EXHIBIT BGJ-1T

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Application of QWEST CORPORATION Regarding the Sale and Transfer of Qwest Dex to Dex Holdings, LLC, a non-affiliate	Docket No. UT-021120

DIRECT TESTIMONY

OF

BRIAN G. JOHNSON

QWEST CORPORATION

JANUARY 17, 2003

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1 ## I. IDENTIFICATION OF WITNESS

2 **Q. PLEASE STATE YOUR NAME, ADDRESS AND EMPLOYMENT.**

3 A. My name is Brian G. Johnson. My business address is 7074 Rocky Point Road, Polson,
4 Montana, 59860. Qwest has retained me as a consultant to assist in the regulatory
5 process related to the sale of the Qwest Dex, Inc. ("Dex") directory publishing assets and
6 business. I am submitting this testimony in support of Qwest Corporation's ("QC")
7 application in this matter.

8 **Q. PLEASE REVIEW YOUR WORK EXPERIENCE AND EDUCATION.**

9 A. From 1970 to 1999, I was employed by QC's predecessors: The Mountain States
10 Telephone and Telegraph Company, and U S WEST Communications, Inc. Throughout
11 my 29 years with these companies, I served in various capacities including Assistant
12 Treasurer, State Regulatory Director for the state of Colorado, and Executive Director of
13 Corporate Public Policy.

14 As Assistant Treasurer, I was responsible for overseeing the financing for the Mountain
15 States Telephone and Telegraph Company. As a result, I am familiar with financial
16 filings, documents, terms, practices and policies. As the Colorado State Regulatory
17 Director, I was responsible for numerous regulatory and legislative issues, including rate
18 cases and alternative forms of regulation filings, tariff filings, depreciation cases, and
19 rulemakings. My role as Executive Director of Corporate Public Policy required me to
20 develop strategy and company policy, as well as serve as the company spokesperson for
21 these policies before individual commissions and the Regional Oversight Committee.
22 Part of my responsibilities included the oversight of regulatory issues associated with

1 retail product and marketing initiatives, including all aspects of rate cases. I am familiar
2 with the history of Dex and its predecessors, and with the interrelationships between Dex
3 and the regulated local exchange provider, today known as QC.

4 I summarize my education and work experience in Exhibit BGJ-2.

5 **II. PURPOSE OF TESTIMONY**

6 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS DOCKET?**
7 A. My testimony is filed in tandem with that of Peter C. Cummings. The purpose of our
8 testimony is to explain why the sale of Dex is critical to the continued financial viability
9 of QC, and Qwest Communications International Inc. ("QCI"), QC's ultimate parent
10 corporation. Mr. Cummings and I focus on the months prior to the announcement of the
11 Dex sale transaction, conditions leading up to the decision to sell Dex, and the
12 significance of the closing of the transaction. In so doing, our testimonies demonstrate
13 that the sale of Dex is in the public interest.

14 Mr. Cummings' testimony focuses on Qwest's[1] historical situation, and current financial
15 obligations and challenges. My testimony touches on those same subjects, but focuses to
16 a greater extent on Qwest's strategic goals and the options Qwest evaluated and pursued
17 to address its financial difficulties.

[1] When the term Qwest is used it refers to the global group of Qwest entities and not specifically to the parent corporation or an individual entity.

1 **Q. WHAT ISSUES WILL YOU ADDRESS IN YOUR TESTIMONY?**

2 A. My testimony addresses the following issues:

3 Section III: Following on Mr. Cummings' general description of QCI and QC financing
4 and discussion of the numerous events leading to concerns about QCI's liquidity and its
5 ability to service its debt, I discuss QCI's decision to sell Dex. With QCI's heavy debt
6 load and significant liquidity issues, the specter of bankruptcy was very much a reality.
7 The options available to QCI were extremely limited, but I explain what they were and
8 why QCI chose to sell Dex. I also explain the critical role of the Dex transaction in
9 facilitating the renegotiation of QCI's syndicated credit facility, without which QCI likely
10 would have defaulted on covenants relating to QCI's debt to EBITDA (earnings before
11 interest, taxes, depreciation and amortization) ratio, leading to a possible bankruptcy.

12 Section IV: I provide a high level summary of the Dex sale transaction, and discuss the
13 decision to complete the sale in two phases. I discuss the critical need to close both
14 phases of the sale transaction, as well as the intended uses of the proceeds from the
15 transaction.

16 Section V: I conclude my testimony by demonstrating that the Dex sale transaction is in
17 the public interest, from the perspective of the financial well-being of both QCI and QC,
18 and recommending that this Commission approve the transaction on an expeditious basis.

1 **III. THE DECISION TO SELL DEX**

2 **Q. WHAT IS THE SIGNIFICANCE OF QWEST' S FINANCIAL DOWNTURNS**
3 **IN 2002?**

4 A. As Mr. Cummings describes more fully in his testimony, by 2002 QCI was in a situation
5 where it needed to improve liquidity and reduce debt, and it needed to do so quickly. In
6 the Amended Credit Facility, QCI had been able to marginally improve the covenants
7 relating to its debt to EBITDA ratios. Continuing declining EBITDA, however, made it
8 very possible that QCI would soon be in violation of those covenants, even with the
9 slightly relaxed debt to EBITDA ratio requirements.

10 Further, QCI had ever dwindling options to raise cash necessary to make upcoming
11 required payments under the Amended Credit Facility in 2003. QCI was required to
12 repay its full borrowing under that facility, $3.4 billion, in May 2003. QC also had $1.1
13 billion of other debt maturing by June 2003. QCI and QC were locked out of the
14 commercial paper market. Their ability to issue intermediate and long term debt was
15 increasingly hampered by the decline, ultimately into junk status, of their credit ratings.
16 Even had they been able to issue replacement debt, it would likely have been on much
17 more onerous terms, given their credit ratings, and it would not have reduced the risk
18 associated with the debt to EBITDA ratio covenants. QCI's dwindling stock price made
19 a public stock issue impractical; the SEC investigation made a public stock issue
20 impossible. By April 2002, having explored numerous options, QCI decided to move
21 ahead with a possible sale of Dex, and solicited proposals from potential purchasers.

1 **Q. WHAT WERE THE DIFFERENT OPTIONS AVAILABLE TO QCI TO RAISE**
2 **CASH TO IMPROVE ITS LIQUIDITY AND REDUCE ITS DEBT LOAD?**
3 A. Increased revenue from internal operations was not an option, due to declining demand
4 for telecommunications products and services, decreasing sales in the context of high
5 fixed costs, increased competition and loss of access lines, and excess capacity in the
6 fiber market.

7 Further reducing operational expenses was also not a viable option to significantly
8 increase cash flow. QCI had already reduced its employee levels and expenses
9 significantly in 2001, and continued to reduce expenses in 2002. The additional
10 reductions could help improve cash flow and free cash flow, but not nearly to the degree
11 necessary to meet maturing debt obligations.

12 Issuing additional equity or debt also proved infeasible. QCI did file an S-3 Registration
13 Statement with the SEC on February 5, 2002 for issue of up to $2.5 billion of common
14 stock or debt securities. However, the SEC investigation initiated on March 11, 2002
15 precluded any public stock sale. In any event, the severe drop in QCI's stock price made
16 a stock issue impractical. The declining bond ratings of both QCI and QC and the severe
17 drop in market prices for the company's bonds made further debt offerings equally
18 impractical.

19 The other option to raise sufficient cash was a potential sale of assets, including the
20 wireless business, wireless towers, access lines, or Dex. The sale of wireless assets could
21 raise cash quickly, but not in sufficient amounts to satisfy QCI's short- and intermediate-

1 term cash needs. Access line sales could raise sufficient cash, but would likely require
2 several years to complete, based on QC's past experience.

3 QCI determined that the sale of Dex was the most promising and appropriate strategy for
4 raising necessary cash on a short timeline. The sale of Dex would also provide enough
5 proceeds to perhaps persuade the bank members of the Amended Credit Facility to
6 negotiate an extension of the repayment dates and further relax the debt to EBITDA ratio
7 covenants, which was an equally important consideration. After significant due diligence
8 by potential purchasers and negotiations with potential purchasers, QCI reached an
9 agreement on August 19, 2002 to sell Dex. I further describe the sale transaction in
10 Section IV of my testimony.

11 **Q. YOU STATED THAT THE DEX SALE WAS IMPORTANT TO QCI' S**
12 **EFFORTS TO FURTHER AMEND ITS AMENDED CREDIT FACILITY. WHY**
13 **WOULD THIS BE NECESSARY, GIVEN THAT QCI HAD JUST NEGOTIATED**
14 **AN AMENDMENT IN MARCH 2002?**

15 A. QCI's continued declining EBITDA and lack of cash to reduce its $26 billion debt load
16 still left QCI in jeopardy of violating its debt-to-EBITDA ratio covenants even though
17 these had been slightly relaxed by in the Amended Credit Facility . In fact, by August 19,
18 2002, QCI had disclosed that, unless it was able to renegotiate the Amended Credit
19 Facility or obtain waivers from the banks relating to the debt-to-EBITDA ratio covenants,
20 it would be in violation of those covenants, and therefore in default by the end of the third
21 quarter, 2002.[2] In addition, the entire $3.4 billion indebtedness under the Amended

[2] "Based on our expectations for the remainder of 2002, we must complete the amendment of the syndicated credit facility or obtain waivers from the banks prior to September 30, 2002. Unless we accomplish one of these alternatives, we anticipate we will fail to satisfy the financial covenants under the syndicated credit facility as of the end of the third quarter." QCI Form 8-K, Aug. 19, 2002.

1 Credit Facility was coming due in May 2003, and QC also had $1.1 billion of other debt
2 maturing by June 2003. There was simply insufficient cash to meet these obligations
3 when they came due, necessitating an extension of the maturity date under the Amended
4 Credit Facility.

5 **Q. WAS QCI ABLE TO NEGOTIATE FURTHER AMENDMENTS TO THE**
6 **AMENDED CREDIT FACILITY?**

7 A. Yes. As discussed in greater detail by Mr. Cummings, the resulting credit agreement is
8 referred to as the Second Amended and Restated Credit Agreement ("ARCA"), which
9 QCI announced on September 4, 2002.[3] QCI also negotiated a $750 million term loan
10 (the "Dex Term Loan"), due in full upon completion of the second phase of the Dex sale
11 transaction, expected in 2003, but in no event later than September 2004.

12 **Q. WHAT WOULD HAVE HAPPENED HAD QCI NOT BEEN ABLE TO**
13 **NEGOTIATE THE ARCA?**

14 A. Absent a renegotiation of the Amended Credit Facility or a waiver relating to the debt-to-
15 EBITDA ratio covenants, QCI would have violated those covenants by the end of the
16 third quarter, 2002.[4] This would have put QCI in default under the terms of the Amended
17 Credit Facility, which likely would have driven QCI into bankruptcy. Setting aside the
18 issue of these financial covenants, QCI would almost certainly have lacked sufficient
19 cash to make the $3.4 billion payment on the Amended Credit Facility required in May
20 2003. Again, this could have potentially driven QCI into bankruptcy. Bankruptcy,
21 however, is not a business plan, and QCI had no intention of pursuing that option until

[3] "On September 4, 2002 Qwest Communications International Inc. ("Qwest") announced that it had reached unanimous agreement with the 29 lenders in its syndicated credit facility to amend Qwest's $3.4 billion credit facility. " QCI Form 8-K, Sept. 5, 2002.

[4] QCI Form 8-K, Aug. 19, 2002.

1 and unless it exhausted all other alternatives. Accordingly, QCI continued to move
2 forward with its plan to sell Dex and renegotiate the Amended Credit Facility.

3 **Q. WOULD QCI HAVE BEEN ABLE TO NEGOTIATE THE ARCA ABSENT THE**
4 **DEX SALE TRANSACTION?**

5 A. No. The Dex sale effectively facilitated QCI's ability to negotiate the terms and
6 conditions in the ARCA. The banks recognized that, absent the sale of Dex, QCI had
7 insufficient cash to make the $3.4 billion payment that would have been due on May 3,
8 2003. The ARCA requires interim payments in the event of asset sales, specifically
9 including the sale of Dex. In particular, the close of the Dexter phase of the Dex sale
10 transaction required a $1.354 billion pay down of the ARCA, and the close of the Rodney
11 phase of the Dex sale transaction requires a further $750 million pay down of the ARCA.
12 In addition, QCI is required to fully pay the $750 million Dex Term Loan upon the close
13 of Rodney. Providing for these interim pay downs of QCI's $3.4 billion indebtedness,
14 using Dex sale proceeds, was critical to QCI's ability to negotiate relaxed financial
15 covenants and an extension in the maturity date to May 3, 2005. Absent the Dex sale
16 agreement, it is very unlikely that QCI would have been able to negotiate the ARCA,
17 which, as I previously described was absolutely critical to avoiding bankruptcy

18 **IV. DEX SALE TRANSACTION**

19 **Q. PLEASE REVIEW THE MAJOR ASPECTS OF THE DEX SALE**
20 **TRANSACTION.**

21 A. On August 19, 2002, QCI reached an agreement to sell Dex for $7.05 billion to a new
22 entity ("Buyer") formed by a consortium of private equity firms, including The Carlyle

1 Group and Welsh, Carson, Anderson & Stowe. The sale is in two stages. The first stage
2 (Dexter) included Dex operations in Colorado, Iowa, Minnesota, Nebraska, New Mexico,
3 North Dakota and South Dakota, and closed on November 8, 2002. The second stage
4 (Rodney) includes Dex operations in Arizona, Idaho, Montana, Oregon, Utah,
5 Washington and Wyoming, and is expected to close in 2003.

6 **Q. WHY WAS THE SALE TRANSACTION STRUCTURED TO CLOSE IN TWO**
7 **PHASES?**

8 A. The primary reason for a two-phased transaction was the need to quickly improve QCI's
9 financial condition with an infusion of cash. QCI's $3.4 billion Amended Credit Facility
10 was coming due in May 2003. As Mr. Cummings' debt maturity charts show, QC also
11 had $1.155 billion of debt maturing by June 2003. There was a concern about the ability
12 to close the entire transaction in time to meet these repayment needs, because of the
13 belief that some states, including Washington, would likely require a regulatory review of
14 the transaction and such a review might not be completed in the necessary timeframe. A
15 staged close would also allow Buyer to acquire a portion of the Dex operations and begin
16 business sooner, recognizing that the regulatory process in certain Rodney states could
17 delay the ability to close in those states.

18 **Q. HOW WAS THE DEX SALE ARRANGED?**

19 A. Qwest solicited potential purchasers for Dex worldwide from April to July 2002 and
20 conducted a rigorous and widely-publicized auction for Dex in July and August 2002 to
21 elicit the highest price for the asset. Qwest then received two fairness opinions with
22 respect to the transaction from its respected financial advisors for the transaction to the
23 effect that, subject to the assumptions, qualifications and terms contained in those

1 opinions, the consideration to be received by Qwest in the transaction is fair to the
2 Company from a financial point of view.

3 **Q. WITH THE NEGOTIATION OF ARCA AND THE CLOSING OF DEXTER, IS**
4 **THERE STILL A NEED TO COMPLETE THE RODNEY PHASE OF THE**
5 **TRANSACTION?**

6 A. Yes. Unless QCI completes the Rodney portion of the Dex sale transaction, it will be in
7 great jeopardy of not being able to pay off its maturing debt. A portion of the Dexter
8 proceeds have been used to pay the first installment of the ARCA loan, reducing QCI's
9 indebtedness under the ARCA from $3.4 billion to $2.0 billion. See Mr. Cummings' debt
10 maturity charts. However, QCI's financial position remains precarious. Without the
11 proceeds from the second phase of the Dex sale, the only other source of cash is cash
12 flow from internal operations. Even if it were to drastically reduce its capital budgets and
13 operating expenditures, QCI would likely have insufficient cash from internal operations
14 to meet upcoming ARCA payments and long-term debt maturities.

15 After the recent closing of the Dexter phase of the transaction, Standard and Poor's
16 commented to the same effect:

> 17 [T]he company still faces the challenge of obtaining state regulatory
> 18 approvals for the close of the western region, and the close of this $4.3
> 19 billion transaction is expected to occur in 2003. These additional proceeds
> 20 are critical in enabling the company to meet upcoming maturities both on
> 21 the bank and public debt, which total about $7 billion from 2003 through
> 22 2005, of which about $4.8 billion is due through 2004, after the $1.4 billion
> 23 pay-down of the $3.4 billion bank loan.[5]

[5] Standard and Poor's Press Release, November 12, 2002. See Exhibit PCC-6.

1 **Q. DID THE DECEMBER 2002 PRIVATE DEBT EXCHANGE ALLEVIATE**
2 **ENOUGH FINANCIAL PRESSURE TO ALLOW QCI TO MEET ITS**
3 **REPAYMENT OBLIGATIONS AND SURVIVE WITHOUT THE CLOSING OF**
4 **RODNEY?**
5 A. It did not. While QCI was pleased that a portion of eligible bondholders took advantage
6 of the exchange offer, the results of the offer have no significant bearing on most of
7 QCI's and QC's repayment obligations. As Mr. Cummings' Table B shows, QCI and its
8 subsidiaries still must make debt maturity payments of over $6.5 billion over the next
9 three years and over $8.5 billion over the next five years. The Rodney proceeds are still
10 vitally needed for QCI and its subsidiaries to avoid defaulting under their obligations.

11 **V. THE SALE OF DEX IS IN THE PUBLIC INTEREST**

12 **Q. DESCRIBE WHY YOU BELIEVE THE SALE OF DEX IS IN THE PUBLIC**
13 **INTEREST.**
14 A. The sale of Dex is in the public interest because it goes a long way toward improving
15 QCI's financial stability over the next several years, addressing critical liquidity
16 concerns, and allowing QCI time to execute on its business plan. With the completion of
17 the sale of Dex, QCI can focus on core telecommunications services and continue to
18 maintain high levels of service quality. The sale of Dex averts what most considered a
19 pending bankruptcy, which otherwise would have been a "lose-lose" solution for
20 customers, employees and shareholders of the Qwest family of companies. On this
21 basis, I believe that, if the Commission finds that it is required to approve this transaction,
22 it should do so as expeditiously as possible consistent with the public interest. Time is of
23 the essence to the parties in completing the transaction.

1 **Q. ARE THERE ANY OTHER FACTORS THE COMMISSION SHOULD**
2 **CONSIDER IN MAKING A PUBLIC INTEREST DETERMINATION?**
3 A. Yes, there are. Earlier in my testimony I mentioned the issue of bankruptcy. The
4 Commission should be concerned about this issue, and should conclude that to the extent
5 that the Dex transactions reduce the possibility of such a filing, that factor weighs heavily
6 in favor of a finding that the transactions are in the public interest.

7 **Q. IF QCI, BUT NOT QC, WERE TO FILE FOR BANKRUPTCY, WHY SHOULD**
8 **THE COMMISSION BE CONCERNED?**
9 A. Such a filing could be disruptive for all the companies in the Qwest family of companies,
10 for the employees of all of those companies, for the people who rely on those companies,
11 and, potentially, for the service provided by some or all of those companies.
12 Additionally, the Commission should be concerned because QCI is the parent company
13 for both QC and Dex. Thus, even if QC were not the party directly seeking bankruptcy
14 protection, QC and Dex, and their operations, would be subject to the jurisdiction of the
15 bankruptcy court. They would be assets of QCI, and as such could be sold or otherwise
16 disposed of to satisfy the interests of the creditors of QCI. Under those circumstances, I
17 am advised that the bankruptcy court and the trustee in bankruptcy would not give much,
18 if any, consideration to ratepayer interests in connection with the disposition of the
19 proceeds from any such sale.

20 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**
21 A. The Dex sale is a critical component of QCI's financial viability over the next few years.
22 QCI needs the proceeds from the sale to provide enough cash to pay down maturing debts
23 and continue operations over the next several years. Failure to rectify QCI's precarious

1 financial position would have serious impacts on QC to the detriment of its customers,
2 shareholders and employees.