WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION STAFF
RESPONSES TO DATA REQUEST

DATE PREPARED: January 7, 2010
DOCKET: UT-090842
REQUESTER: Public Counsel

WITNESS: William H. Weinman
RESPONDER: William H. Weinman
TELEPHONE: (360) 664-1109

REQUEST NO. 7: Please reference the Testimony in Support of Settlement Agreement of William H. Weinman, Exhibit No. ___ (WHW-6T), p. 5, ll. 13-15.

Please explain with specificity how the Settlement Agreement addresses each of the following issues that were raised by Mr. Weinman in his November 3, 2009 direct testimony, Exhibit No.___ (WHW-1T), pp. 5-6:

a. Verizon has a broader product line that helps offset the Washington access line loss.
b. Data requests responses from Frontier show that the Company has not done enough to investigate the condition of the plant it is acquiring or to determine whether its own projections are realistic given the many risks the Company identifies.
c. The merger agreement requires Frontier to issue additional equity if regulatory agencies require additional expenditures by Verizon as a condition of merger approval.
d. Frontier will be constrained from offering equity placements for two years after the close date of the transaction.
e. Frontier is declaring and paying dividends that exceed earnings per share.
f. Risk factors disclosed by Frontier indicate there are substantial issues that could affect the results of Frontier's projected financial results from the merger.
g. Frontier is not able to give adequate interest rate cost estimates of the additional debt ($3.3 billion) needed to be issued by Frontier to make the special cash payment to Verizon.
h. Frontier is not able to articulate the debt covenants that would be required to issue $3.3 billion dollars in debt.
i. Merger synergies will not provide any benefit to Washington customers.

RESPONSE:

a. Verizon does have a broader product line that could help offset Washington access line losses. However, the wireless product line does not add value to the wireline business and Verizon appears to have little strategic will to invest in wireline broadband, which does add value to the wireline business. Verizon's witness, Mr. McCallion indicates the Company is not inclined to continue deploying broadband services to customers in its rural exchanges. The provision of normal voice grade telecommunications services will result in continued loss of customers, which will ultimately degrade economies of scope and scale to Washington customers.

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Frontier, like CenturyLink, has approximately 92 percent broadband availability to its existing customers in other states. The Company has made a substantial financial and operational commitment in the settlement to bring broadband availability to approximately 90 percent in Washington over the next four years.

b. Since that time, the rebuttal testimony, clarification of the replication process and the conditions of the settlement agreements have made it clear that Frontier has performed the necessary activities to eliminate that issue.

c. There have not been onerous regulatory provisions placed on Verizon that make additional equity issuance an issue.

d. Frontier witness, Mr. Whitehouse, has indicated in his rebuttal testimony that Frontier can issue additional equity and not violate the conditions of the Reverse Morris Trust.

e. Frontier is paying dividends that exceed earnings per share. As Mr. Whitehouse has stated in his rebuttal testimony, dividend payments can be reduced if the Company needs to retain cash. Staff believes the Company can maintain its dividend payout amount without jeopardizing the Company's financial integrity. Staff is also aware that need for capital expenditures can be reduced because the FiOS build out is approximately 90 percent complete, the reduction in customers will recover outside plant cable pairs and prices for central office switching have been declining.

f. The substantial risk factors that caused Staff the most concern pertained to financial and replication of the Operational Support Systems (OSS) data base. Those concerns have been resolved with additional data and the conditions agreed to in the settlement.

g. Staff's analysis has determined that Frontier can succeed if the debt interest rate is 9.5 percent. There is a clause in the agreement allowing Frontier to terminate the merger if the Company would incur a higher interest rate than 9.5 percent. Finally, Frontier has been able to refinance its existing debt with interest rates less than 8.5 percent.

h. The settlement agreement has a condition that will not allow Frontier to encumber assets of Frontier NW, the operating company.

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i. While Staff still believes merger synergies will not provide benefits to Washington customers (when comparing Verizon on a total company basis to Frontier on a total, combined company basis), the deployment of broadband facilities will provide a substantial benefit to customers. On the other hand, Staff also believes that the rapid loss of access lines experienced by Verizon would also increase costs to remaining Washington customers over time if the transfer of control is not approved by the Commission. Frontier is likely to do a better job of stemming this loss than Verizon. If it turns out that Frontier does experience synergies that result in reduced costs for Washington operations, the settlement requires the reporting of such synergies, and the residential rate cap prevents the Company from seeking a rate increase until such time as those synergies are likely to be realized (and to meet the known and measureable standard for ratemaking or for design of an AFOR plan).