STATE OF NEW HAMPSHIRE

BEFORE THE

PUBLIC UTILITIES COMMISSION

DT 07-011

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

**Prefiled Testimony of Walter E. Leach, Jr.
On Behalf of
FairPoint Communications, Inc.**

March 23, 2007

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INTRODUCTION

Q. Please state your name and business address.

A. My name is Walter E. Leach, Jr., and my business address is 521 East Morehead Street, Suite 250, Charlotte, North Carolina, 28202.

Q. By whom are you employed and in what capacity?

A. I am employed by FairPoint Communications, Inc., (FairPoint) where I currently hold the position of Executive Vice President, Corporate Development.

Q. Please describe your educational background and professional background.

A. I have an undergraduate degree in Industrial Management from Georgia Tech. I joined FairPoint in October 1994 as the company's Chief Financial Officer. In this role, I was responsible for FairPoint's financial reporting and control, investor relations, treasury and risk management. While I was Chief Financial Officer, FairPoint successfully acquired, integrated and operated 28 independent telephone companies. As the principal financial executive for the company, it was part of my job to ensure that the financial terms of the transactions were reasonable and that the company remained financially sound as a result of these acquisitions. In July 2004, I became Executive Vice President and, in June 2005, I assumed my current position as Executive Vice President, Corporate Development.

Prior to joining FairPoint I spent ten years at Independent Hydro Developers, as an Executive Vice President responsible for project acquisition, financing, and development activities. Independent Hydro Developers is a privately owned independent power company which predominantly develops or refurbishes hydroelectric projects and then operates and maintains such facilities. Prior to that, I held the position of Vice President, Investor Relations, for The Pillsbury Company and served as Treasurer, Assistant Treasurer, and Region Controller for Burger King Corporation.

Q. What are your current responsibilities at FairPoint?

A. In my current role, I am responsible for all aspects of FairPoint's merger and acquisition activity as well as strategic planning. These responsibilities include identifying appropriate strategic acquisition or disposition opportunities, managing the due diligence process for potential acquisitions and other financial initiatives, negotiating key transactional terms (including price and closing conditions), participating in the documentation of transaction agreements, managing the company's relationships with investment banking and private equity firms related to, or required for, such transactions, and supervising the process of seeking regulatory approval related to such acquisitions. In this role, it is my responsibility to ensure that the transactions we pursue are consistent with the strategic direction of the company, are financed in a responsible manner, and have a positive impact on the consolidated financial position of FairPoint.

SUMMARY OF TESTIMONY

Q. Please summarize your testimony.

A. I will begin by providing an overview of several key benefits resulting from the combination of FairPoint with Verizon's northern New England properties, focusing on factors that should interest stakeholders, including customers, employees, and local communities, as well as our investors. Next, I will outline the structure and terms of the transaction, from the FairPoint perspective, following up on Verizon's more detailed presentation. In addition, I will present an overview of the financial analysis that supports the transaction, and which served as a tool for the FairPoint Board of Directors in making its decision to commit to this combination. The financial overview will include a discussion of the pro forma financial projections for FairPoint post-closing, a review of the capital structure, and a demonstration of the company's ability to generate more than sufficient cash flow to meet all of its cash requirements, and invest in operations going forward, as well as the enhanced ability to attract future capital, if needed, on reasonable terms. The final general area I will cover is the merged company's relationship with various other FairPoint entities and with Verizon's operations. For regulatory purposes, it is our plan to maintain distinct operations for the former Verizon assets and for the existing FairPoint[1] operating entities. As a result, FairPoint is preparing to establish and monitor separate accounting

[1] For purposes of this testimony, existing FairPoint operating entities are defined as the local exchange operating subsidiaries currently owned by FairPoint, as distinct from the Verizon properties that are the subject of this transaction and proceeding.

and operations mechanisms to ensure appropriate and accountable inter-affiliate practices.

FOCUS OF TESTIMONY

Q. What is the focus your testimony?

A. I will present an overview of the business and financial rationale for the transaction. In doing so, I intend to describe the benefits to customers, employees and the region, emphasizing FairPoint's commitment to invest significant capital to provide high-quality services today and in the future, including the provision of advanced communications and broadband networks to northern New England.

It is evident that FairPoint's financial investment and commitment in northern New England will be substantial. What may be less evident is the strategic commitment embodied in FairPoint's decision to pursue this transaction. Our significant investment of monetary and human capital, senior management focus, and the other resources of our company demonstrates that the success of this transaction is critical to the long-term viability of the company. With this transaction FairPoint is reaffirming a long-standing strategic commitment to local communications operations that serve rural and small urban areas. As we consider allocation decisions regarding capital and management resources, we note that there are no significant competing interests that distract us from our focus on local wireline telecommunications operations (including voice and data services). We do not have other lines of business that compete for capital or management time. As has been the case throughout the history of FairPoint, the foundation of our success will be defined by our ability to provide high-quality wireline communications services at competitive rates for all of our customers—both in existing FairPoint markets and in the new northern New England markets. This singular strategic focus will allow FairPoint to commit the resources required—financial and otherwise—to provide high-quality, advanced communications services at competitive prices to the new northern New England service area.

Critical to the commitment FairPoint is making is the ability to generate cash flow in excess of amounts required to support the planned investment, operations and other obligations. I will describe our financial plan for the acquired operations based on a five-year period (consistent with our internal business planning and decision-making time horizon). The five-year projection period is useful for several reasons, including: (i) it is long enough to discern the financial characteristics of the steady-state post-transaction operations while (ii) it is not so long as to be overly speculative. While a projection through 2015 was prepared and reviewed by the FairPoint Board of Directors, they focused more intently on a five-year time horizon in evaluating the opportunity and the projections in making the decision to pursue the transaction.

BENEFITS OF THE TRANSACTION

Q. You mentioned substantial benefits from FairPoint's commitment to invest in the Verizon northern New England properties. Can you explain the benefits in more detail?

A. The primary benefits of this transaction can be summarized under four headings: customers, employees, community / economic benefits, and policy. In addition to these areas of external benefit, the transaction is consistent with the interests of investors. As a result of these positive outcomes, we believe that it clearly is in the public interest that this transaction be approved. I will discuss each of these categories of benefits in more detail below.

Q. You indicate that customers will be better off as a result of this transaction. What are the principal customer benefits that FairPoint anticipates?

A. The merger is expected to create a range of benefits for both retail and wholesale customers. These benefits include access for more customers to advanced telecommunications and information services such as broadband Internet, more locally-focused customer service, and competitive pricing of new bundled service offerings tailored to the desires of retail customers in the three states. The benefits also include improvements or updates to the infrastructure on which wholesale customers rely, and assurance that wholesale customers will continue to receive the services they receive today under the same rates, terms and conditions.

First, FairPoint plans to expand significantly the availability of broadband services to customers in the three-state region (primarily using DSL technology). A major expansion is expected to be completed within the first twelve months after the consummation of the merger that will result in a significant number of current Verizon customers having access to DSL who have no such access today. Currently 92% of FairPoint customers in the three states have access to broadband services while only 62% of Verizon's customers in the same region have access to a Verizon broadband product.

Second, FairPoint will have a significant local operational presence in the region, as the back-office functions performed by Verizon outside of the three-state area will be moved into the three states by FairPoint, resulting in the opening of at least three new local service centers to deliver industry-leading customer service. The specific functions to be performed by these three service centers are discussed in greater detail in Mr. Nixon's testimony. FairPoint believes that having these operations located "in-region" should serve to provide some incremental benefit to customers as service functions and personnel will be local to the markets and more responsive to local needs.

Third, the company expects to offer customers an increased selection of competitively priced communications services bundles, providing greater choice in the marketplace for communications services. As these consumer benefits illustrate, this transaction will create a responsive telecommunications provider focused on serving the needs of northern New England customers, able to offer advanced services on a robust network platform, enabling the delivery of a broad range of communications products and services.

In addition to the end-user customer benefits from the transaction as described above, the transaction is expected to have benefits for wholesale customers. The network improvements FairPoint implements for the benefit of its own retail customers will also confer some degree of benefit on wholesale customers (including competitive local exchange carriers (CLECs) and interexchange carriers (IXCs), cable television providers, commercial mobile radio service (CMRS) providers, voice over Internet protocol (VoIP) and other alternative service providers). All of these providers rely to some degree on the universal availability, reliability and quality of the incumbent local exchange carrier (ILEC) network, operations support systems (OSS) and other back-office operations. For that reason, wholesale customers will benefit from any increase in investment made by FairPoint in the acquired exchanges—both in the network itself and in the supporting systems, such as ordering and provisioning systems. Moreover, wholesale customers will continue to receive the same services—including exchange access, interconnection, resale and unbundled network elements—under the same rates, terms and conditions as provided by Verizon. As explained in more detail by Mr. Nixon, FairPoint has committed to assume Verizon's inter-carrier contracts and concur in or adopt Verizon's tariffs (including its wholesale tariffs and Statements of Generally Available Terms and Conditions), so wholesale customers will not be adversely affected by this transaction.

Q. Please describe in greater detail the benefits to employees.

A. As Verizon has explained, the transaction ensures fair and equitable treatment of its current employees in the three northern New England states. Both Verizon and FairPoint believe that this experienced labor force represents the key to serving customers, and it is fundamental that the companies support those employees. FairPoint and Verizon have agreed, as part of the merger agreement, that FairPoint will honor the commitments to the approximately 3,000 employees employed in Verizon's regional operations. The International Brotherhood of Electrical Workers (IBEW) and the Communications Workers of America (CWA) represent approximately 2,500 of these 3,000 employees who will become part of the merged operations. FairPoint has committed as part of this transaction that the collective bargaining agreements with the IBEW and the CWA will continue to apply for the union represented employees and that the management employees will continue to receive the same levels of compensation and benefits they receive now from Verizon.

The employees generally will continue in their existing roles and locations, performing functions consistent with those they perform today, after the transaction is completed. Simply stated, this commitment is intended to ensure stability and benefits to employees, while allowing operating and contractual flexibilities that FairPoint, Verizon or any other employer should have in operating its business. Let me be very clear on this point, FairPoint's plan for the merged company does not include any job cuts or any reductions in compensation or benefits for the Verizon employees, non-union or union, who join FairPoint. Indeed, moving the out of state back-office functions to the three-state area will result in the addition of approximately 600 new positions to the employee base serving the three states. These new positions will provide opportunities for additional employees to join the company and for existing employees to seek out alternative career paths if they so choose. In this competitive environment, FairPoint intends to retain and grow the customer base, and we see a motivated workforce as critical to ensuring a stable and smooth transition to an even more locally focused operation over the following years.

FairPoint has made it clear that it is committed to working with the unions in a collaborative fashion. FairPoint will honor the existing collective bargaining agreements, and it expects to work constructively with union leadership in an effort to offer a strong package of new job opportunities for local, skilled employees. In addition, if the unions are interested in discussing an extension to the existing contract (which has a term through August 2008), with the same general terms and conditions, FairPoint is willing to begin a dialog immediately on such an extension, which obviously would be contingent on the merger closing.

In addition, as previously announced, FairPoint will assume pension and other post-employment benefit obligations for all active, continuing employees of Verizon companies that become part of FairPoint. The pension obligations will be funded fully with assets provided by Verizon as of the closing of the merger. As required by law, FairPoint will be funding the pension plan and other retiree obligations that accrue for these employees after the closing. (Those obligations are included in the projections discussed later in this testimony.) The assets supporting the pension plan essentially will be of the same quality as the assets in the employees' current Verizon pension plan. Retired Verizon company employees from the region will continue to receive their benefits from Verizon pursuant to the Verizon plans. FairPoint believes the continuing employees will be better off after the merger as none of the retired Verizon employees must be supported by the FairPoint pension plan.

Finally, FairPoint intends to establish a New England-based management presence focused on dedicating the necessary resources to benefit local operations and communities, and to ensure that the company can achieve its objectives. We believe that this commitment to local management will provide employees greater opportunities for internal advancement and professional development in these three states, and will provide greater localized decision-making authority, for the benefit of both employees and consumers.

To summarize, the transaction will not result in job cuts or in any reductions in compensation or benefits for the Verizon employees transitioning to FairPoint. The transaction will provide greater local management authority in the region and will create additional opportunities for employment and professional development.

Q. What do you mean when you say that the transaction will result in "economic benefits" to the region?

A. FairPoint believes the transaction will be beneficial to the economies of Maine, New Hampshire, and Vermont in a number of ways, including increased investment in existing network infrastructure and services (which I will address more directly later in my testimony), improved broadband availability, job creation, and investment in new local service support centers. I have already explained that FairPoint intends to expand significantly broadband availability in the three-state region, with the initial expansion expected to be completed within the first twelve months after the conclusion of the merger. The expansion of broadband availability will require significant incremental investment in the network, which the company has already begun to design and plan. This network investment is beneficial to the local economies, as broadband availability is a critical element in driving economic viability and development. By making broadband available to a greater number of northern New England customers, residential and business, FairPoint will strengthen the long-term economic prospects of the region.

In addition, I explained how FairPoint intends to add approximately 600 new positions that will be located in Maine, New Hampshire and Vermont. Some of these positions will be replacing the customer service and systems support operations currently provided to the three states by Verizon operations that were housed outside of the region; other positions will be incremental to existing Verizon in-region employment levels. FairPoint will open at least three new in-region service centers—a network operations center, an information systems center, and an administrative center—which represent a substantial investment in the region above the incremental network investment noted earlier in this testimony. The new facilities will be in addition to our on-going improvements to the FairPoint South China, Maine, East Coast call center, which is expected to remain a key operational asset and will not be affected by the merger.

From an economic development perspective, the transaction should provide real benefits to the three states in the form of incremental network investment, greater broadband availability, more jobs, and investment in local operational facilities.

Q. What are the "policy benefits" that FairPoint expects as a result of this transaction?

A. FairPoint believes that federal and state communications policy will be advanced through the approval of this transaction. FairPoint intends to provide a wide range of services in rural areas throughout the three state region, including broadband, which are comparable to the services found in urban regions and at rates comparable to those found in urban regions. Fairpoint has demonstrated its commitment to rural and small urban markets, as it is an industry leader in making broadband available in these types of markets. As stated previously, currently 92% of FairPoint customers in Maine, New Hampshire and Vermont have access to broadband services. Increasing broadband availability has been defined by national and state policymakers as one of their primary goals. This transaction advances that policy interest.

Further, FairPoint believes that its services in all regions will prove more "competitive" as more expansive marketing and bundling of current products will be tailored to local preferences. For example, the company intends to introduce a branded wireless communications product, thereby creating an additional wireless competitor and incremental wireless competition in the three states. Improved competition in all segments of the communications industry is a goal of policymakers, as it is good for consumers and the economy. This transaction will result in a more focused wireline communications and broadband provider and will create a new regional wireless competitor.

OVERVIEW OF TRANSACTION MECHANICS AND TERMS

Q. What are the mechanics through which the transaction will be accomplished?

A. The transaction is described in detail in the testimony of Verizon witness Stephen E. Smith. Generally, Verizon New England's local exchange and related business assets and interLATA long distance and ISP customer relationships in Maine, New Hampshire and Vermont will be transferred to subsidiaries owned by a newly-organized, wholly-owned subsidiary of Verizon, known as Spinco. At closing, Spinco will incur $1.7 billion of newly-issued debt, its stock will be distributed to Verizon's stockholders, and it will be merged immediately with and into FairPoint. FairPoint will be the surviving corporation, and its executive management team will retain operational control.

Upon the closing of the transaction, FairPoint stockholders will own approximately 40 percent of the company. Verizon shareholders will own approximately 60% of the company, as the merger agreement stipulates each Verizon stockholder will receive one share of FairPoint stock for approximately every 55 shares of Verizon stock held as of the record date. (Verizon will not own any shares in FairPoint at any point during or after the merger.) Both the distribution of the new subsidiary's stock and the merger are expected to qualify as tax-free transactions, except to the extent that cash is paid to Verizon stockholders in lieu of fractional shares. The tax-free nature of the merger is important in assuring that Verizon's shareholders receive an acceptable value for the northern New England assets acquired by FairPoint. It also ensures the transaction results in a financially sound operation, as I will detail, and supports the investment FairPoint believes is necessary and to which we are committed.

The total value to be received by Verizon and its stockholders in exchange for these operations will be approximately $2.715 billion. Verizon stockholders will receive approximately $1.015 billion of FairPoint common stock in the merger, based upon FairPoint's recent stock price and the terms of the merger agreement. Verizon will receive $1.7 billion in value through a combination of cash distributions to Verizon and debt securities issued to Verizon before the stock distribution and merger. As a result, the transaction price is funded by an appropriate combination of equity (37% or $1.015 billion of $2.715 billion) and debt (63% or $1.7 billion of $2.715 billion).

The transaction includes Verizon's switched and special access lines in the three states, as well as its Internet service, enterprise voice CPE ("customer premises equipment") accounts, and long-distance voice and private line customer accounts (for customer private lines with beginning and ending points within the three states) that Verizon served in the region before the 2006 merger with MCI, Inc. The transaction does not include the services or assets of Verizon Wireless, Verizon Business (former MCI), Federal Network Systems LLC, Verizon Network Integration Corp., Verizon Global Networks Inc., Verizon Federal Inc. or any other Verizon businesses in these states. Mr. Smith's testimony describes in more detail the assets and customers that will be transferred, and those that will not.

FairPoint expects that the transaction will be accretive to FairPoint's free cash flow, after transition costs and conversion capital expenditures. As demonstrated below, FairPoint will be able to generate solid operating cash flows that support the company's investment plans, debt service and ongoing dividends. These results will be possible and augmented through management focus, local/regional marketing and customer service initiatives, and future development of innovative technology and processes.

Q. What will be the surviving entity at the end of the process?

A. When the merger is completed, the Spinco companies conducting the Maine, New Hampshire and Vermont telephone and related business operations (the former Verizon operations) will be wholly-owned subsidiaries of FairPoint Communications. Current FairPoint executive management will supervise and manage the operations of FairPoint, including these subsidiaries, following consummation of the proposed transaction. Our executive management team has an average of 23 years of industry experience and includes Eugene Johnson (Chairman and Chief Executive Officer), Peter Nixon (Chief Operating Officer), John Crowley (Executive Vice President and Chief Financial Officer), Shirley Linn (Executive Vice President and General Counsel), and me. As discussed below, the subsidiary that holds the former Verizon New England local exchange assets and offers local exchange service in the acquired exchanges will remain separate from FairPoint's existing local exchange operating subsidiaries.

Q. Describe the composition of FairPoint's Board of Directors following the transaction? Specifically, how will board members be selected, and how will the Chairman be selected?

A. Upon completion of the merger, Verizon will designate up to six of the nine initial Directors of FairPoint. Such directors must be independent, which means that none of Verizon's nominees may be employees of Verizon Communications, its affiliates or Cellco Partnership, d/b/a Verizon Wireless or any of the Verizon Wireless subsidiaries. FairPoint will designate a minimum of three of the nine initial Directors of FairPoint post-closing. Gene Johnson will remain the Chairman of the Board of FairPoint. After this initial slate of Directors assume their duties with FairPoint, directors will be elected by the shareholders of the combined company in the normal course as provided in FairPoint's by-laws.

Q. What remaining steps are necessary in order to close the transaction?

A. In order to complete the transaction, approval must be received from FairPoint stockholders, state regulatory authorities in Maine, New Hampshire, Vermont, and Illinois. In addition, the Federal Communications Commission must approve the transfer of control to FairPoint of certain authorizations and licenses used in Verizon's northern New England operations. An Internal Revenue Service tax ruling acceptable to Verizon must be issued, and clearance must be received under the Hart, Scott, Rodino Antitrust Improvements Act of 1976. In addition, customary closing conditions, as described in the merger agreements, must be satisfied.

FINANCIAL SOUNDNESS OF THE TRANSACTION

Q. Please describe the financial model and pro forma financial projections FairPoint developed.

A. The financial projections were built by FairPoint as we performed our due diligence. In addition to our internal efforts, we engaged Lehman Brothers and Morgan Stanley, two of the largest investment banks in the world, to provide advisory services, which included assisting with the due diligence and negotiation process. Verizon supplied us, and continues to supply us, with financial information for its Maine, New Hampshire, and Vermont operations. With this information as our starting point, we began identifying the various businesses that would be acquired as part of the transaction (local, long distance, and Internet) and built a financial model for those businesses (the Spinco operations or properties). Next, we identified the details within each business line, such as revenue sources, costs of services sold, historical and projected demand, operating expenses, expected capital requirements, cash flow characteristics, and other relevant industry factors, and began analyzing the trends. We compared this information to our own experiences operating the existing FairPoint exchanges in the three state region. Eventually, we modified the model to reflect our assessment of the trends and expectations for the merged company. FairPoint is an experienced acquirer and operator of telephone operations, and we relied on that experience to validate the reasonableness of our assumptions (and the information Verizon supplied us) concerning such factors as expected demand, revenues, cost trends, capital investment and expected cash flows.

Q. **How was this information used by FairPoint**?

A. The pro forma financial projections were a factor considered by our management team and Board of Directors in establishing a value for the Verizon assets to be included in the transaction. In addition, modeling the projected operating results and cash flows allowed us to ensure that the company will be properly capitalized given its expected growth and cash flow generation characteristics. We developed a model through 2015, but focused on a five-year projection period as the primary study period, which was consistent with FairPoint's business planning time horizon for such acquisitions or mergers.

Q. **Turning to the exhibits, please describe Attachment WEL-1.**

A. Attachment WEL-1 contains an overview of FairPoint's financial projections for the company. The projections served as a financial tool for our evaluation of the potential transaction and were a factor considered by FairPoint's Board of Directors' in making its decision to approve the merger. Included in the Exhibit is a summary income statement, a calculation of cash flows, summary balance sheet data, an analysis of key credit ratios, margin and growth analyses, and detail regarding capital expenditures and other assumptions.

**BEGIN CONFIDENTIAL INFORMATION

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END CONFIDENTIAL INFORMATION**

Given the solid ratios, the improving capital structure and the size of the company following the merger, we are confident that the capital markets will continue to be open to us should we need to access them. In addition to maintaining access to capital, the ratios and balance sheet are strong indicators that the company will remain financially stable for the foreseeable future. In fact, one credit rating agency has indicated FairPoint's credit rating is likely to improve following the closing of the transaction, based upon the projected capital structure.

Q. Based on the projected financial profile of the company, as reflected in Attachment WEL-1 and the tables above, will FairPoint be a financially sound company subsequent to this transaction?

A. Yes. Clearly the management team and Board of Directors of FairPoint believe that the merged company will be strong. In addition to the operating and balance sheet items summarized above, I note that other than the identified efficiencies resulting from the replacement of certain Verizon allocated functions and their associated costs, FairPoint has not assumed any cost-cutting measures and, in fact, has assumed some rising operating costs. We firmly believe that FairPoint will be a financially sound and viable company, with the resources to provide the benefits I have described to our customers, our employees, and the communities we serve.

Q. How will assets be carried on FairPoint's regulatory books?

A. The assets related to the regulated business, and under state and federal commission regulatory jurisdiction, being transferred with the transaction will be recorded at Verizon's net book value. This net book value includes the historical cost of the assets (the cost of the asset when first placed into service for regulated telecommunications use) less the accumulated depreciation. FairPoint will not include, nor will it request to include, any acquisition premium or amortization thereof in a future rate base / rate of return proceeding, should such an event be necessary. Other types of costs related to this transaction, such as due diligence, negotiation, and costs to obtain financing, will not be passed on to customers through regulated rates.

Q. Will the business be able to attract capital without seeking an adjustment to rates?

A. Our financial projections described above assumed that rates for telecommunications services will remain the same as those currently charged by Verizon. Based on that assumption and the rest of our financial analysis, we project that during the five-year period FairPoint will be able to generate significant Free Cash Flow, and will be able to attract additional capital, if necessary, to achieve the service improvements we have planned. Again, there will be no costs related to the merger transaction that will be passed on to the customers.

Q. Are you suggesting rates, rate design, or regulatory approaches would or should never change?

A. Not at all. We expect to have no more and no fewer rights than did Verizon to seek changes in rates or regulation as appropriate based on changes in the market. As noted above, however, the company will not seek to recover through rates the transaction costs or any acquisition premium associated with this transaction.

Q. Please describe any cost savings or "synergies" associated with the transaction, how those were determined, and over what time they will be realized?

A. As indicated in our press release announcing the transaction, the reduction in allocated expenses post-closing (due to our state-of-the-art systems infrastructure and lower overhead) is expected to result in operating efficiencies of $60 million to $75 million. We expect to be able to reduce expenses from the levels of Verizon's internal corporate allocations related but not limited to network monitoring, customer care, and back office support. I want to be clear that this does not mean that we intend to reduce personnel or resources committed to these critical functional areas. It merely means that we believe our in-region costs to run these operations will be less than Verizon's internal allocations for these services provided by operations located outside of the region.

PROPRIETARY.

Q. Are there offsetting expenses to these savings?

A. Yes, as described in more detail by other witnesses including Mr. Nixon and Mr. Haga, FairPoint will be establishing new work centers within the three states to perform functions that are provided currently by Verizon out-of-region. There will be initial set-up expenses associated with these new centers. However, we will be modernizing the systems infrastructure which will generate ongoing cost savings and efficiencies. In addition, we believe that these upfront expenses for state-of-the-art systems will generate significant improvements in the level of service for customers, and thus are expected to increase our attraction and retention of customers in the region.

RELATIONSHIP TO OTHER FAIRPOINT OR VERIZON ACTIVITIES

Q. Does this transaction impose any risks on current FairPoint customers, including those in Maine, New Hampshire, and Vermont?

A. We believe that our approach to this acquisition should minimize the risks to current FairPoint customers as well as to current Verizon customers. We plan to continue to operate the existing FairPoint companies as distinct operating companies, with separate regulatory accounting, from the new northern New England operations. Therefore, as we pursue the conversion to independent systems for the acquired properties, and as we operate under the Transition Services Agreement during that conversion, existing FairPoint customers will continue to be served separately by the systems and personnel that serve them today. After the conversion processes are complete, after the Transition Services Agreement with Verizon has been concluded, and after the new operations are up and running smoothly, it will make sense to explore ways to combine operations that benefit both existing and new FairPoint customers. Since our existing FairPoint operations are cost-based rate-of-return companies for regulatory accounting purposes, any savings resulting from such combination would ultimately benefit the rate payers. We are delaying any immediate combination of operations so that we can mitigate any risk from the transaction to the acquired or existing FairPoint customers.

Q. Please provide more detail about the operational, regulatory, and accounting relationship between the existing FairPoint and new companies.

A. Operationally, the existing FairPoint companies will be substantially separate from the newly acquired properties. As is explained in other testimony being filed today, around 3,000 Verizon employees will be retained by FairPoint as a result of this transaction, meaning the former Verizon properties in northern New England will be operated, on a day-to-day basis, by the same people. From a regulatory perspective, existing FairPoint will operate exactly as it does today. The acquired Spinco operations will operate as separate entities, with their own study areas, separate books of account, and separate tariffs from the existing FairPoint LECs.

Q. Please describe the Cost Allocation Manual (CAM) and why it is significant?

A. The CAM is the document under which we will ensure compliance with the FCC's cost allocation rules (47 C.F.R. Parts 32 and 64). Once this transaction closes, Verizon's current CAM will be adopted by FairPoint for the acquired properties. The CAM's cost allocation procedures will be continued under the transition services arrangement with Verizon. The importance of the CAM is that it allows us to document and control how costs are allocated between regulated and non-regulated operations, and among permitted regulated accounts. Since we are adopting Verizon's current CAM, we expect current cost allocation procedures to continue after the closing in the same fashion as prior to the closing.

Q. Please discuss management fees, including what they are, how they will be structured, and what accountability exists concerning them?

A. Management fees consist of charges for services performed by various FairPoint managers and entities for the operating subsidiaries. These services include executive management, accounting, financial reporting, CABS billing, risk management, and others. The costs related to the executive management team will be allocated between the existing companies and the former Verizon operations based upon relevant allocation factors. With the exception of the executive management team, management fees will be incurred separately for existing and acquired properties. A separate management group will be operating the former Verizon properties and their time and efforts will be limited to operating such properties, with the related costs exclusively allocated to such properties. The current services provided by various FairPoint managers and entities to the existing companies will continue to be provided to them, following current procedures, and the costs will be allocated to such companies without any allocation to the former Verizon properties. These costs will be allocated in accordance with the currently effective Management Services Agreement among the existing FairPoint companies and Management Services Allocation Manual.

Q. Will state regulators have access to books and records for the company?

A. Yes. Regulators in the three states will have full access to all the regulatory books of account and other financial records of FairPoint, as is now the case for FairPoint companies. We are always open to discuss with regulators how to accomplish improved accountability in the most efficient and satisfactory way possible.

Q. At some time in the future is it possible that certain functions of new and existing FairPoint operations will be combined?

A. Yes, to some degree. It does not make sense to do so initially for a number of reasons—most fundamentally in order to minimize risk either to existing FairPoint or current Verizon customers. After the processes described by Mr. Haga have been completed, after the Transition Services Agreement with Verizon has been concluded, and after the new operations are up and running smoothly, it will make sense to explore ways to combine some operations—such as back-office operations—if doing so would benefit both existing and new FairPoint customers. To be clear, we will not "combine" the price cap regulated company with the rate-of-return regulated companies, as these differently regulated entities will continue to keep separate books of account

Our past acquisitions have succeeded by drawing on the strengths and talents of the companies we acquire. For example, we have drawn on the talents of key people at all levels of the company from all over the country. We believe that our existing FairPoint employees have much to contribute to our efforts in northern New England, and our new employees in New England will have much to offer to our existing operations as well.

Q. Does FairPoint plan any future acquisitions?

A. FairPoint is and will continue to be a telephone acquisition and operating company. However, we are not considering any new transactions at this time, and do not anticipate entering into any further purchase arrangements before this transaction closes. While FairPoint's business model is focused on acquiring and upgrading telephone companies in, and providing advanced services to, small urban and more rural markets, we recognize the size, complexity and importance of the current transaction in northern New England. After we have completed the merger and successfully converted all systems and processes to the FairPoint platform, and are assured our customer service operations are at acceptable levels, we will then consider future acquisitions, because increasing scale and scope is important to continuing to provide efficient services to all our customers.

CONCLUSION

Q. How would you sum up the transaction from your perspective?

A. I believe this an important transaction not only for the companies involved and their investors, but also for the customers, employees, and communities of northern New England. This combination will bring the benefits of increased broadband availability and other investment to the economies of Maine, New Hampshire and Vermont. The transaction also will provide stability to existing Verizon employees in the region, with compensation and benefits commensurate with what they currently enjoy. In addition, new job opportunities will be created and employees will see additional opportunities for professional development. Finally, the transaction will create a financially strong company with a singular strategic focus of providing high-quality advanced communication services that meet the needs of consumers in northern New England at competitive prices. In summary, I believe that it is clear that this transaction is good for customers, employees, communities and our company and its shareholders.

Q. Does this conclude your testimony?

A. Yes.

ATTACHMENT WEL-1

****PROPRIETARY****