects that will be on-going at the time of closing, thereby adding to FairPoint's cost burdens. The need for other major remediation projects may be uncovered after the transaction closes, as well. Finally, if FairPoint fails to meet its projected financial results, it may be compelled to cut back on the capital investments necessary for ordinary network and systems maintenance, thereby jeopardizing service quality even further.

Q. If the Commission denies this transaction, does the risk that Verizon will ignore service quality and broadband access balance the concerns you have raised?

A. If one assumes that there is a material risk that FairPoint will not be able to deliver on service and broadband expectations, then there is no real risk in keeping Verizon as the local exchange provider in New Hampshire. However, we believe the risks that FairPoint

will not be able to deliver on its commitments and obligations are real. In the event that the Commission does not approve this transaction, and Verizon still wishes to sell, changes will be necessary. If it chooses to stay, it will be doing so after this transaction has shone a very bright light on service quality issues and the comparatively poor state of broadband access in New Hampshire. It is difficult to see how Verizon will remain able to meet customer and regulatory expectations without change, after this proceeding has given these issues such exposure.

8 **Q. What is your recommendation on service quality?**

9 A. We recommend conditions to improve network service quality, including conditions to
10 assure that FairPoint meets Commission service quality requirements both at the
11 statewide and individual central office levels, provides accurate service quality reports,
12 and does not cut back its projected capital expenditures for network maintenance. In
13 addition, we propose a specific condition to address the "double poles" issue.

14 Unexpected capital expense requirements will worsen FairPoint's financial
15 condition. We believe that the best way to address that risk is for Verizon to act as a
16 backstop for specific capital requirements, providing at least a portion of funds for the
17 network maintenance and broadband expansion capital expenditures if they exceed
18 FairPoint's current cost projections. The uncertainties in capital requirements arise
19 principally from FairPoint's incomplete knowledge of Verizon's network. Furthermore,
20 the capital projects addressed in our list of concerns are associated mainly with
21 remediation of conditions that have arisen during Verizon's stewardship of the network,
22 which suggests that Verizon has a share in the responsibility for alleviating them.

We understand the need for effective parameters limiting access to Verizon funds for future capital expenditures. Those parameters can come through a series of protections. First, access to the money should be bounded in time. It should not be available for projects and activities whose need is identified longer than one year after closing. Second, FairPoint and Verizon technical personnel should work together to develop a joint plan for covered projects and activities. That plan should undergo Commission review and approval, as should any disputes about its implementation. Third, FairPoint should be given – and should demonstrate that it has taken advantage of – full access to the Verizon network information and be required to develop detailed and specific plans.

Q. How do you justify a re-allocation of the benefits of the transaction as a solution to the concerns you have addressed?

A. First, our solution is geared toward re-allocating risks, not benefits. If the FairPoint assumptions about which we have concerns prove to be correct, both parties to the transaction will benefit, as will customers. If FairPoint and Verizon have reasonable confidence in the basic accuracy of those assumptions, then there is no substantial risk in requiring that they demonstrate that confidence with what we believe are reasonable protections for customers against aggregate risks that are not as great in the absence of the transaction. On the other hand, if they do not have such confidence, then there is all the more reason to require protection for customers, whether or not it means that, on a net basis, Verizon's shareowners end up with every penny they assumed the deal would give them. The Commission's primary concern in a proceeding like this is the public interest, not the maximization or diminishment of shareowner value.

If Verizon considers, from its superior state of knowledge as well as its experience in the Hawaii experience, that FairPoint has accurately assessed: (a) the infrastructure aspects of service improvement and broadband deployment, and (b) TSA needs, then it should have some confidence that providing the required assurance is not highly risky. If it does not have that confidence, and therefore considers the risks to be great, then the Commission should have no greater optimism. If FairPoint is wrong, our solution puts the consequences on the dealmakers, not the customers and this Commission.

9 **Q. How does your view of the financial risks compare with those of the credit rating**
10 **agencies that have been examining the debt arrangements of the proposed**
11 **transaction?**

12 A. Credit rating agencies focus on the degree to which there are adequate assurances of debt
13 repayment for bondholders. Our concerns are whether difficulties in debt repayment (whether or not they result in default and receivership or bankruptcy) will leave New Hampshire with a local exchange services provider focused on survival, rather than on the delivery of safe and reliable service, the provision of broadband and the achievement
17 of other commitments FairPoint is making. Economic survival quite simply is not a
18 concern for an enterprise like Verizon, which is financially strong and carries very high
19 quality credit rating. The same is not true of FairPoint, which carries a speculative grade credit rating of BB-. That rating denotes a significant risk of inability to pay debt principal and interest. If a financial decline occurs, the pressures on resources to be applied to debt payments and utility service are self-evident. New Hampshire has all too

much experience already to need to be reminded of the direct and indirect impacts that a financial failure by one of its major utilities can have.

Moreover, even if we did believe that the perspective of the rating agencies is dispositive, and even if that perspective were more supportive of FairPoint's financial strength, we need not look long to see clear evidence that the rating agencies cannot (nor do they presume to) predict the future. Observe the continuing financial concerns plaguing the acquirers of Verizon's Hawaiian operations. Hawaiian Telcom has already been forced to sell its valuable directory business in order to provide cash to its lenders as part of a forced debt restructuring. More than two years after closing, its financial condition remains weak and at risk of further slippage. Recently, Standard and Poor's changed its forward-looking outlook for Hawaiian Telcom from "stable" to "negative," based on continuing billing and back-office system delays and heightened competition from other voice and data providers. It does not serve the public interest to expose New Hampshire residents and businesses to these risks.

Q. In addition to the customer impacts resulting from failure of FairPoint to address the broadband, network service quality, capital investment, staffing, and back-office system issues, do you have any other concerns about FairPoint's ability to provide quality service to customers?

A. Yes. Retail customers should be provided the same sales, service, billing and collections options they currently have through Verizon. FairPoint currently has limited experience with the provision of many of those options. FairPoint also needs to assure that call center quality meets Commission standards and that customer transition issues are addressed and customer communications planning is completed.

1 FairPoint has almost no experience providing service to wholesale customers. In
2 order to maintain a vital competitive market in New Hampshire, FairPoint must make the
3 transition for its wholesale customers as smooth as possible and maintain a stable
4 operating environment for them. FairPoint will need to develop new systems and set up
5 completely new work groups and work centers to serve those customers. FairPoint has
6 committed to providing a smooth transition and to offering the same services and
7 maintaining a stable operating environment in the short run; however, it has also chosen
8 to distance itself from some potential Verizon obligations by seeking to avoid
9 classification as a BOC.

10 **Q. What are your recommendations regarding retail and wholesale service?**

11 A. We recommend specific commitments that FairPoint should make to both retail and
12 wholesale customers, including assurances to maintain services and service options and
13 rate stability. We also recommend using part of the directory advertising imputation for a
14 retail rate freeze for three years.

15 **Q. Do you have any other significant concerns about the transaction?**

16 A. Yes. We are concerned about (a) the incomplete state of FairPoint's E-911 transition
17 planning, (b) FairPoint's continued lack of a firm plan to replace some of the network
18 functions Verizon currently performs, (c) FairPoint's failure to acknowledge the directory
19 advertising imputation, (d) certain aspects of the structure of the new FairPoint board of
20 directors, and (e) the need for clarity with respect to the operational relationships and cost
21 allocations among FairPoint's various entities and business units.

22 **Q. What are your recommendations for addressing these concerns?**

A. As noted in Exhibit A, we propose a number of separate conditions on FairPoint. We recommend certain reporting requirements to address some of the concerns. We recommend that the value of the directory advertising imputation be traded for certain other commitments, as I have already mentioned. We also recommend that FairPoint make some commitments regarding its board of directors structure and policies.

Q. Are there any other conditions that the Commission should consider?

A. As I have noted, we have not as yet taken a position on a number of issues raised and conditions proposed by other parties in this proceeding. For example, we have addressed one of the issues raised by the electric utilities and municipalities regarding pole maintenance, but we have not attempted to address all the issues they have raised. We have also addressed some, but not all, of the issues raised by OCA, Labor, and the CLECs. Similarly, we believe that some of the issues raised on behalf of low income customers are addressed in our retail service quality conditions and the proposed trade-off of a portion of the directory advertising imputation for a three-year rate freeze. However, we have not attempted to address such issues as the need for greater efforts to advertise the Lifeline and Link-up programs. We hope to engage in discussions with all parties in the near future to consider these and other issues.

Q. Does that complete your testimony?

A. Yes, it does.

FairPoint/Verizon Asset Transfer
NHPUC Staff Proposed Conditions

Concern	Proposed Solution
1. The synergies and TSA assumptions in the base financial model are too optimistic.	FairPoint and Verizon should revise the terms of the transaction in order to achieve Debt/EBITDA < 4.5 : 1 (4.75 in the first year) and EBITDA/Interest > 2.75 : 1 (2.50 in the first year), assuming the following in the FairPoint financial model: • No synergies • TSA lasts for 18 months after close • All other conditions below are in place – in particular, the condition that Verizon shares in CAPEX funding if they exceed expectations • All other financial model assumptions remain unchanged.
2. FairPoint's leverage and dividends are too high in relation to its cash flow.	FairPoint should meet the conditions outlined in item 1 above, and the Commission should review and approve final debt agreements. FairPoint should not pay dividends if its leverage ratio is above 5.0 : 1.
3. Broadband plan may be more costly than assumed.	Verizon must: • Provide FairPoint 3 months before close all the information FairPoint needs about the New Hampshire network to allow FairPoint to make a more accurate estimate of the cost of its broadband plans. • Pay broadband CAPEX expenditures that exceed $21.6 million to accomplish FairPoint's broadband build out plan.
4. New Hampshire customers need assurance of improved broadband availability.	FairPoint must agree to meet the following DSL availability objectives: • 75% of access lines in 18 months after close • 85% of access lines in 24 months.

	DSL availability should include an option with 1.5 Megabits downstream.
5. Back-office system development may take longer than expected, leading to a temptation for premature withdrawal from the TSA.	FairPoint and Verizon should: • Renegotiate the terms of the TSA to remove the incentive for premature withdrawal and mitigate its financial impact (to be addressed in combination with item 1 above). We recommend that this include an overall price reduction, removal of automatic price increases after month 12, and designation of service groups that can be transitioned independently with an associated reduction in TSA monthly charges when these services are cutover. In addition, FairPoint must • Agree to a Commission approval of system test plans, test criteria and test results of its systems, processes, and personnel before cutover.
6. Network quality needs to be improved.	FairPoint and Verizon must meet the following conditions: • Verizon must provide FairPoint 3 months. before close all the network information necessary to allow FairPoint to conduct a complete and specific root-cause analysis of the service quality problems in New Hampshire. • FairPoint must provide the Commission with a network improvement plan 2 months after close • FairPoint must meet Commission standards at a statewide level 9 months after close • FairPoint must meet Commission standards at the central office level 12 months after close. • FairPoint must reduce the number of double poles to 500 by December 2010. Verizon should pay overtime

	to achieve. • Verizon must pay for 50% of capital costs to replace faulty equipment and facilities necessary to remediate service quality problems uncovered within 12 months of close. • FairPoint must agree to an audit of the accuracy of service quality measurement reports within 12 months of cutover.
7. Imputation of the yellow pages value to New Hampshire rate payers will be lost as part of the transaction.	Use imputed value to achieve other objectives. Trade off yellow pages imputation for: • Commitment to reach 95% DSL availability in 60 months, and • No rate increases for 3 years.
8. Major network capital projects (e.g., Raymond and Pinkham Notch) will be on-going at the time of closing.	Verizon must continue to pay for these projects until they are complete.
9. Solution for E911 and replacements of some Verizon network functions (e.g., OS/DA, AIN) currently undetermined.	FairPoint must provide the Commission with an explanation of the solutions 3 months before close.
10. FairPoint may have insufficient and/or poorly trained staff.	FairPoint must provide monthly reports to the Commission beginning 3 months before close providing status of staffing plans and progress.
11. Other major remediation projects may arise.	Verizon must pay for unexpected capital expenditures for remediation of past known issues for one year after close.
12. Failure to meet the projected financial results will lead FairPoint to cut back on capital expenditures and jeopardize service quality.	FairPoint agrees to no reductions below current forecasted levels of CAPEX.
13. The transaction may undermine the wholesale market.	FairPoint must: • Assume the Verizon PAP for all CLECs, regardless of whether the PAP is referenced in the CLEC's interconnection agreement or whether the CLEC purchases out of a tariff. • Commit to provide all products and services that Verizon offers or would be required to offer, regardless of whether these services stem from

	Verizon's status as a BOC, such as those related to section 271. • File rates for wholesale services that Verizon would have been required to provide, pursuant to RSA 378:1. • Commit not to seek for three years after close any change in its wholesale obligations, through such means as forbearance or other regulatory waivers (including the effect of forbearance petition pending for Rockingham and Strafford counties). • Agree to an independent audit of the PAP report one year after cutover.
14. FairPoint may not be able to maintain retail service quality	In addition to the network service quality conditions noted above in item 6, FairPoint must: • Provide by cutover the same sales and service options as Verizon • Assume or have redirected all Verizon published numbers • Meet the Commission's call center standards within six months of cutover • Provide for the Commission's review a copy of its proposed bill format at least three months prior to cutover • Negotiate contracts with the same payment agencies used by Verizon to ensure that customers can continue paying in person at a qualified third-party location • Assemble and review with the Commission a viable and comprehensive customer communications plan at least three months prior to close.
15. FairPoint's Board structure and policies need to be adjusted.	FairPoint must: • Assure that at least two Board members have strong ties to New Hampshire or agree to create an advisory board composed of

	distinguished local community and business leaders • Create a Board Finance Committee • Limit the powers of the Executive Committee.
16. Insufficient controls exist on affiliate transactions.	FairPoint must adopt and provide for Commission review before closing a detailed Cost Allocation Manual, service agreements, and affiliate transaction policies and procedures.