Verizon is Abandoning Rural America
The Proposed Frontier Purchase of Verizon's Properties
Would Place Consumers, Workers and Communities at Risk

Communications Workers of America

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Verizon has proposed selling its wireline, long distance and broadband assets in 14 states for $8.6 billion to Frontier. Frontier will give Verizon shareholders $5.3 billion in Frontier stock and give Verizon $3.3 billion in cash. The deal is structured to take advantage of a tax loophole so that Verizon will not have to pay any taxes on the $3.3 billion it gets. The proposed transaction must be approved by the Federal Communications Commission and the state utility commissions in ten states. There are significant questions concerning Frontier's capacity successfully to operate and fund a new company that is three times its size especially in West Virginia where new operating systems must be developed. Indeed, the sale poses significant risks to consumers, workers and the economic health of our communities. These risks overwhelm any supposed benefits from the deal.

Verizon has a bad track record with similar sales – just ask the consumers and regulators in Maine, New Hampshire, Vermont and Hawaii

- **FairPoint Communications, the company to which Verizon sold its Maine, New Hampshire and Vermont operations in 2008, is foundering as it tries to integrate operations and is choking on the debt it incurred to finance the transaction.** In 2008, Verizon sold its 1.5 million access lines in Maine, New Hampshire and Vermont to FairPoint. FairPoint has struggled to provide adequate service prompting an unprecedented number of complaints to state regulatory commissions from frustrated consumers. FairPoint's finances are also in disarray: FairPoint stated that it could be at risk of failing to meet an interest requirement on its debt. If this happens, bankruptcy could be an option. Since the deal was announced, FairPoint's stock price has declined by about 95%, and the company has been forced to suspend dividend payments.

- **Hawaiian Telcom, the company to which Verizon sold its Hawaii operations in 2005, filed for bankruptcy**. Verizon sold its 715,000 access lines in Hawaii. Since then, Hawaiian Telcom has experienced significant transition issues that resulted in major financial and customer service problems. In three years, the company lost 21% of its customers. In December 2008, Hawaiian Telcom filed for bankruptcy.

- **The yellow pages company that Verizon spun off also filed for bankruptcy**. In November 2006, Verizon spun off its yellow pages directory business to Verizon shareholders, loading the new company, Idearc, with about $9.5 billion in debt and extracting a cool $9 billion in cash and debt reduction. Last year, interest payments alone on Idearc's debt accounted for almost one-quarter of its total revenues! Representing something of a Verizon failing company "hat trick," Idearc filed for bankruptcy in March 2009.

Verizon's proposed sale to Frontier will put consumers, workers and communities at significant risk. The operations in the affected states will be financially weaker after the sale to Frontier than they are currently with Verizon. With significant increases in debt, and questionable savings, Frontier will not have the money to improve service quality or adequately expand high speed internet.

- **The mouse swallowing a cat.** If the transaction is approved, Frontier management will have to deal with a 300% increase in access lines (from 2.2 million access lines now to 7 million after the sale) and a 200% increase in employees (from 5,700 employees now to 16,700 after the sale).

- **High debt.** Frontier's debt will increase from \$4.55 billion to \$8 billion – an increase of over \$3.4 billion. Servicing this debt will mean less money for infrastructure, service quality, and high-speed internet build out.

- **The operations in the affected states will be financially weaker**. While Frontier argues that somehow this deal will make it stronger, the issue for the states being sold is *how much weaker it will make the operations in those states*. The leverage ratio is one way to measure the financial health of a company. The leverage ratio is calculated by taking net debt and dividing it by earnings (before interest, taxes, depreciation and amortization). The leverage ratio for the states being sold will increase from 1.7 immediately before the transaction closes to 2.6 after the sale.

- **Projected \$500 million expense savings are questionable**. The entire deal revolves around Frontier's ability to cut its operational expenses by \$500 million or 21%. This is significantly greater than the 8-10% cut that FairPoint hoped to achieve – and much of these savings were to be generated from replacing Verizon's network and back-office systems. Yet, Frontier states that all of the operations except for West Virginia will continue on Verizon's existing systems – for which Frontier will pay a fee. Where will Frontier generate the savings – from reduced service quality, workforce, or maintenance of the communications infrastructure?

- **Lack of any firm financial commitments.** In spite of brave talk from Verizon and Frontier, as recent events have demonstrated, obtaining financing for a transaction this size can be difficult. Frontier does not currently have financing for the additional debt it will take on for this transaction.

Frontier's ability to provide truly high-speed internet to its newly acquired customers is questionable. High speed broadband is now an economic necessity enabling such activities as economic development, telemedicine, e-commerce and interactive distance learning. These benefits can only be realized fully with truly high-speed internet access. Speed Matters on the Internet. However, the operations that Verizon is selling are woefully lacking in slow copper based technologies such as DSL, much less high-capacity fiber networks. Fiber networks enable speeds up to 100 megabits per second (mbps) while DSL typically enables just 1.5 to 6 mbps. The Frontier transaction will not bring our states any closer to the high speeds needed to take full advantage of the telecommunications super highway.

- **Verizon's high-speed fiber to the premises (FiOS) is available to 600,000 residential and small business customers – what will happen to them?** Verizon's former Verizon FiOS customers in New Hampshire may lose their high speed internet because investment funds are being used to pay back loans, not make investments

- **Will Frontier be able to invest in high speed fiber to the premises?** Frontier faces significant challenges with debt and running a significantly larger company in the wake of a major recession. Where will it get the money to invest in high speed fiber?

- **Frontier has NOT yet made any commitments to deploy the fiber needed to enable truly high-speed internet access**.

West Virginia is especially vulnerable

- **Verizon had already committed to increase fiber investment throughout West Virginia**. Given Frontier's high debt load and potential problems with integrating West Virginia into new systems, Frontier's ability to build high speed internet is questionable.

- **There is a significant risk that Frontier will run into delays and cost overruns when it replaces Verizon's operational, support and administrative systems** Frontier will have to replace all of Verizon's operational and back office systems with new systems, *on the day the deal closes*. This is a daunting task that led to disasters in Maine, New Hampshire, Vermont and Hawaii, which didn't even attempt the day one cutover of operational and back office systems that Frontier says it will undertake in West Virginia.

The Bottom Line: The risks posed by the sale to Frontier vastly outweigh any supposed benefits

Frontier promises to increase capital expenditures; improve service quality; significantly expand broadband availability; provide wholesale services to Competitive Local Exchange Carriers; and do it all right away at significantly less cost than one of the largest and most experienced telecom companies in the world. Frontier basically says to trust them – they can do it all and satisfy everyone. However, Frontier will not have the resources to do it all.

- **Consumers, workers and communities will bear the risks of this transaction.** Traditionally, when companies run into problems they cut capital expenditures, lay off workers and attempt to increase rates. Consumers risk higher rates and/or worse service. Workers risk lost jobs, benefits and job security. Communities risk worse service quality, less ability to respond to emergencies, and less build out of the high speed Internet needed for development.

- **The Frontier option could be much worse than the Verizon option.** While Verizon has had problems with service quality and build out – it at least has the deep pockets and vast operational resources needed to improve service, build out high speed infrastructure and sustain its operations over the long term amid economic dips and natural emergencies. Frontier will have much fewer resources and no margin for error to sustain on-going operations, much less address emergencies or greater than expected line losses.

- **Just ask the consumers in Maine, New Hampshire, Vermont and Hawaii if they are better off now than when Verizon ran their telecom operations.**

- **Frontier's chief executive will not face any risks – and has been richly rewarded even though Frontier's stock has significantly decreased.** In two years, the annual compensation of Frontier's CEO, Maggie Wilderotter, increased by 131% (from $2.36 million in 2006 to $5.45 million in 2008) even though total shareholder return decreased by 24% in 2008 after having decreased by 5% in 2007.

Verizon will avoid paying any taxes on the $3.3 billion it will get from Frontier by using a tax loophole

- **Verizon will avoid paying taxes on $3.3 billion by using a tax loophole** called a Reverse Morris Trust (RMT). This is "loophole" allows businesses to reorganize and sell assets without having to pay taxes. Thus, taxpayers are subsidizing this transaction at a time when money is needed to expand broadband and expand jobs.

- **Verizon only picked Frontier in order to qualify for the tax loophole.** Verizon could only obtain "tax free" treatment by selling its operations to a smaller company – no matter the consequences to consumers, workers or communities.

Don't Let Verizon off the hook!

- **Don't let Verizon make billions by abandoning millions of consumers and thousands of workers**. For over a hundred years, ratepayers have generated billions upon billions of dollars that allowed the phone company to prosper. Now Verizon will abandon them, dump billions of dollars of debt onto a financially weaker Frontier and get subsidized to do it. Verizon could clearly afford to make such investments, but it has chosen not to do so. The company should meet all of its commitments and regulatory requirements for investment, public safety and service quality before it should be allowed to sell – especially since the prospective buyer in this case does not appear to have the resources to meet Verizon's commitments.

- **Verizon is keeping the lucrative wireless spectrum it was awarded for free because it owned the landlines in their service area**. This spectrum is very valuable and Verizon should reimburse the communities it is abandoning.

- **Stop the Sale**. State regulatory commissions in Maine, New Hampshire, Vermont and Hawaii approved the sale of Verizon's operations with numerous conditions that they thought would protect FairPoint and Hawaiian Telcom financially and protect consumers. They were wrong. Indeed, FairPoint has run into significant problems even after the regulatory commissions required Verizon to reduce the price of the transaction by more than $300 million and required FairPoint to reduce its dividends and increase its infrastructure investment by millions of dollars. But forcing Verizon to leave more funds with the states it is abandoning is not enough. It must be told that it can't shed operations like an old pair of shoes. It's time to Stop the Sale completely.

WHAT YOU CAN DO

- **Who is impacted**? Verizon's proposed sale to Frontier directly impacts the residents of Arizona, Idaho, Illinois, Indiana, Michigan, Nevada, North Carolina, Ohio, Oregon, South Carolina, Washington, West Virginia and Wisconsin. However, the ability of people everywhere to communicate effectively is adversely affected when significant telecommunications providers like Frontier (and FairPoint and Hawaiian Telcom) overreach, become financially challenged and cut back on needed services and the expansion of high-speed internet.

- **Regulatory approvals required**. The transaction must obtain the approval of the Federal Communications Commission and ten state regulatory agencies, including West Virginia, Illinois, Ohio, Washington, Oregon and, possibly, Pennsylvania.

Contact your elected officials at the state, local and federal levels expressing your opposition to this tax subsidized scheme that foists substantial risks onto consumers, workers and communities.